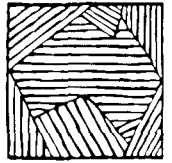


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A·F·T·A
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OF TRAVEL AGENTS
LIMITED
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The General Manager
Adjudication Branch
Australian Competition & Consumer Commission
PO Box 1199
DICKSON ACT 2602

By email: adjudication@acc.gov.au

26 May 2006

Dear Sir/Madam

**Qantas and Air New Zealand Applications for Authorisation: A91001, A91002, and A91003
Tasman Networks Agreement**

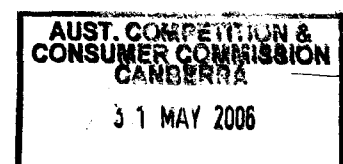
We refer to your letter of 19 April 2006.

The Australian Federation of Travel Agents ("AFTA") makes the following submissions in response to the applications.

The Applications

1. These submissions address the applications made on behalf of Qantas Airways Limited ("Qantas") and Air New Zealand Limited ("Air New Zealand") in relation to the Tasman Networks Agreement ("TNA") and the supporting submission.
2. AFTA has a number of concerns in respect of the applications and the TNA going to:
 - The likely impact on competition on the Tasman routes;
 - The impact of airfares;
 - The ability of travel agents to compete with Qantas and Air New Zealand for the sale passenger air travel tickets on the Tasman routes.

The extent of the TNA



3. The TNA between Qantas and Air New Zealand is in fact an agreement covering the coordination of activities between four airlines as it includes Jetstar and Freedom Air. Jetstar and Freedom Air are the low cost carriers (LCC) of Qantas and Air New Zealand respectively.
4. Paragraph 2.12 of the submission to the ACCC states that flights operated by Jetstar or Freedom Air will not automatically form part of the code share arrangements, **but may be introduced at a later date** (emphasis added). Additionally, it is proposed that Jetstar and Freedom Air will be included in the cooperation under the TNA and the revenue on the Tasman routes will be subject from the TNA model from the outset.
5. Annexure "D" to the submission sets out the Tasman carriers and frequency per week on a one way basis. **Table 1** below compares the TNA carriers to the total frequency on the Tasman routes on a one way basis, the information being extracted from Annexure "D". This shows that on the main routes Sydney-Auckland and Melbourne-Auckland the TNA carriers account for 81% and 82% respectively of the total frequency. On many other routes the TNA carriers account for 100% of the frequency.

Table 1: Tasman Frequency Comparison - All carriers and TNA carriers

Route	Total Frequency per week one day	TNA	TNA%
BNE/AKL	33	17	51
SYD/AKL	85	69	81
MEL/AKL	40	33	82
ADL/AKL	3 (QF/JQ)	3	100
CNS/AKL	3 (NZ/FA)	3	100
OOL/AKL	9	7	78
PER/AKL	7 (NZ/FA)	7	100
BNE/CHC	22	15	68
SYD/CHC	43	31	72
MEL/CHC	22	18	82
OOL/CHC	7	7	100
BNE/WLG	12	9	75
SYD/WLG	26	26	100
MEL/WLG	14	14	100
OOL/WLG	1(FA)	1	100
SYD/ZQN	6	6	100

Key:

BNE – Brisbane	MEL – Melbourne	OOL – Gold Coast
SYD – Sydney	CNS – Cairns	PER - Perth
WLG- Wellington	AKL – Auckland	ZQN - Queenstown
CHC - Christchurch		

6. The reality is that the fifth freedom carriers on the Tasman routes provide little in the way of competition.
7. **Table 2** sets out the frequency and departure time for the fifth freedom carriers on the Tasman routes. Emirates with a daily service out of Brisbane, Sydney and Melbourne to Auckland and from Sydney to Christchurch is the

only fifth freedom carrier with a single daily service. The Royal Brunei service out of Brisbane departs either very early in the morning or late at night. The two flights a week by Garuda from Brisbane to Auckland leave at 06:50.

8. On the Sydney-Auckland route Aerolineas Argentinas flies three times a week departing at 09:30 whilst Lan Chile departs four times a week departing at 10:55.
9. It is difficult therefore to support the Qantas and Air New Zealand submission that fifth freedom carriers provide a competitive constraint on the applicants on the Tasman routes. Further, it is difficult to see how Emirates with one flight a day can act as a "maverick" thereby keeping the applicants on a continual competitive alert as it is asserted in paragraph 4.2(e) of the submission.
10. Whilst it is accepted that fifth freedom carriers can engage in marginal cost pricing this must be balanced in the market as against availability/timing. As Table 2 shows the fifth freedom carriers have little to offer by way of frequency and in the specific case of Emirates only a single daily departure.
11. By their very nature fifth freedom carriers do not have the ability to expand services on the Tasman routes.
12. Any competitive constraint which fifth freedom carriers could provide to the applicants would be limited only to the times of the fifth freedom carriers' departure. The proposed default departure schedule would enable the applicants to structure their fares to target the fifth freedom carriers' irregular flights and the applicants would then be relatively unrestrained for the rest of the schedule. This has become possible by the introduction by the applicants of sector fares much like which operate now in the Australian domestic market. This allows the airlines to vary the cost of a sector depending on availability, timing and competition.

Table 2: Comparison Draft Initial Tasman Networks Plan and Fifth Freedom Airline Schedules

AKL to BNE					From BNE				
Fits	Freq	Dep	Arr	Eqps	Fits	Freq	Dep	Arr	Eqps
NZ205	34567	6:25	8:05	320	NZ206	34567	9:05	14:30	320
NZ207	123_5_7	15:30	17:20	320	NZ208	123_5_7	18:20	23:45	320
JQ414	23_5_7	6:15	8:05	320	JQ413	23_5_7	8:45	14:05	320
JQ416	1_4_6	14:45	16:35	320	JQ415	1_4_6	17:15	22:35	320
GA	3_6	13:35		330	GA	3_6	6:50		330
BI	1	10:30		763	BI	1	4:20		763
	2	10:10		763		2	21:50		763
	6	10:10		763		6	22:50		763
EK	1234567	8:10		773	EK	1234567	8:10		773

AKL to SYD					From SYD				
Fits	Freq	Dep	Arr	Eqps	Fits	Freq	Dep	Arr	Eqps
QF40	1234567	6:30	7:55	763	QF163	1234567	7:00	12:00	763
NZ119	1234567	8:00	9:30	744	QF19	1234567	9:15	14:10	763
NZ904	1234567	9:30	11:00	320	NZ118	1234567	11:30	16:30	744
QF190	1234567	13:15	14:45	763	NZ905	1234567	12:00	17:00	320
QF120	1234567	15:30	17:00	763	QF43	1234567	13:30	18:30	763
QF902	1234567	16:30	18:00	763	QF49	1234567	18:15	23:15	763
NZ906	1234567	18:00	19:30	320	QF903	1234567	19:00	23:59	763
QF45	1234567	19:45	21:15	763	NZ907	1234567	20:30	1:30	320
AR	2_4_7	5:25		340	AR	2_4_7	9:30		340
LA	123_5	6:10		340	LA	123_5	10:55		340
EK	1234567	15:50		77W	EK	1234567	9:15		77W

AKL to MEL					From MEL				
Fits	Freq	Dep	Arr	Eqps	Fits	Freq	Dep	Arr	Eqps
NZ908	12345_7	6:00	7:45	763	NZ909	12345_7	8:45	14:05	763
QF26	1234567	7:00	8:45	744	QF27	1234567	10:55	16:15	744
NZ900	12345_7	12:00	13:55	320	NZ901	12345_7	15:00	20:25	320
NZ900	6	12:00	13:55	772	NZ901	6	15:00	20:25	772
NZ134	1234567	16:00	17:25	763	NZ139	1234567	18:45	0:10	763
EK	1234567	17:50		345	EK	1234567	7:15		345

CHC to SYD					From SYD				
Fits	Freq	Dep	Arr	Eqps	Fits	Freq	Dep	Arr	Eqps
NZ181	1234567	7:00	8:30	320	QF45	1234567	8:25	13:20	763
QF46	1234567	14:35	15:50	763	NZ182	1234567	9:50	14:50	320
NZ183	1234567	16:00	17:30	320	NZ184	1234_6	18:25	23:25	320
JQ410	1234567	6:45	8:10	320	NZ184	5_7	19:30	0:30	320
JQ412	3_5_7	15:05	16:30	320	JQ409	1234567	8:50	13:50	320
					JQ411	3_5_7	17:10	22:10	320
EK	1234567	18:10		345	EK	1234567	7:50		345

13. Virgin Blue only provides competition on six routes being:

- Brisbane to Christchurch;

- Melbourne to Christchurch;
- Sydney to Christchurch;
- Brisbane to Wellington;
- Brisbane to Auckland;
- Coolangatta to Auckland.

14. Notably Virgin Blue does not fly the Sydney and Melbourne to Auckland trunk routes.
15. **Table 3** compares Virgin Blue's frequency to the total frequency and the applicants' frequency on the Tasman routes.
16. Only on the Brisbane/Christchurch route does Virgin Blue fly a daily service which departs at 18:10.

Table 3: Frequency Comparison on Routes Flown by Virgin Blue

Route	Total Frequency	TNA	Virgin Blue	Virgin Blue %
BNE/CHC	22	15	7	32
MEL/CHC	22	18	4	18
SYD/CHC	43	31	5	12
BNE/WLG	12	9	3	25
BNE/AKL	33	17	4	12

Full Service Airlines and Low Cost Carriers

17. The applicants have approached the trans Tasman market by utilising their respective LCCs Jetstar and Freedom Air with ever increasing frequency. This has been partly in response to a perceived threat from fifth freedom carriers but predominantly as a way of reducing costs and increasing profit on those routes. As the applicants note at paragraph 5.50 of their submission Jetstar's presence on certain Tasman routes has seen it effectively replace the Qantas mainline services which have been withdrawn from Brisbane, Christchurch and Melbourne.
18. Part of the cost reduction initiatives include simplified and cheaper fares with an accompanying reduction in service.
19. Any perceived threat to the applicants by fifth freedom carriers is more than adequately addressed by the applicants' reliance on their respective LCC's.
20. The applicants' assertion at paragraph 9.31 that they must limit deployment of their LCCs due to the "cannibalising" impact that their widespread deployment would have on the network feed traffic upon which the parent airlines rely ignores the fact that the Tasman routes are now being effectively treated as domestic trunk

routes. Further, Qantas is increasingly using Jetstar as its substitute airline to a number of Asian ports as Qantas withdraws services or introduces low cost services to new destinations. Qantas, and to a lesser degree Air New Zealand, is evolving into a two tier carrier utilising its LCC to compete with fifth freedom carriers and other airlines operating on a lower cost base.

21. AFTA is concerned that there is a real risk that in the event authorisation is extended to Jetstar and Freedom Air there will be a reduction in competition on the Tasman routes; that the LCCs will gradually replace the FCAs and that prices will rise at those times of the day when there is limited or no competition.

Incentive Commissions

22. The TNA provides that the applicants are to implement a "one off" alignment of the basis for paying incentive commissions to travel agents (paragraph 2.1 of the submission and schedule 10 sec 2 of the TNA). The TNA provides Qantas and Air New Zealand will pay agents based on who is the marketing carrier but the applicants will continue to unilaterally determine the level of commissions each pays.
23. Clause 2.1 of schedule 10 provides that where the basis for calculating an incentive payment uses "Operating Party" revenue, that party must take all reasonable steps to change the basis of payment to "Participating Party" revenue.
24. Operating Party is defined in the TNA as being the party operating a codeshare flight. Participating Party is defined as meaning in respect of a codeshare flight, the party which does not operate such flight but places its designated code on such flight and offers seats for sale on that flight under its own designated code or flight number.
25. Neither Qantas nor Air New Zealand nor their LCCs pay a base commission on trans Tasman fares. Travel agents however have been able to negotiate incentive payments with the applicants.
26. Travel agents which operate on both sides of the Tasman are able to negotiate incentive agreements separately with Qantas and Air New Zealand and separately in Australia and New Zealand. AFTA's concern is that if authorisation is granted Qantas and Air New Zealand will then coordinate incentive payments to travel agents which must inevitably lead to a reduction in such payments. AFTA takes little comfort from the applicants' assertion that they will continue to unilaterally determine the level of commissions each pays: base commissions have been abolished on Tasman routes and the applicants intend to change the basis of the payment incentives to take into account the proposed pooling of revenue. The abolition of competition between the applicants for market share on the Tasman routes must inevitably lead to a reduction of income paid to travel agents by the applicants.

27. As the Commission has already determined in Authorisation A90791 airlines compete with travel agents for the sale of air travel and in very competitive airline markets there is an incentive for airlines to reduce the costs of distribution as much as possible. Travel agents in recent times have seen the abolition of base commissions by the applicants on the Tasman routes. A further reduction in the ability of travel agents to earn remuneration on the trans Tasman market coupled with the effective creation of a monopoly on many of the trunk routes must, in AFTA's opinion, give rise to a public detriment.

Management of the Tasman Network

28. The applicants contemplate that management of the Tasman network will be undertaken by a committee in accordance with principals set out in the TNA (Sec 11). The committee is to comprise six members with three members each being appointed by Qantas and Air New Zealand. AFTA is concerned that the quorum is only two members. The functions of the committee are extensive and are set out in paragraph 2.13 of the submission. AFTA notes that one of the functions is the setting of pricing. In effect the business of the committee may be undertaken by only two of its members which would potentially reinforce the observation that in respect of the Tasman routes Qantas and Air New Zealand would operate as a single airline.
29. The TNA also provides for a Working Group to be established to take responsibility for the day to day operation of the TNA and to provide operational support to the committee. The Working Group is covered in Sec 12 of the TNA and will be comprised of eight members. The provision for a quorum of the Working Group is found in Schedule 3 to the TNA. AFTA is concerned that the quorum of the working group will only be two members in respect of a proposed one off fare change and in all other circumstances two members appointed by each of the airlines.

Tasman Air Passenger Services Market

30. The applicants assert at paragraph 7.2 of the submission that the applications are based on a single product market for air passenger services on the routes between any point in Australia and any point in New Zealand.
31. The applicants assert at paragraph 7.4 that there is no relevant distinction between business and leisure passengers, or economy and business/first class passengers in respect of this market primarily as a result of the routes being short haul in nature.
32. In Authorisation A90791 (at Sec 7.2 and following) the Commission noted:
- It has consistently stated that the most important dimensions of the passenger transport market are the geographic and product dimensions;
 - It cannot be assumed that a single air transport market exists for both economy and premium class passengers and the Commission noted the differences in demand characteristics and service

- requirements of premium class and economy class passengers and the extent to which substituted services are acceptable to premium class passengers can be provided by airlines in competitive markets;
- It considered that in the premium class cabin the high proportion of passengers travelling under corporate contracts and within loyalty programs would effectively lock those passengers into specific airlines and make it difficult for other airlines to enter that market (paragraph 7.16).
33. AFTA is concerned that the TNA will have a public detriment by reason of the reduction in substitution possibilities.
34. The TNA foreshadows the coordination of activities (in effect the removal of choice) in matters such as in flight servicing and pricing.
35. AFTA takes issue with the applicants' assertion that there is no relevant distinction between business and leisure passengers, or economy and business/first class passengers in respect of the Tasman market as a result of the routes being short haul in nature. As the applicants themselves have noted at paragraph 9.31 of their submission the deployment of the low cost subsidiaries is limited out of fear of the impact this would have on the Network feed traffic which is provided by full service airlines. In AFTA's experience connecting inbound and outbound non leisure passengers require the same class of travel on their onward legs. AFTA disputes the applicants' assertions that the alternatives on the Tasman routes being Virgin Blue and Emirates offer close substitutes. For the reasons set out above on many of the Tasman routes there is in fact no substitutes and on those routes where Virgin Blue and Emirates operates the frequencies are such that they do not constitute close substitutes.

Tasman Load Factors

36. The applicants in figure 2 of the submission provide Tasman load factors for all carriers on services between Auckland/Wellington/Christchurch and Brisbane/Sydney/Melbourne. The figures, which are stated to have been supplied by Air New Zealand, show that as at December 2002 the Tasman load factor was 80% but steadily reduced to below 70% around December 2004 and has remained constant since then. It should be noted that Emirates entered the trans Tasman market in August 2003 and currently operates B777s and Airbus 340s on the routes.
37. The applicants at paragraph 5.8 give estimates of daily empty seat capacity across the Tasman. But this of course is deceptive as it includes unused capacity of the fifth freedom carriers. As set out in these submissions the fifth freedom carriers operate limited scheduling and only Emirates has a daily service from the major ports.
38. What the applicants do not provide the Commission (and which in AFTA's opinion is highly relevant) are the applicants' individual load factors on the Tasman routes.

The likely impact of the TNA on average air fares

39. AFTA is concerned that if authorisation is granted then it would result in Qantas and Air New Zealand having a high market share in the relevant market. As set out above AFTA does not believe fifth freedom carriers provide sufficient competition to constrain the proposed joint activities. The only real fetter on Qantas and Air New Zealand comes from Virgin Blue whose route network is limited.
40. AFTA believes that Qantas and Air New Zealand unrestrained will exercise its ability to raise prices. AFTA notes the finding of the New Zealand Commerce Commission in respect to the application of a proposed alliance between Qantas and Air New Zealand that the expected average air fare increase on the trans Tasman routes (in year 3) would be 16%.

Conclusion

41. There are a number of factors giving rise to anti-competitive detriment in the TNA which are of concern to AFTA. In summary they are:
- The inclusion of the LCCs Jetstar and Freedom Air in the authorisation;
 - The Qantas Group and Air New Zealand Group together accounts for a high proportion of capacity and frequency and on some routes on the trans Tasman represent 100% of capacity;
 - There is a real risk Qantas and Air New Zealand will not be constrained by competition;
 - No real competition is provided by fifth freedom carriers and in reality fifth freedom carriers do not have the ability to expand services on the trans Tasman;
 - The only real competition is likely to come for Virgin Blue and even then that is only on certain routes;
 - There is a real risk that Qantas and Air New Zealand acting in concert will reduce remuneration to travel agents in respect of the sale of passenger air tickets on the trans Tasman routes which must result in a public detriment as Qantas and Air New Zealand will increasingly sell directly rather than through an agent.
42. In AFTA's opinion if the TNA is to be authorised that authorisation should not extend to Jetstar and Freedom Air.

Yours faithfully,



Mike Hatton
Chief Executive