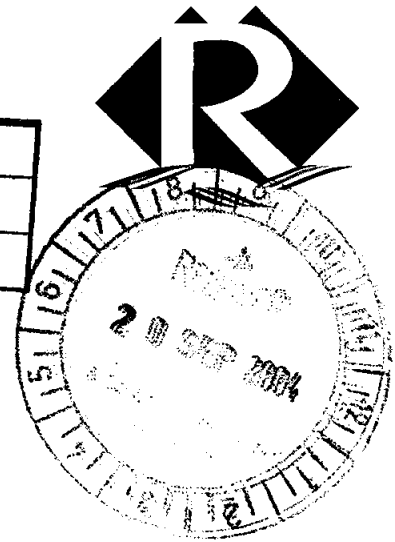


Our Ref:
Your Ref:
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14 September 2004

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

FILE No:
DOC: D04/45325
MARS/PRISM:



Dear Ms Arblaster

**AIRSERVICES AUSTRALIA LONGER TERM PRICING PROPOSAL - ACCC
ISSUES PAPER**

We refer to your letter of 17 August 2004 enclosing a copy of the ACCC's issues paper regarding Airservices Australia's (AsA) proposed 5-year price plan for Aviation Rescue Fire Fighting (ARFF) and Air Traffic Control (ATC) services.

Overview

Rockhampton City Council is the owner and operator of Rockhampton Airport. In recognising its geographic location in relation to Central Queensland, it has endeavoured to provide affordable air transport facilities that are not only compatible with user's expectations, but also capable of encouraging greater utilisation.

Expansion works carried out in the 1990's provided the airport with the capability of facilitating all categories of commercial and military aircraft. If the potential of the region is to be realised for the benefit of all, Rockhampton requires the services of a stable and growing airline industry.

We will attempt to address the following Issues for Comment as defined in your letter:

Long term pricing plan

Consultation process
Risk sharing arrangements

Structure of prices

Method of allocation of indirect costs
Pricing across services and user groups

Operating costs

Capital expenditure

Impact on users

Activity forecasts

Long Term Pricing Plan

Consultation Process

From our experience, the consultation process with airports was very limited in its scope and expectations. To date we have not received any answers to the questions we raised during the consultation meeting or in the subsequent feedback letter.

AsA's decision not consult with Airports in the first round of proposed price increases in 2003, would indicate that it does not consider the Airports to be valid customers. It would also appear that AsA considers their services are being provided for and managed on behalf of, airlines and aircraft operators.

It is our assertion that AsA should be viewed as a (Government mandated monopoly) supplier of services to airports and as such, should be managed similarly to any another part of the airport business (i.e. electrical & water supply, security, passenger screening, retail or ground handling services). It is with this perspective of the client / customer relationship that we find Airservices Australia's lack of customer involvement difficult to comprehend.

Risk Sharing Arrangements

To date we have not received any proposed risk sharing offers, either related to capital expenditure or operational expense from Airservices Australia.

We have made a verbal offer to enter into a risk sharing relationship in relation to capital expenditure. Though the initial response was negative, through a meeting with AsA representatives at the recent AsA "Waypoint 2004" conference, we may now be able to progress this proposal.

Operating costs

Capital expenditure

With reference to the enclosed Profit & Loss (P&L) statements for Rockhampton Airport ATC & ARFF, it has been difficult to discover the reasoning for the level of capital expenditure. The following issues highlight our concern over the proposed expenditure:

ARFF – as AsA has chosen not to include capital expenditure in the P&L statements for ARFF, it is very difficult to determine what AsA is intending to spend on ARFF services at our airport. We have received verbal advice that AsA is intending to commit to significant capital works in the proposed construction of a new ARFF building (and possible ATC Tower in the same structure), though details of the scope of the project have not yet been disclosed to our satisfaction.

ATC – there have been several changes in the Major Investments Planned from the original released P&L for ATC at our airport. In the revised P&L submission to the ACC, ATC services at Rockhampton Airport are estimated to expend an additional \$850,000 over 5 years. In the past few weeks we have established that two (2) of our current navigation aids will be replaced and funded by the ATC business unit.

Activity forecasts

From the information provided in the ATC & ARFF P&L statements, it is clear that AsA's figures for tonnes landed at Rockhampton Airport do not correlate with the Airport Management's figures. Though a portion of this can be explained through the hours of operation of ARFF & ATC versus the 24hour nature of airport operations, we currently receive all landing data from AsA; therefore we are actually comparing statistics derived from the same dataset.

We assume that the primary difference in landed tonnes is in relation to military services operating at our airport, though we have not included proposed large military exercises in our traffic forecasts.

As AsA's growth estimates for Rockhampton Airport are directly related to the per-tonne charge for their services, it is critical that these figures are as realistic as possible. To date we have not received any request from AsA for information regarding our figures or future estimates.

	Year								
	00/01	01/02	02/03	03/04	04/05	05/06	06/07	07/08	08/09
	Actual	Actual	Actual	Actual	Forecast	Forecast	Forecast	Forecast	Forecast
AsA figures for ARFF ('1,000 tonnes)									
	137	101	124	158	163	167	171	173	175
AsA figures ATC ('1,000 tonnes)									
	146	107	131	168	173	177	181	184	186
Rockhampton Airport Figures ('1,000 tonnes)									
	171	126	159	177	185	195	200	205	208
Difference ('1,000 tonnes)									
ARFF	34	25	35	19	22	28	29	32	33
ATC	25	19	28	9	12	18	19	21	22

Structure of prices

Method of Allocation of Indirect Costs

It has been noted that for ATC services, AsA proposes to charge \$4.40 per tonne at Townsville and \$3.10 per tonne to land at Darwin Airport. The respective P&L statements indicated zero (0) staff employed at these locations. If there is currently no ATC staff employed at these airports, how is AsA able to levy an ATC service charge?

It is assumed that these charges are used to recover other AsA infrastructure costs, primarily navigation facilities. If this is correct, we are unable to determine why AsA doesn't levy ATC charges for other airports that make use of their navigation facilities. For example; Proserpine Airport has three (3) navigation aids (VOR, DME and NDB) servicing several instrument approaches to this airport, yet an ATC charge is not levied on aircraft operating from this airport.

Rockhampton Airport is serviced by identical navigation aids, yet aircraft operators (and indirectly passengers) are expected to subsidise the upgrade of the VOR and DME at a cost of \$780,000 (\$156,000 over 5 years).

AsA has indicated in its submission to the ACCC¹ that one of the reasons for the prices changes is to “*Reduce cross-subsidisation between service lines*”. The above examples clearly demonstrate that AsA is funding the maintenance and replacement of navigation aids at several airports by some form of cross-subsidisation, though this has not been specified in their submission.

Pricing Across Services and User Groups

The Australian Defence Force (ADF) currently provides ATC & ARFF services at Newcastle Airport. As a result of the lack of a charging regime for these services, commercial advantage is given to domestic aircraft servicing this port. Based on the Australian average cost of ATC & ARFF services², the saving is in the order of \$11 per passenger³. For Rockhampton Airport, the price differential is approximately \$14.00 per passenger.

\$14 per passenger may not appear to be a large price differential but it is significant when considering that current airfares between Rockhampton / Brisbane and Rockhampton / Sydney are available for \$69 and \$89 respectively. When considering Rockhampton Airport’s annual passenger arrival figures were approximately 200,000 (2003/04 financial year), the \$14 per passenger cost differential equates to a saving of approximately \$2.8M in favour of airlines operating from Newcastle Airport.

The ADF also provides free ATC services to domestic aircraft operating at Townsville and Darwin Airports, again providing substantial cost savings when compared to airports served by Airservices Australia.

The imminent arrival of AsA managed ARFF services at Townsville Airport is of significant interest as AsA’s has advised that the ADF has agreed to pay for the provision of ARFF services to the ADF. Of concern is that regardless of the change in ADF policy for Townsville Airport, AsA continues to advise that it is unable to recover the costs associated with the provision of ATC or ARFF to the ADF at Rockhampton Airport.

The table below details the unrecovered ARFF & ATC income from military operations at Rockhampton Airport. By not recovering these charges directly from the ADF (approx \$240,000 per annum), AsA is forced to pass these costs onto domestic aircraft operators, providing a distinct competitive disadvantage to our airport.

Rockhampton Airport - Military Tonnes Landed		
1995 to 2004 Profit / Loss		
Total tonnes '95 to '04		127,108
ARFF (\$ per tonne)	\$	9.59
Total loss to ARFF*	\$	1,218,963
ATC (\$ per tonne)	\$	7.42
Annual Loss to ATC*	\$	943,139
Total loss for '94 to '04	\$	2,162,103

¹ Airservices Australia Draft Price Notification - August 2004 “Overview of the Notification”, page 3

² Taken as an average of all ARFF and ATC services operated by AsA within Australia

³ Based on a 737-700 (70 tonnes) with 70% load factor & an Australian averaged ARFF charge of \$8.15 and an Australian averaged ATC charge of \$7.30. Note: this is using current Airservices Australia charges, not the proposed increased prices.

Pricing Across Services and User Groups (continued)

The Australian Airports Association (AAA) currently manages all military landing charges associated with member airports⁴. The table below details the estimated average tonnes landed at all member airports⁵ and the effective annual loss to AsA as a result of its inability to recover the costs associated with military operations.⁶

Based on the abovementioned assumptions, we estimate that domestic air operators and passengers at AsA serviced ports are effectively subsidising ADF operations by approx \$1.2M per annum. Lower capacity airports that require AsA's services are clearly disadvantaged by military operations being conducted at their airports.

All Australian Airports - Military Tonnes Landed

Average Annual Profit / Loss (FY 2000 to 2004)

Average annual tonnes		114,812
ARFF (\$ per tonne)	\$	8.15
Annual loss for ARFF*	\$	935,718
ATC (\$ per tonne)	\$	7.30
Annual loss for ATC*	\$	838,128
Total annual loss (70%)	\$	1,241,692

** Note: This is the average of all Airservices Australia managed ARFF and ATC services*

Impact on users

The tourism industry in Central Queensland is in its infancy when compared to more established destinations. It is an industry that has a proven record of delivering substantial benefits to regional communities.

Low cost carriers are aggressively targeting the leisure travel market in an effort to grow their businesses. The benefits are most noticeable in regional communities where affordable air travel is enabling short stay interstate and intrastate tourism.

The proposed increases in AsA charges and their discriminatory pricing methods have the potential to reduce the appeal of Central Queensland as a tourism destination by distorting ticket prices further in favour of other destinations.

Please refer our enclosed letter to Airservices Australia for a detailed explanation of the regional impact of the proposed price increases⁷.

⁴ As at 01 January 2002, represented the interests of over 255 member aerodromes and airports Australia.

⁵ Due to privacy legislation, the AAA was unable to provide specific information on military movements, therefore landed tonnes has been estimated by dividing the annual AAA military landing income by the AAA military landing fee. It has been assumed that 70% of all military landed tonnes were fixed wing and 30% rotary wing.

⁶ Assuming that 70% of all AAA military landing fee income was derived from airports serviced by AsA.

⁷ Please note that this letter was written in response to AsA's original price increase proposal

Summary

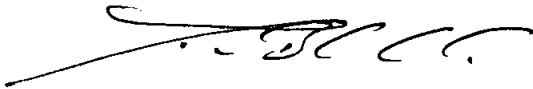
The geographical diversity of airports does not necessarily inhibit competition and many airports with similar socio-economic demographics and / or tourism product do compete vigorously for market share.

Rockhampton Airport is in competition with several Australian airports and we find it incongruent that some enjoy a significant commercial advantage as a result of AsA's inconsistent location based pricing policy.

It is acknowledged that Central Queensland derives significant benefits from military exercises in the region. As long as AsA is unable (or unwilling) to recover the cost of providing services to the ADF at Rockhampton Airport, we will continue to be commercially disadvantaged by military operations. The result is that our domestic customers (both passengers and aircraft operators) are effectively subsidising military operations at our airport.

We recommend that AsA's develop a commercial relationship with the ADF and review the forecasted traffic figures for our airport. These tasks should reduce the proposed price increases for ARFF and possibly ATC at Rockhampton Airport.

Yours faithfully



David J Blackwell
General Manager
Rockhampton Airport

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