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## BY EMAIL

Ms Tess Macrae  
Adjudication Branch  
Australian Competition & Consumer Commission  
Level 35 - The Tower - Melbourne Central  
360 Elizabeth Street  
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Dear Ms Macrae

### **Collective bargaining conduct notification CB00143 Further submissions in response to WAC and Redspot objections**

We refer to our detailed submission on 27 May 2010 in response to the Commission's Draft Objection Notice to the collective bargaining notification CB00143 lodged by our client, Hertz Australia Pty Ltd (**Hertz**) on behalf of itself and Avis, Budget, Thrifty and Europcar (**Notification**).

Following the lodgement of our detailed submission on 27 May 2010, we became aware of further submissions lodged by Westralia Airports Corporation Pty Ltd (**WAC**) on 12 May 2010 (**WAC Submission**) and Redspot on 25 May 2010 (**Redspot Submission**).

Let us be very clear about what WAC is really saying when it objects to the Notification. WAC is a monopoly supplier of airport space for the provision of car rental services at Perth Airport. The substance of its submission is that the exercise of monopoly power (ie setting prices as high as it is profitable for a monopolist to do so) is economically efficient and, apparently, unambiguously good for consumers, but that any collectively negotiated decrease in overall input prices, or any reduction in the marginal costs of car rental companies, is apparently inefficient and therefore bad for consumers. The hypocrisy in this submission should be self evident.

We consider that the substance of WAC's position has already been addressed in previous submissions, but for completeness, we set out below further responses to the issues raised in latest WAC Submission and the Redspot Submission.

## 1. WAC Submission

### 1.1 Characterisation of the Notification

WAC seeks to adversely characterise the Notification as a *'Cartel Immunity Application'*<sup>1</sup> and to claim that the car rental operators are *'colluding to subvert this process for their own commercial gain'* and that *'proposed collective bargaining will result in a cartel market for the purchase of airport space'*<sup>2</sup>.

While the submissions use inflammatory and offensive language, they raise no issue of economic substance to which any response is required.

### 1.2 WAC's process – current level of negotiations

WAC seeks to characterise its RFP process as being 'transparent, timely and fair'<sup>3</sup> and involving meaningful levels of negotiation between the parties.

In reality, the majority of the commercial terms and conditions in WAC's self described 'transparent' and 'competitive' process have been unilaterally set by WAC and are not subject to meaningful negotiation or bids in the RFP process.<sup>4</sup>

The process is also only asymmetrically 'transparent'. That is, WAC sees all prices and terms, whereas under the RFP process the car rental companies see nothing of other parties' pricing and have extremely limited input or ability to meaningfully negotiate on any individual element.<sup>5</sup>

Even in relation to those elements of the RFP process that can be bid on by the operators,<sup>6</sup> the ultimate allocation decision is still at WAC's discretion. Even in respect of those items, the RFP process is hardly transparent about the consequences of bidding higher or lower amounts. For example, WAC does not even guarantee that a 'Premium Location' will be awarded to the operator who submits the highest bid for that location.

### 1.3 Frustrating entry of other operators at airports

WAC claims that the parties to the Notification have consistently sought to frustrate the entry of the sixth car operator at Perth and other airport, including *'making representations to WAC that rental car operators at Perth Airport should be limited to five'*.<sup>7</sup>

No detail or evidence is provided in relation to this allegation. We are instructed that this allegation is unfounded.

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<sup>1</sup> WAC Submission, paragraph 1.2

<sup>2</sup> WAC Submission paragraph, 3.2 and 3.4

<sup>3</sup> WAC Submission, paragraphs 3.1 to 3.3

<sup>4</sup> Frontier Economics Report, section 3.2

<sup>5</sup> Frontier Economics illustrate the lack of transparency in the WAC RFP process by contrasting it with the example of an open tender multi bid process, where parties can revise their bids once they have seen offers put forward by other parties. Frontier Economics Report, p. 25.

<sup>6</sup> Frontier Economics Report, section 4.2

<sup>7</sup> WAC Submission, paragraph 3.5

This allegation is inconsistent with the collective bargaining group's recent invitation to Redspot to join the collective bargaining group.

WAC controls access to its own facilities. Redspot currently holds one of the six on-airport car rental licence available. WAC has indicated 6 licences are currently being offered. Is WAC seriously suggesting that if a collective bargaining process involving the 5 other operators proceeded, that Redspot (or indeed some other unidentified new entrant) will face any higher risk of exclusion from the airport? Fundamentally, this submission makes no sense because it is WAC that controls access to the airport land, not the other proposed members of the collective bargaining group.

#### 1.4 Collective bargaining likely to lead to price distortions

WAC asserts that:

- *'[the] market based mechanisms incorporated into the [RFP process] ensure that scarce airport space is put to its highest value use'<sup>8</sup>; and*
- *collective bargaining 'would distort the market based mechanism... with the likely outcome that the process will be below their efficient level'.<sup>9</sup>*

The first point relates to the issue of the allocation of terminal floor space and land surrounding the terminal. As set out in our previous submission, the RFP process contains no mechanism which would address this particular allocation issue. It is not designed to do so. Frontier concludes in relation to this issue that: *'the RFP process does not enable any of the allocation issues in section 2.1 [ie the allocation issue identified in the first point above] ... to be addressed'.<sup>10</sup>* Nor does the WAC Submission provide any coherent explanation as to why genuine scarcity issues cannot properly, and more efficiently, be addressed through the proposed collective bargaining process.

In relation to the second point, the fundamental premise of WAC's submission is that its own level and structure of prices (ie as set by a monopolist supplier) are 'efficient' and that any reduction in the overall levels or structure of these prices must be economically inefficient. There is no justification for this proposition as a matter of basic economic principle. Monopoly pricing involves the restriction of output below competitive levels and an associated deadweight loss to society. It is not an optimally efficient allocation of resources. Given this starting point, a collective bargaining process which seeks to establish a degree of both countervailing power and meaningful input by major users of the monopolist's services in relation to all elements of that service (which may include the structure as well as level of prices) has the potential to result in a more efficient allocation of society's resources (ie reducing the deadweight loss to end consumers).

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<sup>8</sup> WAC Submission, paragraph 3.8

<sup>9</sup> WAC Submission, paragraph 3.9

<sup>10</sup> Frontier Economics Report, p.13

Throughout its various submissions, WAC consistently ignores<sup>11</sup> the inconvenient fact that while it is a monopolist in relation to the provision of ready bays and counter space at Perth Airport, the car rental companies are not monopolists in relation to the provision of car rental services. They provide their own services in a competitive market with multiple on and off airport competitors. Reductions in marginal costs of inputs will result in increased output and lower prices in downstream car rental prices.<sup>12</sup>

Accordingly, we refer to our previous submission<sup>13</sup> where we demonstrate, on sound economic grounds, that:

- there is no theoretical or empirical basis to conclude that the WAC RFP process will result in more efficient outcomes than the proposed collective bargaining process – in fact, a number of features of the WAC RFP process are demonstrably likely to result in inefficiencies; and
- the proposed collective bargaining process is in fact more likely to promote allocative efficiency than the flawed RFP process.

### 1.5 Alternative uses of the facilities

WAC argues that *'airports facing below market prices for car rental space would allocate less space for that purpose in favour of other uses that bring higher returns'*.<sup>14</sup>

This argument is flawed for a number of reasons.

First, as discussed previously, it assumes that the RFP process is designed with this particular allocative issue in mind. However, on examination, it is apparent that there is nothing in the RFP process which contemplates the allocation of airport resources between car rental services and other services. The allocation decisions in relation to these facilities (in terms of both location and price) appear to have been unilaterally made by WAC and are not subject to negotiation or bids in the RFP process.<sup>15</sup>

Secondly, it assumes that monopsony power will be exercised through the collective bargaining process.<sup>16</sup> However, in this case the collective bargaining group is seeking to negotiate with a monopoly supplier, not a supplier subject to market based competitive constraints. The airport will seek to impose monopoly prices, not competitive or efficient prices. The car rental operators on the other hand provide services in a competitive market meaning that at their functional level of the market, they will have no ability to profitably restrict downstream output.

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<sup>11</sup> Or alternatively asserts that the car rental companies do not operate in a competitive market, contrary to all observable market facts.

<sup>12</sup> In fact, this would be true even if the car rental companies operated as a monopoly in the downstream market.

<sup>13</sup> Hertz submission dated 27 May 2010, section 2.2

<sup>14</sup> WAC Submission, paragraph 3.11

<sup>15</sup> Frontier Economics Report, section 3.2

<sup>16</sup> The theoretical concern being that a monopsony buyer could reduce price and therefore output below socially optimal levels.

Finally, even if the extreme assumption were made that there was both an monopsony buyer of ready bays and counter space who also enjoyed a monopoly in relation to the supply of car rental services at Perth Airport, it would still be the case that any reduction in input prices would represent a decrease in marginal costs. In turn, this would result in higher output of car rental services. This implies a reduction in deadweight loss and consumer benefit.

In summary then, the argument that the collective bargaining process could lead to public detriment through sub-optimal amounts of airport space being acquired makes no sense where the supplier of the services enjoys a monopoly such as WAC.

## 1.6 Validity of the Notification

We reiterate our previous submissions in relation to the validity of the Notification. In particular:

- each of the parties had (and continue to have) a reasonable expectation that the price for the acquisition of the relevant services from WAC will not exceed \$3 million in any 12 month period. Further information in support of these expectations is provided in Confidential Annexures A, B and C to this letter. Restriction of publication is claimed in respect of those parts of the submission set out in the Confidential Annexures;<sup>17</sup>
- there is no legal basis for WAC's assertion that the transactions of Avis/Budget and Hertz/Thrifty should be aggregated,<sup>18</sup> but even if aggregation were to be properly applied to related bodies corporate (an interpretation which Hertz rejects):
  - the operators of the Avis and Budget businesses at Perth Airport are not related bodies corporate - WAC is fully aware that this is the case and it is concerning that WAC continues to provide obviously misleading information to the Commission on this point;<sup>19</sup> and
  - Hertz and Thrifty are not related bodies corporate and will not become related bodies corporate even if the global acquisition of the Dollar Thrifty Automotive Group by Hertz were to complete;<sup>20</sup> and
- there is no 'overarching arrangement' between the parties to collectively bargain with multiple Australian airports. WAC continues to make unsubstantiated allegations in relation to this issue that are not supported by any evidence. WAC asserts that there is '*good reason*' to believe there is such an 'overarching arrangement'<sup>21</sup> but fails to enunciate these reasons and indeed states in a different section of its submission that it is '*unclear*' whether collective bargaining will be pursued at other airports.<sup>22</sup> Hertz reiterates its

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<sup>17</sup> Hertz submission dated 11 May 2010, section 2 and Hertz submission dated 12 May 2010, section 1

<sup>18</sup> Hertz submission dated 11 May, section 2

<sup>19</sup> Hertz submission dated 12 May, section 2

<sup>20</sup> Hertz submission dated 12 May, section 2

<sup>21</sup> WAC Submission, paragraph 5.17

<sup>22</sup> Footnote 4 of the WAC Submission

previous submissions that WAC's arguments on this point are incorrect as a matter of both fact and law.<sup>23</sup>

### 1.7 Net public benefits – cost savings to consumers

WAC argues that '[there] will be no cost savings to consumers as claimed by the Car Rental Majors'<sup>24</sup> and that any cost savings as a result of collective bargaining will not be passed on to consumers.<sup>25</sup> The Commission has previously recognised that, given the level of competition at the retail level, cost savings are likely to be reflected in lower prices for consumers.<sup>26</sup>

In any event, as matter of economic principle, irrespective of the competitiveness of the downstream market, any reduction to the marginal cost of providing car rental services at Perth Airport would necessarily lead to lower prices for consumers.

Frontier considers that:

- there is nothing in the RFP process that would be likely to decrease the marginal cost for the car rental operators relative to the existing terms and conditions at Perth Airport;<sup>27</sup> and
- in fact, the increase in the minimum gross turnover fee and the introduction of a minimum guarantee under the RFP process would increase these marginal costs and therefore increase prices paid by consumers.<sup>28</sup>

In contrast, collective bargaining will allow the parties to meaningfully engage and negotiate on all levels, including the gross turnover and minimum guarantee fees. To the extent that this results in lower marginal costs for the car rental operators it will result in lower prices for end consumers than under the RFP process.<sup>29</sup>

As a practical example of the principles outlined above, the collective bargaining group was able to negotiate, inter alia, lower turnover based fees than first proposed with the operator of Mackay Airport, clearly demonstrating the public benefit (in the form of lower marginal costs and therefore higher output and lower prices to consumers) that the process is able to generate.

### 1.8 Different prices on and off airports

WAC asserts that the car rental operators charge higher rates at airports than at other locations due to the inelastic demand of air travellers for car rental services and that these higher prices will be exacerbated by collective bargaining.<sup>30</sup>

Hertz agrees that on-airport car rental is to some extent a differentiated service offering to off-airport services and that customers may be willing to pay more at

<sup>23</sup> Hertz submission dated 11 May 2010, section 3 and Hertz submission dated 19 May 2010, section 3

<sup>24</sup> WAC Submission, paragraph 5.6

<sup>25</sup> WAC Submission, paragraphs 5.6 to 5.10

<sup>26</sup> Hertz submission dated 11 May 2010, section 4

<sup>27</sup> Frontier Economics report, section 5.2

<sup>28</sup> Frontier Economics report, section 5.2

<sup>29</sup> Frontier Economics report, section 5.2

<sup>30</sup> WAC Submission, paragraph 5.8

airports for the convenience of picking up or dropping off a car at the airport. However, Hertz faces strong competition in relation to the supply of both on and off-airport services. Accordingly, margins for all car rental services (whether differentiated by the convenience of on-airport pick/drop off or otherwise) are subject to competitive constraint. However, because on-airport car rental operators face higher input costs (due to monopoly pricing by the airport operator), it is to be expected that market prices for on-airport car rental services will tend to be higher than for the equivalent off airport service. This does not mean that on-airport margins are either uncompetitive or inefficient; rather the contrary is true.

WAC further argues that the *'drivers of prices for rental car services at Australian airports will be unchanged by any reduction in the costs of airport space'*.<sup>31</sup> Once again, we submit that any reduction in costs that lead to reduced marginal costs for car rental operators will lead to reduced prices for consumers of car rental services at airports.<sup>32</sup>

## **2. Redspot Submission**

### **2.1 Allocation of facilities based on market shares**

Redspot submits that collective bargaining will lead to the parties to the Notification negotiating with WAC for the allocation of facilities based on market share.<sup>33</sup> Hertz maintains that this assertion is unfounded and that implementation of a collective bargaining process does not mean that the process or outcome is not competitive.<sup>34</sup> Ultimately, all allocation decisions are at WAC's discretion.

In any event, the proposition that considering existing market share in making allocation decisions is economically inefficient has no obvious logic. The obvious relevance of existing market share to allocation decisions as between car rental operators is that it may provide a possible proxy for future requirements (ie because market share reflects existing demand for a particular operator's car rental services). This is a highly relevant consideration for the airport – there is obvious, arguably greater, potential for misallocation of available resources if no regard is had to existing demand conditions. Consideration of existing market share is not a mechanism for excluding entry or expansion by an operator such as Redspot. To the extent there is in fact scarcity of ready bays or counters, it is ultimately up to any particular car rental operator (whether part of a collective bargaining group or otherwise) to demonstrate that it has a superior commercial proposal than another operator – and the final allocation decision is at WAC's discretion.

### **2.2 'Underpriced' services at Perth Airport**

Redspot argues that facilities at Perth Airport are currently underpriced, that this is being taken advantage of by the parties to the Notification and that any reduction in prices that is collectively negotiated is not likely to be passed on to consumers.<sup>35</sup>

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<sup>31</sup> WAC Submission, paragraph 5.10

<sup>32</sup> See section 1.7 above

<sup>33</sup> Redspot Submission, paragraph 1 and 2

<sup>34</sup> Hertz submission dated 12 May 2010

<sup>35</sup> Redspot Submission, paragraph 4

There is no evidence presented by Redspot in support of this submission and its relevance is not immediately obvious. Ultimately, the real question is whether the collective bargaining process is preferable to the WAC's RFP process in determining the structure and level of future pricing of airport space for car rental services.

We reiterate our previous arguments that the WAC RFP process is unlikely to deliver efficient outcomes<sup>36</sup> – in fact, collective bargaining is more likely to promote allocative efficiency<sup>37</sup> and any reduction in fees that is collectively negotiated are likely to be reflected in lower prices for consumers.<sup>38</sup>

Indeed, even if Redspot were correct that the future base prices WAC is asking for may be commensurate with current prices at other airports (as noted above, an unsupported assertion made by Redspot)<sup>39</sup> this would say nothing about whether or not those prices were efficient.

### **2.3 Redspot commercially disadvantaged**

Redspot argues that it will be at a competitive disadvantage by not having the benefit of the knowledge of the information that will be shared between the parties to the Notification if collective bargaining were allowed by the Commission.<sup>40</sup>

As the Commission is aware, the members of the collective bargaining group have no objection either to Redspot's joining the collective bargaining group or with WAC disclosing to Redspot the commercial terms discussed with the members of the collective bargaining group in any collective process. The proposed collective bargaining group seeks genuine transparency in relation to this process. Given this, Redspot's submission on this points lacks credibility.<sup>41</sup>

More generally, we refer to our previous submissions on this issue.<sup>42</sup>

### **2.4 Allocation of facilities between car rental services and other services<sup>43</sup>**

We refer to section 1.4 above.

### **2.5 Collective bargaining at other Australian airports<sup>44</sup>**

We refer to section 1.5 above.

### **2.6 Negotiations at Mackay Airport**

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<sup>36</sup> Hertz submission dated 27 May 2010, section 2.2 and 23

<sup>37</sup> Hertz submission dated 27 May 2010, section 2.2

<sup>38</sup> See section 1.6 above

<sup>39</sup> Redspot Submission, paragraph 3

<sup>40</sup> Redspot Submission, paragraph 5

<sup>41</sup> Hertz submission dated 19 May 2010, section 2

<sup>42</sup> Hertz submission dated 12 May 2010

<sup>43</sup> Redspot Submission, paragraph 6

<sup>44</sup> Redspot Submission, paragraph 7



Redspot claims that the negotiations of the group at Mackay Airport led to reduced commission and turnover based fees that were in the operators' own best interests and maximise the charges payable by customers.<sup>45</sup>

On the contrary, as discussed in section 1.6 above, the Mackay example demonstrates the potential benefits to be gained from collective bargaining (vis-à-vis monopoly pricing) by reducing the marginal costs of the members of the collective bargaining group at Mackay airport relative to that originally proposed by the airport operator. This outcome is unambiguously good for consumers, as it is likely to lead to higher output and lower prices for car rental services.

## 2.7 Fee structures

Redspot points to the differences in business methods and rate structures offered by Redspot compared to the collective bargaining group as having the effect of reducing the amount of turnover based fees payable by the collective bargaining group.<sup>46</sup> We cannot see the relevance of this issue to the Commission's consideration of the Notification. Redspot is free to structure its fees any way it chooses, including structuring it in the same way as its competitors if it considers that to be the most commercially advantageous structure.

If you have any questions or require any further information, please do not hesitate to contact myself or Celesti Hodgman of our office.

Yours faithfully  
**MINTER ELLISON**

**Geoff Carter**  
**Partner**

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<sup>45</sup> Redspot Submission, paragraph 7 and 8

<sup>46</sup> Redspot Submission, paragraph 8

Restriction of Publication of Part Claimed

## CONFIDENTIAL ANNEXURE A

EXCLUDED FROM PUBLIC REGISTER

Restriction of Publication of Part Claimed

## CONFIDENTIAL ANNEXURE B -

EXCLUDED FROM PUBLIC REGISTER

Restriction of Publication of Part Claimed

## CONFIDENTIAL ANNEXURE C

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