



**SUBMISSION TO**

**THE AUSTRALIAN COMPETITION &  
CONSUMER COMMISSION**

**BY THE  
Royal Victorian Aero Club**

**DRAFT PRICE NOTIFICATION  
AIRSERVICES AUSTRALIA**

14<sup>th</sup> September 2004

## INTRODUCTION

Our main concern with the present proposal is the large and unnecessary transfer of costs from the major airline sector to the financially weaker, small business, general aviation sector. This is excessive use of market power by the majors.

Our other concern is a conflict that AsA appears to be ignoring. It cannot comply with its responsibility under the Air Services Act to promote and foster aviation while at the same time reducing cross subsidisation between service lines and user groups. The more that location specific pricing is applied the more AsA is destroying general aviation.

We see no reason why the present balance should not be retained and any cost increases spread equally on a percentage basis over all sectors. In the present proposal we are looking at a 71% increase at Moorabbin over 4.5 years compared with a 5.8% weighted average total increase.

The following comments address the issues raised in the Issues Paper and are oriented on the effect of the proposal on operations and operators at Moorabbin Airport in Melbourne.

This submission is in addition to that already supplied in July to both Airservices Australia (AsA) and the ACCC as part of the consultation process with General Aviation businesses.

### The Consultation Process

*Comment on the effectiveness of AsA's consultation processes and the extent of our support.*

The original proposal for 565% increase at Moorabbin was a disaster that should not have occurred.

It was created without input from general aviation interests. While this input might be hard to obtain from busy operators, it nevertheless should have been totally obvious that the first proposal would be violently objected to by such people.

When consultation with general aviation began in June 2004 it occurred, not in a spirit of discussion and negotiation prior to decision making, but rather as an adversarial fight over indefensible proposals. The proof of this is in the 600 submissions to AsA and the highly modified proposal now before us.

It is our view that the first proposal was a huge mistake that should never have seen the light of day.

Even now we do not support the current proposal for reasons stated later in this submission.

RVAC proposes that representatives of the ACCC attend a meeting of GA operators in the Melbourne basin. RVAC will host the meeting and ensure that the agenda is focused on finding a workable solution for the Melbourne basin airports. We also consider that the ACCC should also attend other capital cities with a view to holding similar meetings with GA operators.

## **Risk Sharing Arrangements**

*Comment on the appropriateness of risk sharing arrangements should changed circumstances occur during the next five years.*

We have no difficulty with a review of pricing within the five-year period so long as AsA will consult with general aviation interests and follow standard price notification processes to the ACCC.

## **Operating Costs**

*Comment on the efficiency with which AsA provides its services, including the level of costs and incentives to contain costs.*

We are unable adequately to comment on the overall level of AsA operating costs, nor their ability to contain or reduce the overall level of costs.

However, it is of interest to note that staff costs and total operating expenses of the tower at Moorabbin, the only AsA service we really use, are forecast to rise over the five year period by only 16%, well under the overall 24%. In the same five-year period the charges proposed on our tower usage are to rise by 71%.

## **Capital Expenditure**

*Comment on the efficiency of the capital expenditure program, including the appropriateness of projects, the level of costs proposed and the approach taken to determine the program.*

Our only comment on this subject is that it is obvious that all the capital expenditure is for the benefit of the major airlines. We see nothing in the way of capital expenditure at Moorabbin. So we do not accept that this is any reason for increasing prices at Moorabbin. It is illogical shifting of costs to a virtual non-user.

## **Asset Base**

*Comment on the efficiency of AsA's asset base, the appropriateness of new values and the appropriateness of revaluations from zero written down book values.*

The matter of revaluing assets is an accounting matter, which should not be allowed to impact on cost calculations for AsA services.

It is stated that the revaluations are related to the extension of the useful life of assets by constant repair and maintenance. It would seem highly probably that those expenses have already been factored into costing.

Revaluing and then charging out new depreciation, as well as ongoing maintenance, is double dipping and should not, in our opinion, be allowed.

## **Rate of Return**

*Comment on the proposed rate of return (9.75%), the progressive transition to this figure over the five-year period and the extent to which this is an incentive to increase productivity and contain costs.*

With AsA paying the full range of taxes, plus a dividend to the Federal Government, we wonder why there is a need to build up a surplus for the benefit of future users. Why should current users of AsA's services pay more than is required to meet actual costs? This is not "user pays" it is "user overpays".

Any profit made by AsA is an unnecessary charge on current users for the benefit of others, including the Federal Government. If nothing else this profit should be returned to the payers in funding a community service obligation (see later comment on this subject)

We would also comment that we are highly sceptical that a desire to achieve a 9.75% return on assets is adequate incentive to management to control costs. We do not know what penalty applies to management (including the Board) if the rate of return is not achieved.

## **Activity Forecasts**

*Comment on the reasonableness of AsA's activity estimates.*

The activity level at airports, and in particular at Moorabbin, is mainly dependent on costs.

There are numerous examples of aircraft leaving Moorabbin for other non-towered airfields close by because of the cost of operating at Moorabbin.

AsA's costs are only one of the many costs, including in particular the charges of the airport owner. To Moorabbin Airport Corporation's credit however is that their increases basically follow CPI increases.

This is not so with the current AsA proposal which is way above the CPI.

We consider the activity forecasts are only reasonable if cost increases mirror CPI increases. If costs escalate beyond that then there we warn of negative activity going forward.

In the latter event AsA will not achieve its forecasts.

## **Structure of Prices**

*Comment on whether the proposed method of cost allocation is appropriate.*

In our view cost allocation via location specific pricing is definitely not appropriate.

Location-specific pricing is an idealistic accounting and academic theory that fails when the blowtorch of reality is applied to it.

AsA is already moving away from it with a statement that it has adjusted its approach to the allocation of indirect costs to take into account "capacity to pay". That is reality at work and proof that location specific pricing is not viable commercially.

Capacity to pay is a powerful tool. No business in the world can sell a product at a price that the customer is unwilling or unable to pay. Even monopolies like AsA cannot force users to pay more than they are willing to pay.

In our view it is about time that the networking principle was accepted. Cross subsidisation, eventually, cannot be avoided.

### **Basin Approach**

*Comment on the application of the capital city basin approach to charging for terminal navigation services.*

The basin approach is networking under another name. It is certainly a better answer than the first AsA proposal, but it is still networking. Why not extend networking through the whole AsA operation?

In effect, the basin approach proves the efficiency and viability of network pricing.

### **Timing of Price Increases**

*Comment on the phasing in of proposed price increases stemming from both changes in cross subsidisation and increased costs.*

We see no reason for the first huge increase. The total increase should be spread evenly over the five years, commencing say on 1 January 2005 and annually thereafter. Alternatively there could be a half-annual increase in January, followed by full annual increases in July of each subsequent year.

### **Pricing Across Services and User Groups**

*Comment on the stated aim of AsA of avoiding cross-subsidies and on the appropriateness of the levels of cross-subsidies between services and between user groups.*

We register our protest, in the strongest possible terms, of the total 71% increase imposed on secondary airports such as Moorabbin.

As stated earlier, increases in costs at Moorabbin are around 16%, so a 71% increase in costs is harsh, unreasonable and in fact unconscionable.

**What we are witnessing is a desire to transfer cost recovery from the major airlines to general aviation**, which is a minimalist user of AsA services compared with the majors. Likewise the majors would be the main beneficiaries in the reduction in the en-route service cost.

Without a transfer of costs between the majors and general aviation, the status quo could be maintained with an increase of 5.8% on current costs, spread over the five years.

We also see cross subsidisation as a practical and desirable attribute.

The concept of network pricing does not appear to be contrary to Government policy. This seems to be a similar concept used by other Government organisations. For example, Australia Post charges 50 cents to send a standard letter anywhere in Australia, and Telstra is required to cap the cost of a

local telephone call in all areas. These charges are not reflective of location specific pricing, but rather network pricing.

In business it often makes practical sense. The reality of life in the business world is such that eventually cross-subsidisation will come to be accepted.

Also, in our opinion, the major airlines form a group exerting unacceptable business power. They see large financial benefits from this issue of location specific pricing.

*Further comment on whether the proposed prices provide incentives for AsA to provide services at particular locations and whether users have incentives to provide their services.*

AsA does not need a financial incentive to provide a service at a particular location. Its charter to provide air safety governs this.

Users of AsA services are very much influenced by the cost. If one cannot operate profitably at a location, then one will simply and quickly walk away. Cost increases (especially unreasonable and unfair increases) are a huge disincentive to small businesses and contrary to AsA's charter to promote aviation.

## **Impact on Users**

*Comment on the likely impact of the proposed prices on the users of airports and air traffic control services and to the providers of aviation services*

The high increase in prices at Moorabbin will have a severe affect on providers of various aviation services.

Every customer who leaves the airport because of the higher costs reduces the business viability of the whole airport community.

Each airport is a small economic group, in many ways interdependent on each other. There are flying schools, aircraft maintenance businesses, spare parts businesses, charter operators, bookshops, coffee shops, restaurants etc. They all depend on each other for their livelihood. Price increases above the norm drive people away and they never come back. Again we say that this is not compliant with AsA's charter to operate in a way that promotes the general health of the aviation industry.

## **Other Issues**

### **Community Service Obligation**

This issue keeps being dismissed by Government and it may well be beyond the scope of this inquiry.

Nevertheless we continue to press for its implementation. The fact that the \$7m capping subsidy (another word for a CSO) has been withdrawn is no doubt a political matter and we may well have to pursue this matter in that arena.

In our view the need for a CSO commitment is clear.

There are so many areas where AsA's services are for the benefit of the public at large. The Air Services Act requires AsA to regard the safety of air navigation as its most important consideration. Also it is required to protect the environment (meaning also the public in our view) from the effects associated with the operation and use of aircraft.

These towers play a significant safety role for not only the pilots and their passengers, but also, significantly, for all persons and property under and in the vicinity of the flight paths.

They also provide a safety role for the general public via community-based services such as the Police Air Wing, Air Ambulance, Fire Fighting Services, Royal Flying Doctor Service and State Emergency Services.

Therefore, the funding that the Federal Government has provided since the implementation of location specific pricing in 1998/99 should continue, not as a one-off subsidy, but specifically as an ongoing commitment to its community service obligation. This would include a portion funded by the State Government.

### **Unemployment**

It is our considered opinion, based on experiences at Moorabbin over the past few years that continuing price increases will result in business closures and unemployment.

Over the past few years, prices in many sectors of aviation have escalated enormously. The ability to pass on these costs to our consumers has reached breaking point.

Cost increases have arisen in the following areas – wage increases, spare parts cost, the GST, CASA costs, aircraft repair costs, fuel costs, rental costs, airport owner charges and numerous other costs.

There is evidence of numerous business closures at Moorabbin over the last few years, so we are confident that further cost increases, such as the current proposal, will be directly reflected in unemployment.

### **Monopoly Service Provider**

We are frustrated by the cost pressures being proposed by AsA in this proposal.

One should be able to seek alternative services from a competitor. We can do just that with electricity and telephone services.

We only need to look at Europe and Canada to see how successful EuroControl and Transport Canada have been to know that alternative and competitive systems exist.

### **Business Investment**

This proposal has brought all strategic planning and capital expenditure to an immediate halt. This Club, and other operators we know, have stopped planning for growth and development until this issue is satisfactorily resolved.

We believe that the proposed increases are unsustainable for general aviation.

## **Overview of Issues Facing General Aviation**

Whilst it is recognised that AsA does not have control over areas other than its specific business, the proposal to increase fees must be viewed in context with other issues that are facing every GA business within the same timeframe.

In some instances, GA is over serviced at secondary airports; for example, Essendon Airport has Air Traffic Controllers on duty 16 hours per day.

We have been advised that the Civil Aviation Safety Authority (CASA) has also reviewed its pricing structure. Fees to industry have at least doubled and may well increase substantially more than that as they try to move to full cost recovery. We understand that the implementation date for these fees is also 1 July 2005. Coupled with this is the impost of around \$220 each pilot is likely to face every two years for a security clearance.

Moorabbin Airport is now privately owned and the airport owner (Moorabbin Airport Corporation) is extremely concerned at the possible loss of a very large proportion of general aviation aircraft from this airport. Conversely, we wonder if the present developer-owner may welcome the potential closure or size reduction of the airport so that it may move further with its extremely profitable full commercial development.

The Civil Aviation Safety Authority will be introducing the new Civil Aviation Safety Regulations (CASR) Part 61 Flight Crew Licences and Part 141 Flight Training Operators rules within this same general timeframe. This will involve all flying schools being required to rewrite syllabi, produce new operations manuals, and implement Safety Management Systems and train staff to be compliant with the new regulations. This will incur a significant cost to each organisation.

The introduction of the GST has had an adverse impact on the GA industry. Prior to its introduction, aircraft parts were free of sales tax as cost of replacement parts was considered to be a safety issue. The GST was also applied to labour cost for the first time and the GA industry is very labour intensive.

Because the GST imposes very significant cost on the GA industry, and the Federal Government returns GST back to the States, it would seem appropriate for the State Government to apply this GST to meet costs associated with community service obligations for aviation activities.

The cost of fuel comprises 25 – 35% of operating costs and this item is at a historically high level, exacerbated by the application of the GST

Our concern is that when all of the above factors are taken into account, our costs will be substantially greater than previously experienced, which will affect the viability of our business.

## **Level of ATC Service at Moorabbin**

At the current air traffic movement rates we do not believe that, as a general rule, Moorabbin Tower could be safely operated with fewer controllers or for fewer hours per day.

The most recent safety case investigation, conducted approximately 18 months ago by the Australian Transport Safety Board (ATSB), while not concluding that additional staffing and hours were required, was very critical of the current level of staffing.



This investigation was conducted after a fatal in-flight collision that occurred during night hours, when the tower was unmanned and the airport was experiencing a high level of traffic movements.

The collision occurred within the airport boundary, but had it occurred over nearby private housing, the outcome would have been much more serious. This is further reason why we consider the Federal and State Government has a community service obligation to provide AsA services.

RVAC does not support a reduction in the current tower service levels at Moorabbin.

Needless to say, if the fees as proposed are implemented the traffic will most likely decline to such an extent that tower services would have to be cut or withdrawn altogether. Uncontrolled aircraft flying over neighbouring residential area at night and at weekends would not be acceptable from a safety viewpoint to the people residing in the near vicinity of the airport.

The further transfer of a substantial number of Moorabbin based aircraft to outlying satellite airfields in the Melbourne basin would adversely affect both safety and the environment at those airfields. Some of these airfields are already operating at maximum capacity at peak periods.

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