Determination

Applications for authorisation

lodged by

Virgin Australia Airlines Pty Ltd,
Air New Zealand Limited and Others

in respect of

an airline alliance between the applicants

Date: 3 September 2013

Authorisation numbers: A91362 & A91363

Commissioners: Schaper
Rickard
Court
Walker

Summary

The ACCC grants conditional authorisation until 31 October 2018 to Virgin Australia and Air New Zealand to continue to give effect to an Australasian Airline Alliance Agreement, an associated Code Share Agreement and related agreements contemplated by the Australasian Airline Alliance Agreement (collectively, the Alliance).

Authorisation is subject to conditions which require the airlines to maintain at least an aggregate base level of capacity across the following routes:

- **Christchurch – Brisbane;**
- **Christchurch – Melbourne;**
- **Dunedin – Brisbane;**
- **Wellington – Brisbane;**
- **Queenstown – Brisbane;**
- **Auckland – Gold Coast.**

Rather than prescribe a minimum growth factor for these routes, the ACCC considers it appropriate to review the Applicants' capacity additions in light of actual demand growth over the next two years and may impose a growth factor at that time, if appropriate. This review will commence on 1 September 2015.

The conditions of authorisation also require the Applicants to provide specific data to the ACCC at the end of each scheduling season to assist the ACCC in assessing the Alliance's impacts on competition in the future. The ACCC will take this information into account when considering any application for re-authorisation from the Alliance parties.

On 8 March 2013, Virgin Australia and Air New Zealand Limited (the Applicants) lodged applications for authorisation to continue to give effect to an Australasian Airline Alliance Agreement, an associated Code Share Agreement and related agreements contemplated by the Australasian Airline Alliance Agreement (collectively, the Alliance).

The Alliance between Virgin Australia and Air New Zealand involves coordination of their international air passenger transport operations and related services between Australia and New Zealand (the trans-Tasman). The airlines' freight operations are outside the scope of the Alliance as are the Applicants' domestic networks, except to the extent that a particular domestic service is part of a connecting service across the trans-Tasman.

The ACCC previously granted conditional authorisation for the Alliance on 16 December 2010. While the ACCC recognised that the Alliance was likely to result in a number of public benefits, it was concerned that the Alliance would result in public detriment through its effect on competition on a number of trans-Tasman routes. Given the fine balance of the benefits and detriments, the ACCC imposed conditions of authorisation requiring the airlines to maintain a base level of capacity on certain routes and on the trans-Tasman as a whole.

In considering the current applications for authorisation, the ACCC has assessed the public benefits and detriments of the proposed conduct for which authorisation is sought (proposed conduct) on the basis that in the likely future without the Alliance:

- both Virgin Australia and Air New Zealand would continue to operate on the trans-Tasman as independent competitors;
- Virgin Australia's trans-Tasman operations would be significantly more limited than its key competitors (including Air New Zealand) in terms of schedule depth and breadth;
- Virgin Australia is likely to review the viability of certain trans-Tasman routes;
- Air New Zealand may review the operation of certain trans-Tasman services which rely on the combined feed and presence of both Alliance partners;
- Air New Zealand is likely to be at some competitive disadvantage to the Qantas-Group/Emirates alliance due to its weaker sales presence in Australia and more limited access to the domestic market in Australia; and
- the Applicants would have limited commercial incentives to enter into alternative bilateral arrangements with each other in the absence of the Alliance.

At a broad level, the ACCC notes that the Alliance links Virgin Australia's domestic Australian network and sales presence with Air New Zealand's domestic New Zealand network and sales presence to contribute to the formation of a second integrated Australasian network which in turn would facilitate a stronger competitive response from the Qantas-Group/Emirates alliance.

Public benefits

The ACCC considers that in the two years the Alliance has been in operation it has resulted in material public benefits in the form of enhanced products and services (particularly through new frequencies) and the promotion of competition on the trans-Tasman routes. In addition the ACCC considers that the Alliance has resulted in small public benefits in the form of cost savings and efficiencies and the stimulation of tourism.

The ACCC accepts that due to the limited period the Alliance has been in operation there may be some public benefits that are yet to be fully realised.

In light of this, the ACCC considers that moving forward the Alliance is likely to result in:

- material public benefits in the form of enhanced products and services. These products and services are comprised of loyalty program benefits, lounge access, and new frequencies (each of which the ACCC considers will be material benefits going forward) and increased online connections and better schedule spread (which the ACCC considers will result in small public benefits going forward). Increased access to existing frequencies may also form a public benefit, however based on the evidence available, the ACCC cannot conclude the magnitude of this benefit;
- material public benefits in the form of the promotion of competition on trans-Tasman routes, particularly in relation to the business traveller segment. The

ACCC considers that this benefit is likely to manifest in a competitive response from the Qantas Group to the enhanced products and services of the Alliance on these routes. To a lesser extent the ACCC considers that the Alliance is likely to result in similar benefits in the domestic Australian market but is unable to determine the extent to which the Alliance (as opposed to other factors) will contribute to the increased competitiveness of Virgin Australia within Australia;

- small public benefits in the form of cost savings and efficiencies. These small benefits are likely to be derived from joint procurement, co-location of certain functions, utilisation of common resources and the removal of double marginalisation. The ACCC also considers that operational optimisation and high load factors may deliver efficiencies for the Alliance. However, based on the evidence available, the ACCC cannot conclude that high load factors are a likely benefit of the Alliance; and is unable to reach a conclusion on the magnitude of the benefit resulting from operational optimisation; and

- small public benefits in the form of stimulating tourism spend in Australia.

Taken together, the ACCC is satisfied that the Alliance would, or would be likely to, result in material public benefits.

Public detriments

The ACCC has assessed the public detriments that arise or are likely to arise as a result of the Alliance having regard to two forms of competitive harm: unilateral and coordinated effects.

Unilateral effects

In assessing unilateral effects, the ACCC has had regard to the fact that in the likely future without the Alliance, Virgin Australia's trans-Tasman offering would be significantly more limited than its key competitors and therefore is unlikely to be a strong rival to the offerings of the Qantas-Group/Emirates alliance and Air New Zealand (particularly on the business orientated routes which Virgin Australia has indicated are most likely to be negatively impacted absent the Alliance). In light of this, the ACCC considers that the Alliance is unlikely to result in significant public detriment through its effect on competition on the major trans-Tasman routes between:

- Auckland-Sydney, Auckland-Melbourne and Auckland-Brisbane;

- Wellington-Sydney and Wellington-Melbourne; and

- Christchurch-Sydney

in spite of the fact that the Alliance potentially reduces the number of Australian and New Zealand designated airlines from three to two on these routes. The ACCC considers that competition will not be substantially less in the future with the Alliance on these routes as compared to the likely future without the Alliance. The Alliance is likely to face sufficient competitive constraint from the Qantas/Group-Emirates alliance and fifth freedom carriers where applicable on these routes going forward.

On the minor routes between:

- Auckland-Adelaide, Auckland-Cairns, Auckland-Perth and Auckland-Sunshine Coast;
- Queenstown-Sydney and Queenstown-Melbourne;
- Christchurch-Gold Coast;
- Rotorua-Sydney;
- Dunedin-Sydney; and
- Dunedin-Melbourne

the ACCC considers that there are factors (such as the competitive constraint posed by the Qantas Group and/or the likely presence of only one Alliance partner on a thin route in the future without the proposed conduct) which mean that the Alliance is unlikely to result in significant public detriment.

On the remaining routes set out below, the ACCC considers that the Alliance is likely to result in public detriment by giving the airlines an increased ability and incentive to unilaterally reduce capacity (to increase air fares) compared to the future without the Alliance:

- Christchurch-Melbourne and Christchurch-Brisbane;
- Wellington-Brisbane;
- Queenstown-Brisbane;
- Auckland-Gold Coast; and
- Dunedin-Brisbane.

Together, these routes account for around 16% of trans-Tasman capacity for the year ending February 2013.

Having regard to the Applicants' submissions after the draft determination regarding the Dunedin – Melbourne/Sydney routes the ACCC now considers that bundling these routes with the Dunedin–Brisbane route will provide little additional flexibility for the Applicants. As the ACCC identified in the draft determination, due to the extremely thin nature of these routes, and given that these routes are likely to remain monopoly routes, such that it is extremely unlikely, absent the Alliance, that both Virgin Australia and Air New Zealand would compete on these routes, the public detriments arising from the Alliance are likely to be minimal. For these reasons, the Dunedin – Melbourne/Sydney routes are unlikely to warrant a standalone condition and the ACCC has removed them from the capacity condition proposed in the draft determination.

Coordinated effects

In assessing the coordinated effects, the ACCC has had regard to the fact that the Alliance creates a market structure on the trans-Tasman that increases the risk of coordination by the Qantas-Group/Emirates alliance and the Virgin Australia/Air New

Zealand Alliance over the longer term. Absent the Alliance, the ACCC considers that Virgin Australia would be a third, and smaller, operator on the trans-Tasman, with potentially divergent incentives that could disrupt coordination. Through removing Virgin Australia as an independent competitor on the trans-Tasman, the ACCC considers that the Alliance has increased the risk of coordination, which results in public detriment. However, the extent of the public detriment arising as a result of an increased risk of coordinated conduct is uncertain. Going forward, the ACCC intends to closely monitor the conduct of airlines operating on the trans-Tasman to assess whether coordination may be occurring.

Overall, the ACCC considers that the proposed conduct would, or would be likely to, result in public detriments by:

- giving the Alliance an increased ability or incentive to unilaterally reduce or limit capacity (in order to increase air fares) on certain trans-Tasman routes; and

- increasing the risk of coordinated conduct over the longer term on the trans-Tasman.

Conclusion of public benefits and detriments

After weighing the public benefits and detriments discussed above, the ACCC has reached the view that the proposed conduct, subject to the conditions outlined, is likely to result in material public benefit that would outweigh the detriment to the public constituted by any lessening of competition that would result or would be likely to result from the proposed conduct. The ACCC notes that, as was the case in the 2010 authorisation, the public benefits and detriments likely to result from the Alliance are finely balanced.

Conditions

The Competition and Consumer Act 2010 allows the ACCC to grant authorisation subject to conditions.

In order to address the concern that the Alliance may unilaterally reduce or limit capacity on certain routes, the ACCC is imposing conditions requiring the airlines to maintain at least an aggregated base level of capacity on the routes of concern. Following the provision of further information, including confidential data, by the Applicants after the draft determination, the ACCC considers that, rather than initially prescribing a minimum growth factor, it is appropriate to review the Applicants' capacity additions in light of actual demand growth over the next two years. The review will enable the ACCC to consider whether increases in the minimum required capacity are warranted.

The ACCC is also imposing conditions requiring the Applicants to provide information on key aspects of performance of the Alliance at the end of each scheduling season to assist the ACCC in assessing coordinated and unilateral effects in the future.

The airlines have sought unconditional authorisation for five years. In its draft determination the ACCC proposed to conditionally authorise the Alliance for three years and that the routes subject to a capacity condition would have a growth factor imposed. Following the draft determination the Applicants made further submissions in relation to the importance of the five year term. The Applicants submit that a longer period is necessary in order to enable them to fully implement Alliance products on the trans-

Tasman and do so with investment certainty. In light of these submissions, and having regard to the confidential information regarding route performance, the ACCC considers that the longer period with a review is appropriate. Accordingly, the ACCC grants conditional authorisation until 31 October 2018.

Contents

Glossary

2010 alliance	means the Australasian Airline Alliance Agreement, an associated Code Share Agreement and related agreements contemplated by the Australasian Airline Alliance Agreement in relation to air passenger services between Australia and New Zealand as authorised by the ACCC on 16 December 2010.
ACCC	The Australian Competition and Consumer Commission
Act	*Competition and Consumer Act 2010* (Cth)
Air New Zealand	means Air New Zealand Limited
Alliance	means the Australasian Airline Alliance Agreement between Air New Zealand and Virgin Australia, an associated Code Share Agreement and related agreements contemplated by the Australasian Airline Alliance Agreement in relation to air passenger services between Australia and New Zealand the subject of the applications for authorisation A91362 and A91363.
ANZ ASA	the Air Services Agreement between the Government of Australia and the Government of New Zealand made on 8 August 2002 at Auckland
Applicants	means Virgin Australia and Air New Zealand
ASA	Air Services Agreement
ASK	available seat kilometres
BITRE	Bureau of Infrastructure, Transport and Regional Economics
CIAL	Christchurch International Airport Limited
codeshare	arrangements involving the assignment of one airline's designator code to a flight operated by another airline
Department	Australian Government Department of Infrastructure and Transport
DFAT	Australian Government Department of Foreign Affairs and Trade
DIAC	Australian Government Department of Immigration and Citizenship
DIAL	Dunedin International Airport Ltd
Emirates	Emirates Airlines, a Dubai Corporation established by Decree No. 2 of 1985 (as amended)
FFC	fifth freedom carrier, that is an airline operating services between two foreign countries on flights which commence or end in the airline's home country
FSA	full service airline
free sale	a type of codeshare where the marketing airline effectively only pays for the seats it sells

fare schedule	refers to a table of airfares offered for particular routes based on fare class
Game Change strategy	the strategy adopted by Virgin Australia since May 2010 in relation to positioning the airline and its related airlines in the domestic Australian market and its broader network. The strategy is designed to attract higher yield corporate and business passengers while remaining attractive to leisure passengers.
IASC	International Air Services Commission
IATA	International Air Transport Association
interlining	interlining involves the carriage of passengers and/or freight between two points using the services of more than one airline under an arrangement which typically involves baggage check through and the honouring of tickets between airlines
Jetstar	Jetstar Airways Pty Ltd
KWSG	Key Wellington Stakeholders Group
LAN	LAN Airlines
LCC	low cost carrier
load factors	load factors measure the percentage of seats filled on an aircraft on any given route. This is derived from dividing the number of passengers travelled by the number of seats available
metal neutrality	means an alliance in which each member airline is incentivised to treat all passengers as if they were flying on the airline's own network regardless of which member airline they are actually flying on, such that member airlines become neutral in their marketing, pricing and capacity decisions as to the choice customers make between flying on each member's aircraft (metal)
Network Alliance Routes	comprises any sector between a point in Australia and a point in New Zealand (Trans-Tasman Sectors) plus any domestic Australian or New Zealand sectors connecting to a Trans-Tasman Sector as part of an international itinerary.
New World Carrier	means a low cost, high value airline that aims to attract a broader cross-section of passengers than the traditional LCC model, through leveraging the airline's low cost foundations and adding valuable new products which appeal to higher yielding passengers
NS	means the scheduling season for Northern Summer from 1 April to 31 October of any year
NW	means the scheduling season for Northern Winter from 1 November to 31 March of any year
NZ Airports	the New Zealand Airports Association
online connection	a passenger itinerary of two or more flight segments where connections are made between flights of the same airline or

	its codeshare partners
pre-Alliance year	the period from 1 November 2009 to 31 October 2010
proposed conduct	the conduct for which authorisation is sought
QAC	Queenstown Airport Corporation
Qantas	Qantas Airways Limited
Qantas Group	Qantas and its controlled entities
Qantas-Group/Emirates alliance	Alliance between Qantas and Emirates which is the subject of the ACCC's Determination-Applications for Authorisation A91332-A91333 lodged by Qantas and Emirates, 27 March 2013
RASK	means revenue per available seat kilometre
RIA	Rotorua International Airport
SAM	Single Aviation Market
special prorate agreement	is a reciprocal agreement under which each airline makes passenger inventory available at a favourable rate for sale as an interline ticket
tactical fares	refers to fares that are provided as a short term response to competitors' offerings and/or lower than expected demand
TNZ	Tourism New Zealand
trans-Tasman Sector	comprises any sector between a point in Australia and a point in New Zealand
Tribunal	the Australian Competition Tribunal
Virgin Australia	means Virgin Australia Airlines Pty Ltd, Virgin Australia Airlines (NZ) Ltd, Virgin Australia Airlines (SE Asia) Pty Ltd and Virgin Australia International Airlines Pty Ltd
Virgin Blue	Virgin Blue Airlines Pty Ltd, Pacific Blue Airlines (Aust) Pty Ltd, Pacific Blue Airlines (NZ) Limited
VFR	Visiting Friends and Relatives
Year 0	means the period from 1 November 2010 to 31 October 2011
Year 1	means the period from 1 November 2011 to 31 October 2012

The applications for authorisation

1. On 8 March 2013 Virgin Australia Airlines Pty Ltd, Virgin Australia Airlines (NZ) Ltd, Virgin Australia Airlines (SE Asia) Pty Ltd and Virgin Australia International Airlines Pty Ltd (together **Virgin Australia**) and Air New Zealand Limited (**Air New Zealand**) (together the **Applicants**) lodged applications for authorisation A91362 & A91363 with the Australian Competition and Consumer Commission (**ACCC**) pursuant to subsections 88(1A) and 88(1) of the *Competition and Consumer Act 2010* (Cth) (the **Act**).

2. Authorisation is a transparent process where the ACCC may grant protection from legal action for conduct that might otherwise breach the Act. The ACCC may 'authorise' businesses to engage in anti-competitive conduct where it is satisfied that the public benefit from the conduct outweighs any public detriment. The ACCC conducts a public consultation process when it receives an application for authorisation, inviting interested parties to lodge submissions outlining whether they support the application or not. On 10 July 2013, the ACCC issued a draft determination[1] proposing to grant authorisation, subject to conditions, to the Applicants to continue to give effect to an Australasian Airline Alliance Agreement, an associated Code Share Agreement and related agreements contemplated by the Australasian Airline Alliance Agreement (collectively, **the Alliance**) for a period of three years. A conference was not requested in relation to the draft determination.

The conduct

3. The Applicants seek authorisation for five years to continue to give effect to the Alliance). The Applicants also seek authorisation to make any further associated code share agreement and related agreements which are contemplated by the Australasian Airline Alliance Agreement. The application extends to the making of agreements to the extent that those agreements give effect to the Australasian Airline Alliance Agreement. The conduct for which authorisation is sought is referred to as the **proposed conduct**.

4. The Alliance applies to 'Network Alliance Routes' and 'trans-Tasman sectors'. The trans-Tasman sectors are any non-stop flights between a point in Australia and a point in New Zealand, including when the ultimate destination of the service is another point in Australia, New Zealand or another country, and are a subset of Network Alliance Routes. The Network Alliance Routes comprise the trans-Tasman sectors plus any domestic Australian or New Zealand sectors connecting to a trans-Tasman sector as part of an international itinerary.

5. In relation to trans-Tasman sectors, the Alliance provides for the Applicants to cooperate with each other in relation to:

    - the setting of fares, tariffs, rates, and charges;

    - coordination of networks, schedules and routes;

1 Subsection 90A(1) requires that before determining an application for authorisation the ACCC shall prepare a draft determination.

- revenue sharing; and

- alignment of products such as fare rules, baggage handling processes, on board food and beverage, and in-flight entertainment.

6. In relation to the Network Alliance Routes (which also includes trans-Tasman sectors), the Alliance provides for the Applicants to cooperate with respect to:

   - pricing, tariffs, sales and marketing, and revenue management;
   - fare products (including conditions of carriage and the development of new fare products);
   - entering into freesale codeshare agreements[2];
   - entering into special prorate agreements[3];
   - entering into a Frequent Flyer Program Implementation Agreement which provides for reciprocal frequent flyer benefits; and
   - entering into a Lounge Sharing Agreement which provides for reciprocal lounge access.

7. The Alliance provides for the Applicants to coordinate their non-flying operations on the Network Alliance Routes in relation to:

   - joint purchasing of goods and services, including in relation to ground handling, joint fuel handling, aircraft maintenance, real estate and commercial leasing, information technology and services, catering services and in-flight consumer products;
   - regulatory cooperation;
   - the co-location of airport operations;
   - coordination of information technology; and
   - reciprocal employee travel benefits.

8. Freight services, including freighter operations and cargo belly space on scheduled flights, are explicitly excluded from the Alliance and are not covered by the authorisation application.[4]

9. The Applicants' domestic Australian and New Zealand networks are outside the scope of the Alliance, except to the extent that a particular service is part of a connecting service across the Tasman. The Applicants' non-trans-Tasman networks are also outside the scope of the Alliance to the extent not already mentioned.

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[2] Freesale codeshare refers to a direct sale of seats on the other carrier's aircraft with no obligation to pre-purchase any volume of seats.

[3] A special prorate agreement is a reciprocal agreement under which each party makes inventory available at a favourable rate for sale as an interline ticket.

[4] Virgin Australia and Air New Zealand, Response to Information Request, 7 May 2013.

The 2010 authorisation

10. On 16 December 2010, the ACCC granted conditional authorisation to Virgin Blue (now Virgin Australia) and Air New Zealand in relation to an Australasian Airline Alliance Agreement, an associated Code Share Agreement and related agreements contemplated by the Australasian Airline Alliance Agreement in relation to air passenger services between Australia and New Zealand (**the 2010 Alliance**).

11. The ACCC considered that the 2010 Alliance was likely to result in material public benefits in the form of:

    - enhancement of the Applicants' products and service offering (including increased access to existing frequencies, increased online connection options, better schedule spread, enhanced value added services and new frequencies) and associated increased consumer choice;
    - potential for lower fares as a result of cost savings and efficiency improvements through removal of double marginalisation and higher load factors;
    - promotion of competition in the business traveller segment of the trans-Tasman market; and
    - stimulation of tourism.

12. The ACCC considered that the 2010 Alliance was likely to result in public detriment through its effect on competition on a number of routes in the market for trans-Tasman air passenger services.

13. Specifically, the ACCC was of the view that the 2010 Alliance raised material competition issues on the trans-Tasman routes to and from Wellington (Wellington-Sydney, Wellington-Melbourne and Wellington-Brisbane) as well as Dunedin-Brisbane. Together, these routes accounted for 12% of trans-Tasman passenger traffic in April 2010. The ACCC considered that the effect of the Alliance on Auckland-Brisbane (13%) and Queenstown-Sydney (1%) routes was uncertain.

14. The ACCC decided to impose conditions to address the identified competition concerns. Broadly speaking, the conditions required the Applicants to maintain a base level of capacity, subject to a growth factor, on the routes of concern and across the trans-Tasman for the term of the authorisation. The growth factor required the Applicants to increase capacity seasonally on each of the routes of concern in line with the most recent economic growth (GDP) or growth in trans-Tasman passenger demand (whichever was greater).

15. The ACCC concluded that given the fine balance of benefits and detriments, and the significant role of conditions in that balance, that it was appropriate to review developments after three years and granted conditional authorisation until 31 December 2013.

Variations to conditions of authorisation

16. In response to requests from the Applicants following force majeure events, the ACCC has approved a number of variations to the capacity condition since authorisation was granted in 2010:

- on 27 July 2011 the ACCC varied the capacity conditions to take into account the effect on demand following the Christchurch earthquake. The variation permitted the Alliance to fly 97% of the total trans-Tasman base year capacity for the Northern Summer (**NS**) 2011 season and 94.4% of the total trans-Tasman base year capacity for the Northern Winter (**NW**) 2011 season;
- on 4 August 2011 the ACCC varied the capacity conditions to take into account the effect of the Chilean volcanic ash cloud. The variation permitted the Alliance to fly 95.9% of the total trans-Tasman base year capacity for the NS 2011 season (a 1.1% reduction over that permitted by the Earthquake reduction); and
- on 31 May 2012 the ACCC varied the capacity conditions to take into account the ongoing effects on demand following the Christchurch earthquake and subsequent aftershocks. The variation permitted the Alliance to fly 95.8% of the total trans-Tasman base year capacity for the NS2012 and NW2012 seasons.

Implementation of the Alliance to date

17. Authorisation of the Alliance came into effect on 7 January 2011. At the time of the Applicants lodging the current application for authorisation, the Alliance had been operational for 18 months.

18. The Applicants submit that since the 2010 authorisation came into effect they have:

- commenced code share sales on Network Alliance Routes from 26 July 2011;
- implemented joint pricing on code share routes for travel from 26 July 2011;
- commenced lounge and frequent flyer reciprocity from 26 July 2011;
- begun aligning product offerings, including meal specifications on trans-Tasman flights, the alignment of child and infant fares, age policies, check-in policies and baggage policies and fees;
- implemented a revenue share model from 1 August 2011;
- commenced joint scheduling from April 2011 with comprehensive network changes starting on 30 October 2011;
- commenced joint promotion of the Alliance and its destinations through the Joint Sales Team, which has been established under the Alliance to deal with Alliance sales and marketing planning and coordination; and
- complied with the conditions of authorisation.

19. The Applicants submit that while key aspects of the Alliance have been implemented under the 2010 authorisation, reauthorisation will allow the Applicants to:

- continue the delivery of public benefits that have been realised to date such as increased dual coded frequencies and the public benefits flowing from lounge and frequent flyer reciprocity; and
- enhance and expand the public benefits achievable as a result of the Alliance.

20. The Applicants submit that reauthorisation will enable them to realise more benefits from the Alliance as a result of Virgin Australia's recent migration to an improved IT system, SabreSonic, in January 2013. The migration to the new IT system will allow the Applicants to achieve a greater level of compatibility and integration between their IT infrastructures and enable Virgin Australia to support settlement of dual destination itineraries. Virgin Australia is now able to adopt consistent, streamlined industry standard (**IATA**) practices and processes. As part of its IT improvement, Virgin Australia now operates under a single IATA designator.

The Applicants

Virgin Australia[5]

21. The Virgin Australia Group commenced operations in Australia in August 2000 as a low cost carrier (**LCC**) under the 'Virgin Blue' brand. Virgin Australia currently operates services under the 'Virgin Australia' brand and the 'Virgin Samoa' brand (a joint venture with the Samoan Government).

22. Since its entry 13 years ago, Virgin Australia has made a number of changes to its business model in order to take account of changing conditions in the Australian (and global) aviation industry and to pursue opportunities to increase its share of passengers and its profitability.

23. In late November 2005, Virgin Blue (as it was then) re-defined its business model and announced its move towards becoming a New World Carrier (**NWC**). A NWC is a low cost, high value airline that aims to attract a broader cross-section of passengers than the traditional LCC model, through leveraging the airline's low cost foundations and adding valuable new products which appeal to higher yielding passengers.

24. Under this strategy Virgin Australia was able to continue low cost operations while strengthening yields and profitability. As part of the NWC strategy, it introduced additional initiatives to enhance its product offering including a frequent flyer program (Velocity), airport lounges, self-check-in kiosks, premium economy, Corporate Plus fares and Blue Holidays. Virgin also expanded its network reach by purchasing new aircraft and adding new destinations to its network as well as commencing interlining arrangements with other airlines.

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[5] The information in this section is sourced from the Applicants' submission in support of authorisation applications A91362-A91363, Annexure B.

The ‘Game Change’ strategy

25. Since May 2010, Virgin Australia has pursued its ‘Game Change’ strategy, designed to attract higher yield corporate and business passengers while remaining attractive to leisure passengers. Virgin Australia has also reconfigured aircraft cabins to cater for business class passengers.

26. The strategy is intended to enable Virgin Australia to match Qantas’s offers in the domestic Australian market and challenge Qantas across more market segments by improving Virgin Australia’s ‘network and product in order to expand its passenger base, providing enhanced choice and competition for all Australian passengers’.[6]

27. On 4 May 2011, the Virgin Australia name and brand was introduced for the airline’s domestic operations as part of its Game Change strategy. The brands Virgin Blue, Pacific Blue and V Australia were replaced by the single brand Virgin Australia and Polynesian Blue was renamed Virgin Samoa.

28. Virgin Australia operates services to 34 Australian and 17 international destinations including the USA, United Arab Emirates, New Zealand, Indonesia, Thailand, Papua New Guinea, Fiji, Samoa, Solomon Islands, Tonga, Vanuatu and the Cook Islands.

29. Virgin Australia has sought to match Qantas’s offer on international routes to and from Australia by developing a virtual international network through a series of alliances with partner international airlines. Virgin Australia has established alliances with Air New Zealand, Etihad Airways, Delta Air Lines and Singapore Airlines. Each of these alliances has been authorised by the ACCC.

30. Through this network, Virgin Australia is able to connect passengers to Europe via the Middle East and Singapore, to destinations throughout Asia and onwards to India, Africa and the Middle East, to numerous cities within the US and beyond to Canada and Mexico and to a number of trans-Tasman frequencies and destinations.

31. Virgin Australia has continued to expand its services to new domestic and regional leisure destinations including the introduction of services to Ayers Rock (Uluru), and increases in the number of services to Hamilton Island and Queenstown. More recently, Virgin Australia has sought to expand its corporate and government travel offering through the acquisition of Skywest Airlines.

32. Virgin Australia has also sought to expand its domestic Australian operations by acquiring a 60% interest in Tiger Airways Australia Pty Ltd.

33. For the year ending 30 June 2012, Virgin Australia reported revenue of $3,919.5 million. Virgin Australia’s profit before tax for the year ending 30 June 2012 was $82.5 million.[7]

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[6] Virgin/Air New Zealand, Submission in Support of Application, 8 March 2013, Annexure B, p. 2.

[7] Virgin Australia, Annual Report 2012, p.3.

Air New Zealand[8]

34. Air New Zealand is New Zealand's national flag carrier, offering air services in New Zealand and internationally. It also operates business units and subsidiaries providing engineering, ground handling services, aircraft interior design, and domestic and international cargo services.

35. Air New Zealand[9] operates:

- over 500 domestic New Zealand services per day to 26 destinations;
- services on 18 trans-Tasman routes at various times throughout the year with codeshare services operated by Virgin Australia on a further four routes;
- services to Rarotonga, Fiji, Vanuatu, Samoa, Tahiti, Noumea, Norfolk Island, Tonga and Niue in the Pacific Islands; and
- twice daily services to London and Los Angeles and services to other international ports in the US, Canada, Japan, China, Hong Kong and Indonesia.

36. Air New Zealand has been a member of the Star Alliance since March 1999 and has code share agreements with several Star Alliance members including United Airlines, Air Canada, Continental and Lufthansa. In addition, Air New Zealand also has code share or partnering arrangements with Virgin Atlantic, Etihad Airways and a number of Pacific carriers.

37. For the year ending 30 June 2012, the Air New Zealand Group reported revenue of $NZ 4,483 million. Air New Zealand's profit before tax for the year ending 30 June 2012 was $NZ94 million.[10]

Background

The aviation industry

International aviation regulation

38. The international airline industry is highly regulated. The 1944 Convention on International Civil Aviation established the principle that each country has exclusive sovereignty over its airspace. This principle continues to guide the regulatory framework today.

39. International air transport cannot occur unless it is specifically authorised pursuant to a government to government bilateral air services agreement (**ASA**).

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8 The information in this section is sourced from Virgin Australia & Air New Zealand's submission in support of authorisation applications A91362-A91363, Annexure B.

9 Together with its wholly owned subsidiaries Eagle Airways, Mount Cook and Air Nelson.

10 Air New Zealand, Annual Financial Results 2012, p. 2.

40. An ASA specifies the terms and conditions of airline activity between two countries. An ASA may indicate the destinations that can be served in a particular country, the permitted frequencies per week and any rights to operate via or beyond to third countries. Typically, the rights granted under an ASA can only be exercised by designated carriers of the countries that are parties to them.

41. An Open Skies Agreement is one form of ASA between two countries. In essence, it is an agreement which provides minimal (or no) restrictions on the ability of the airlines of two countries to operate services between countries.

Air services agreement between Australia and New Zealand

42. The Australian Government Department of Infrastructure and Transport (the **Department**) submits that the Australia/New Zealand air services market is one of the most open in the world and notes that the Agreement between the Government of Australia and the Government of New Zealand relating to Air Services (the **ANZ ASA**), made at Auckland on 8 August 2002 has no restrictions on capacity, frequency or routes that airlines of either country can operate to, within or beyond the two countries.

43. The ANZ ASA provides for eligible airlines to be authorised as Single Aviation Market (**SAM**) airlines. In order to operate services in the SAM, carriers must meet the following criteria:

    - at least 50% ownership and effective control by Australian and/or New Zealand nationals;
    - at least two-thirds of the Board members are Australian and/or New Zealand nationals;
    - the Chairperson of the Board is an Australian or New Zealand national;
    - the airline's head office is in Australia or New Zealand; and
    - the airline's operational base is in Australia or New Zealand.

44. Under the ANZ ASA, Australian and New Zealand airlines can also continue to be designated using the incorporation and principal place of business criteria.[11]

45. In conjunction with SAM arrangements, the mutual recognition of safety and operational regulatory approvals streamlines airlines' flying within the SAM.

46. Section 2 of the Annex to the ANZ ASA provides for ninth-freedom rights to airlines that are authorised as SAM airlines, and allows them to operate both international services between, and domestic services within, either country with full traffic rights.

[11] Carriers designated using the incorporation and principle place of business criteria are not able to operate within the domestic markets of the other country, although they have the same operating access as SAM airlines in terms of operating between the two countries.

Trans-Tasman airline operations

47. New Zealand is one the busiest travel destinations for Australians. Table 4.1 below shows the number of passengers travelling between Australia and New Zealand based on uplift/discharge data.

Table B.1 Australia-New Zealand passenger numbers[12]

Year ended June	Number of passengers	Percentage change from previous year
2012	5,733,220	1.4
2011	5,646,170	1.9
2010	5,404,839	4.8
2009	5,156,875	-0.3
2008	5,173,083	2.7
2007	5,036,228	3.3
2006	4,873,461	0.5
2005	4,850,699	13.1
2004	4,287,516	17.7
2003	3,642,898	3.7
2002	3,514,281	-0.3
2001	3,524,777	15.8
2000	3,044,538	10.3

Airlines

48. Air New Zealand, Virgin Australia, Qantas and Jetstar operate on the trans-Tasman as SAM airlines. As such they do not face regulatory restrictions on the trans-Tasman and in reciprocal domestic markets.

49. The ACCC acknowledges that airlines operating on the trans-Tasman may face barriers in the form of restricted access to landing slots at relevant airports. However, the ACCC understands that generally airports relevant to the trans-Tasman are not currently slot constrained so this is unlikely to act as a restriction.[13]

50. Air New Zealand operates the most frequencies across the widest range of trans-Tasman routes. Specifically, Air New Zealand operates on 18 trans-Tasman routes at various times throughout the year plus a further four routes through codeshare with Virgin Australia.[14]

51. Virgin Australia operates 71 frequencies on 14 routes.

52. The Qantas Group operates services on a large number of routes across the trans-Tasman. Qantas operates services between:

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12 Sourced from BITRE, *International Airline Activity Report*

13 The ACCC acknowledges that Sydney international airport faces slot constraints that may result in increased barriers to entry for an airline seeking to fly between Sydney and ports in New Zealand – see The Australian Government and Government of NSW, *Joint Study on aviation capacity for the Sydney region,* 2 March 2012.

14 Virgin/Air New Zealand, Submission in Support of Application, 8 March 2013, Annexure C, pg 12.

i. Sydney/Melbourne/Brisbane and Auckland;

ii. Sydney/Melbourne and Wellington;

iii. Sydney/Melbourne and Queenstown;

iv. Sydney and Christchurch; and

v. Perth and Auckland.[15]

53. Jetstar operates services between:

vi. Gold Coast and Auckland;

vii. Gold Coast/Melbourne/Sydney and Christchurch; and

viii. Melbourne/Sydney and Queenstown.[16]

54. Jetstar also operates New Zealand domestic services which it commenced in June 2009.

55. Emirates operates on the trans-Tasman as a fifth freedom carrier (**FFC**), with services from Dubai-Sydney/Melbourne/Brisbane-Auckland and from Dubai-Bangkok-Sydney-Christchurch. Emirates operates its trans-Tasman services in the scheduling window that currently exists around its Australia-Dubai services. Emirates submits that this scheduling window constrains its ability to add further capacity on the trans-Tasman and limits its ability to add trans-Tasman services on new routes, since its wide bodied aircraft cannot land at other airports in New Zealand, including Wellington Airport.[17]

56. The other carriers operating on the trans-Tasman are FFCs LAN Airlines (**LAN**) and China Airlines.

57. China Airlines operates three weekly A330-300 services from Taipei-Brisbane-Auckland. It also began operating four weekly A330-300 services from Taipei-Sydney-Auckland in October 2012. The ACCC understands that China Airlines operates its trans-Tasman services in the scheduling window around its services between Australia and Taipei.

58. LAN operates six weekly A340-300 services between Sydney and Auckland. These flights are an extension of LAN's services between Santiago and Auckland.

59. Qantas offers codeshare services on the LAN operated flights to Santiago via Auckland and also for destinations beyond Santiago in South America. LAN also codeshares on Qantas' three return services per week from Sydney to Santiago.[18] The ACCC does not consider that these arrangements act to significantly constrain competition between the carriers on the trans-Tasman because (from Qantas' perspective) they are focused on providing services to South America.

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15 To begin operating in December 2013 – January 2014.

16 Virgin Australia & Air New Zealand, Submission in Support, 8 March 2013, Annexure D, p. 17.

17 ACCC, Determination in relation to applications by Qantas Limited and Emirates, 27 March 2013 at [471].

18 Qantas, *Qantas Launches Santiago Flights*, http://www.qantas.com.au/travel/airlines/media-releases/mar-2012/5380/global/en (Last retrieved 5 June 2013).

60. The ACCC notes that the decision for a FFC to operate services on the trans-Tasman as an extension of its international services to Australia is typically opportunistic and linked to the carrier's broader network considerations. One consequence of this is that, just as it may be opportunistic for a FFC to enter a Trans-Tasman route, it equally may be opportunistic to exit the route in response to a change in demand or supply conditions elsewhere in a FFC's network. This helps explains the pattern of entry and exit by FFCs on the trans-Tasman over the last decade.

Trans-Tasman routes

61. The top four trans-Tasman routes operating throughout the year accounted for approximately 65% of trans-Tasman capacity and the top ten routes accounted for approximately 88% of trans-Tasman capacity in the year ending 31 December 2012.[19] In order of size based on capacity, these routes are:

- Auckland-Sydney
- Auckland-Melbourne
- Auckland-Brisbane
- Christchurch-Sydney
- Wellington-Sydney
- Auckland-Gold Coast
- Christchurch-Melbourne
- Christchurch-Brisbane
- Wellington-Brisbane
- Wellington-Melbourne
- Auckland-Perth
- Queenstown-Sydney
- Auckland-Cairns
- Christchurch-Gold Coast
- Auckland-Adelaide
- Dunedin-Brisbane
- Rotorua-Sydney

[19] Traffic carried via Australia to/from New Zealand is not recorded.

62. There are also seasonal routes from Queenstown to Melbourne, Brisbane and the Gold Coast, and from Dunedin to Sydney and Melbourne.

Submissions received by the ACCC

63. The ACCC tests the claims made by the Applicants in support of an application for authorisation through an open and transparent public consultation process.

Prior to the draft determination

64. The ACCC sought submissions from over 70 interested parties potentially affected by the application, including competitors, airports, regulators and industry groups. A summary of the public submissions received is set out below.

The Applicants

65. Broadly, the Applicants submit that the core rationale for the Alliance is to increase the number of passengers travelling on the Applicants' combined services through the development of an integrated Australasian network offering enhanced products and services including a greater choice of flights, better online connections, better schedule options and enhanced loyalty programs and lounge benefits.

66. They submit that customers now have the choice to access an Alliance product with better frequencies, pricing, frequent flyer value and a more integrated network than either airline could have offered alone. This has allowed the Applicants to compete more effectively with the Qantas Group for both leisure and business passengers on the trans-Tasman and throughout Australasia.

67. The Applicants submit that since the authorisation of the Alliance in 2010 the trans-Tasman market has seen frequent and aggressive tactical pricing activity and carrier entry and expansion. For example, from January to August 2010 to the same period in 2012, there has been an increase in the total frequency of tactical sales activity on the Auckland-Sydney route. In particular, Qantas, Jetstar and Emirates increased their sales activity over that period. The Applicants submit that the Auckland-Sydney route is representative of the increased tactical sales activity across other trans-Tasman Sectors due to each airline generally releasing network wide sales.

68. The Applicants submit that entry and expansion on the trans-Tasman since the Alliance has included the entry of China Airlines onto the Auckland-Brisbane route in 2011 and onto the Auckland-Sydney route in October 2012. Jetstar and Emirates have also expanded their trans-Tasman operations. There have been substantial increases in capacity by Emirates (13.3%), Jetstar (5.2%), LAN (4.2%) and Qantas (2.1%) on the trans-Tasman from the Pre-Alliance Year to Year 1. Since November 2012, Jetstar has increased capacity further with an additional aircraft added to its New Zealand based fleet.

69. The Applicants also submit that the Alliance has enabled Virgin Australia to access more of the corporate market than would otherwise be the case. The Applicants

state that they have had significant growth in corporate revenue as a result of the Alliance.

70. The Applicants also submit that the Alliance has enabled them to retain significant corporate contracts and attract new corporate contracts which might previously have been signed with Qantas. This is due to the greater scope of benefits available to consumers under the Alliance than could be offered by the Applicants on their own and has allowed Virgin Australia to quickly and efficiently provide customers with a stronger product offering in competition with the Qantas Group. This in turn, the Applicants submit, has promoted competition for air travel within and to/from Australia and given Australian travellers the choice of a second international Australian based airline.

71. In summary, they submit that in its short operation the Alliance has already delivered on the core rationale and resulted in substantial public benefits. Reauthorisation will result in further and deeper benefits as the Alliance matures.

72. Finally, the Applicants submit that conditions are not necessary to satisfy the net public benefits test as the public benefits derived from the Alliance are sufficient in and of themselves to outweigh any risk of an anti-competitive detriment on the trans-Tasman.

Interested parties

Submissions by other airlines

73. Qantas does not oppose authorisation and broadly agrees with the Applicants that airline alliances are pro-competitive and deliver consumer benefits. It also supports the Applicants' claims that the trans-Tasman routes are 'characterised by excess capacity and competitive market behaviours' and notes that capacity conditions imposed as part of authorisation can produce 'operational inefficiencies and costs'.

74. Emirates does not oppose an authorisation that is 'subject to the same regulatory conditions imposed on Emirates and Qantas'[20]. Emirates notes that this Alliance has 'similar competition dynamics' to the consideration of the Emirates and Qantas alliance, such that it is unclear that Qantas and Emirates would constrain the Alliance. However, any condition imposed should be similar to the Emirates and Qantas condition, to avoid the creation of market distortions, with appropriate flexibility in the condition enabling innovation and responses to changes in demand.

Submissions by associations

75. The Key Wellington Stakeholders Group (**KWSG**)[21] supports re-authorisation of the Alliance, but 'only for a further term of three years' and 'only with continued

[20] See Australian Competition and Consumer Commission, *Determination- Applications for Authorisation A91332-A91333 lodged by Qantas and Emirates – Conditions of Authorisation (Attachment B)*, 27 April 2013.

[21] The Key Wellington Stakeholders Group is a group of business, local government and tourism organisations from the Wellington region. The Key Wellington Stakeholders Group includes the Greater Wellington Regional Council, Grow Wellington, Positively Wellington Tourism, Wellington

appropriate capacity conditions'. While it acknowledges that the Alliance has led to public benefits, it considers that these benefits would be outweighed by the detriments in the absence of appropriate conditions. It considers that, in the absence of conditions, there is a 'very real incentive on the Applicants (and certainly no disincentive) to reduce capacity and to increase fares.' By way of example, it submits that the Wellington-Brisbane route would be negatively affected by the removal of conditions, as they consider that little growth has occurred on this route, beyond that required by the conditions during the operation of the Alliance.

Submissions by airport operators

76. Christchurch International Airport Limited (**CIAL**) supports reauthorisation of the Alliance for a further period of three years, subject to conditions requiring the Applicants to maintain and grow a base level of capacity on the trans-Tasman as a whole, and maintain and grow capacity on individual routes, including the Christchurch-Brisbane/Melbourne/Gold Coast/Sydney routes. CIAL initially submitted that conditions are required as, since the Alliance commenced operating, average fares have increased, consumer demand on the above routes has not been met and material competition concerns have been raised.

77. CIAL made a supplementary submission indicating that the concerns raised in its earlier submission had been largely dealt with by further confidential information provided by Air New Zealand.[22]

78. Dunedin International Airport Limited (**DIAL**) supports conditional authorisation. DIAL submits that, if authorisation is granted, then the current conditions for the Dunedin-Brisbane route ought to be continued, with additional conditions imposed requiring a maintenance of capacity on the Sydney/Melbourne-Dunedin routes.

79. The New Zealand Airports Association (**NZ Airports**) also supports conditional authorisation, but is opposed to the unconditional re-authorisation sought by the Applicants. They submit that, absent conditions, the Alliance will "inhibit the natural competitive dynamics of New Zealand's most significant air travel market", noting that the Alliance "controls 51% of all capacity flown on trans-Tasman sectors".

Submissions by government bodies

80. The Department considers that continued cooperation between Virgin Australia and Air New Zealand on the trans-Tasman is positive and consistent with aviation policy settings. The Department provided contextual information on the relevant aviation market, the air service arrangements which underpin it and the Australian Government's aviation policy. The Department noted that the Australia/New Zealand air services market is one of the most open in the world, with no restrictions on capacity, frequency or routes that airlines of either country can operate to, within or beyond the two countries, with eligible airlines authorised to operate as SAM airlines. The Department further notes that New Zealand is Australia's largest international aviation transport market, with 5.7 million passengers travelling between Australia and New Zealand in 2012, representing 19.4% of total international passengers in that year.

Employers' Chamber of Commerce, Wellington City Council and Wellington International Airport Limited.

22 Christchurch International Airport Limited, further submission to the ACCC, 13 June 2013.

Submissions by tourism authorities

81. Kiss Travel International submits that there has been a large increase in air fares between Australia and New Zealand, for example, on the Brisbane-Queenstown route. They consider that the Alliance will result in a reduction in competition and a reduction in the number of passengers flying Australia-Queenstown, especially from Brisbane.

Submissions by other parties

82. The Consumers' Federation of Australia declined to provide a full submission to the ACCC. However, they noted that a number of principles were important to the consideration of the Alliance, including:

    - affordable and equitable access to essential services;
    - protection from unsafe or unfit products and services; and
    - products and services that are sustainable in terms of their environmental effects.

The Applicants' response to interested party submissions

83. The Applicants note in response to interested party submissions that the submissions overwhelmingly support reauthorisation of the Alliance, and recognise that the Alliance has delivered a range of public benefits.

84. The Applicants reiterated that the benefits realised under the Alliance to date are substantial and that further and deeper benefits can be obtained by reauthorisation of the Alliance.

85. In their response, the Applicants note that their submission and those of interested parties diverge most notably in regard to the necessity for capacity conditions. They submit that, given the Alliance has demonstrated its ability to deliver benefits that were once only theoretical within a short window of operation, and without any anti-competitive detriment on the trans-Tasman or any individual route, the capacity conditions should be removed.

86. The Applicants refer to and agree with the Department's submission that "the Qantas-Emirates alliance acts as a strong competitive counterweight" and "barriers to entry are sufficiently low that if the market is left to operate naturally and competition was to wane, additional competitors are likely to enter the market, causing the market to reach a natural balance point".

87. The Applicants also note CIAL's supplementary submission that indicates CIAL's concerns have been lessened and it no longer opposes the Alliance.

Following the draft determination

Further submissions from interested parties

88. The ACCC received further public submissions in response to the draft determination from:

- Rotorua International Airport (**RIA**)[23] which supports authorisation, although submits that the capacity conditions are not required as incentives and market dynamics already exist to ensure that fares are kept at a reasonable level and capacity is added where required.

- DIAL[24] which is supportive of reauthorisation and submits that the period of three years and the capacity conditions proposed are appropriate. DIAL's submission after the draft determination supported the ACCC's inclusion of the Dunedin-Sydney and Dunedin-Melbourne routes as part of the proposed condition. It strongly contested the Applicants' proposed changes to the structure of the condition in the draft determination.[25]

- Queenstown Airport Corporation Ltd (**QAC**)[26] which is supportive of authorisation, although it submits that it may be more appropriate to impose total capacity conditions on routes in and out of Brisbane to the South Island, namely the Christchurch, Dunedin and Queenstown – Brisbane routes.

- KWSG[27] supports authorisation for a period of three years, and the capacity conditions proposed for the Wellington – Brisbane route. It remains of the view that the proposed authorisation without capacity conditions on the Wellington – Sydney and Wellington – Melbourne routes may substantially lessen competition over the trans-Tasman.

Further submissions from the Applicants

89. In response to the draft determination and interested party submissions, the Applicants made the following submissions[28]:

Public Benefits

90. Broadly, the Alliance has resulted in substantial public benefits, and has been critical to providing greater competition on the trans-Tasman generally and in the domestic Australian market, particularly in relation to competition for corporate and frequent travellers. Further, without the Alliance, the trans-Tasman operations of both Applicants would be diminished to the detriment of consumers.

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23 Rotorua International Airport, Submission in response to draft determination, 19 July 2013.
24 Dunedin International Airport Ltd, Submission in response to draft determination, 23 July 2013.
25 CAPA Consulting, ACCC submission for Dunedin International Airport, August 2013.
26 Queenstown Airport, Submission in response to draft determination, 24 July 2013.
27 Key Wellington Stakeholders Group, Submission in response to draft determination, 24 July 2013.
28 Virgin Australia & Air New Zealand, Submission in response to the draft determination, 24 July 2013.

91. The Alliance has increased the opportunity and incentive of the Applicants to increase trans-Tasman capacity. Further, where there is the demand to support it, the Applicants have grown capacity on condition routes beyond what is required by the 2010 conditions.

92. The Applicants have lowered overall fares which has in turn resulted in lower market fares as Qantas in particular has had to respond to the more competitive service offering provided by the Applicants.

93. The Applicants submit that there is no evidence of any adverse coordinated effects and that strong competitive constraints and incentives will remain after reauthorisation. The trans-Tasman has consistently been a highly competitive market for reasons including a large number of carriers, no material barriers to entry, and a history of persistent strong capacity growth.

Competitive constraint of Jetstar on the Alliance

94. The Applicants note that Jetstar has both a domestic New Zealand and domestic Australian network with high brand awareness; Jetstar has the advantage of its connection to the Qantas Group in terms of brand awareness, connectivity, disruption management and access to customers through the Qantas Frequent Flyer program.

95. They further submit that Jetstar is part of the Qantas-Group/Emirates alliance which means it has access to that alliance's large schedule frequency and breath, and network connection advantage over all other operators.

96. The Applicants submit that Jetstar faces no operational barriers to its continued entry and expansion on any particular trans-Tasman route.

97. In the Applicants' view there is no commercial reason why Jetstar would not expand further. Jetstar has the competitive advantage of the LCC business model, in particular, higher seat density and its role in substantially reducing cost per seat. LCCs have an incentive to and can profitably fill up their planes by offering more seats at lower fares than full service carriers. The Applicants submit that Jetstar has demonstrated its ability to move quickly to deploy capacity in response to any business opportunity.

98. The Applicants submit that not only is there no commercial reason why Jetstar (alone) would not expand in response to a profitable opportunity, the Qantas Group has every commercial reason to deploy Jetstar more widely.[29] Jetstar has replaced Qantas on domestic New Zealand routes where the proportion of business passengers is significantly higher than on the trans-Tasman. The presence of Qantas has not deterred Jetstar from entering a large number of routes. Over 80% of the 71 routes Jetstar has entered were operated by Qantas prior to Jetstar entry. Jetstar replaced Qantas on 45% of these routes and operates in tandem with Qantas on 37% of these routes.

[29] Despite these submissions, the ACCC notes that the Qantas Group, which includes Jetstar, operates as a single entity and is unlikely to act contrary to the interests of the group as a whole, including in its deployment decisions of Jetstar on a particular route.

99. The Applicants submit that Jetstar is an aggressive price competitor that both Applicants are forced to respond to regardless of whether or not Qantas is also present on the route.

Length of authorisation

100. The Applicants submit that an authorisation period of five years will provide an increased level of certainty and confidence for the Applicants to continue to invest in key projects that will drive benefits from the Alliance.

101. They submit that there will be significant risks and costs associated with having a shorter authorisation term, including:

- removal of a viable competitive alternative to the Qantas-Group /Emirates Alliance which was authorised by the ACCC for five years, potentially distorting market behaviour
- undermining the ability to achieve the benefits that could be derived from deeper integration between the Applicants over a longer period, and the incentive of the Applicants to further develop the Alliance
- the limited data available to fully evaluate the benefits of the Alliance when the ACCC is required to consider a reauthorisation in two to three years.

Proposed conditions

102. The Applicants acknowledge and agree with the ACCC's decision in the draft determination to not apply a condition on the Wellington-Melbourne and Wellington-Sydney routes.

103. The Applicants submit that the Brisbane – Queenstown/Dunedin/Christchurch routes should be grouped together in terms of applying conditions, as they are often used interchangeably by customers and are complimentary, operating on a seasonal basis. Further, all three routes compete for the same aircraft time, such that grouping these routes will allow the Applicants to interchange services as necessary and spread additional frequencies between the sectors depending on seasonal demand.

104. The Applicants submit that the Brisbane – Wellington route should be grouped together with the South Island grouping above, and all the routes should be subject to an initial growth factor of zero. This would mitigate the route specific effects recognised by the ACCC in its draft determination.

105. The Applicants submit that market dynamics do not support the application of conditions on the following routes:

- Dunedin – Melbourne/Sydney: are thin seasonal routes which have always been served by one carrier. It is extremely unlikely that both Virgin Australia and Air New Zealand would compete on these routes.
- Auckland – Gold Coast: a highly competitive route and largely a leisure/visiting friends or relatives (VFR) route. The route is particularly suited to the budget travel product of Jetstar, which acts as a major competitive constraint with 37% market share.

- Christchurch – Melbourne: is also a highly competitive route and Jetstar again acts as a major competitive constraint with 37% market share. FFC entry/re-entry is likely once Christchurch recovers from the 2011 earthquake.

106. If the ACCC is minded to impose capacity conditions on the routes above, the Applicants submit that these routes should also be included in a grouping such that there are no route specific conditions.

107. The Applicants' initially made submissions that any capacity conditions should commence from the start of Northern Summer (NS) 2014 (April). This submission was made in the context of the proposed imposition of a growth factor by the ACCC in the draft determination. The Applicants submitted that commencing the capacity conditions earlier would have a material negative impact on the Applicants and consumers. Capacity for NW 2013 has already been planned and slots confirmed.

108. The Applicants also submit that any growth factor should initially be set at 0%:

- the ongoing reporting obligations permit the ACCC to monitor capacity and properly consider the actual capacity decisions in light of relevant market circumstances prevailing over the period of the authorisation, particularly where there is already substantial capacity in the market

- applying capacity conditions with a capacity floor, as opposed to a growth factor, will enable the ACCC to assess the true Alliance impact as opposed to the impact created by the growth factor

- adding extra capacity on a number of the proposed capacity condition routes would effectively add capacity that is out of line with passenger demand, and result in the Applicants being forced to redirect capacity away from other, better performing routes where the addition of capacity is required to meet demand.

109. The Applicants submit that capacity growth factor calculation, excluding "negative quarterly changes in Australia's Trend Chain Volume GDP" would result in the Applicants being required to grow capacity ahead of GDP.

110. In conclusion, although the Applicants maintain that no conditions are necessary, they submit that authorisation should be granted for 5 years, commencing 1 January 2014, and any competition concerns could be addressed with capacity conditions on the Brisbane – Wellington/Christchurch/Dunedin/Queenstown routes, and the reporting obligations.

111. The views of the Applicants and interested parties are outlined in the ACCC's evaluation chapter of this determination. Copies of public submissions may be obtained from the ACCC's website www.accc.gov.au/authorisationsregister.

ACCC evaluation

112. The ACCC's evaluation of the proposed conduct is in accordance with the relevant net public benefit tests[30] contained in the Act. In broad terms, under the relevant tests the ACCC shall not grant authorisation unless it is satisfied that the likely benefit to the public would outweigh the detriment to the public constituted by any lessening of competition that would be likely to result. While there is some variation in the language of the tests, in broad terms, the ACCC is required to identify and assess the likely public benefits and detriments, including those constituted by any lessening of competition and weigh the two. In broad terms, the ACCC may grant authorisation if it is satisfied that the benefit to the public would outweigh the public detriments.

113. In order to assess the effect of the proposed conduct and the public benefits and detriments likely to result the ACCC identifies the relevant areas of competition and the likely future should authorisation not be granted.

The relevant area of competition

114. The ACCC considers that the relevant areas of competition for the purposes of this assessment are:

- international air passenger transport services between Australia and New Zealand;
- air freight transport services on the trans-Tasman;
- Australian domestic air passenger transport services;
- the sale of international travel services; and
- the supply of, and procurement of, various goods and services that form inputs to the supply of passenger and air cargo transport services (e.g. line maintenance engineering services, flight training for aircrew and cabin crew, and the procurement of aircraft, aviation fuel and catering products and services).

International air passenger transport services

115. Under the Alliance, Virgin Australia and Air New Zealand propose to coordinate their trans-Tasman air passenger transport operations.

116. The ACCC has recognised in previous decisions that people travel for different reasons and can have substantially different demand characteristics. In general, passengers travelling for the purpose of leisure or visiting family and friends (leisure travellers) are relatively more price sensitive and relatively less concerned about factors such as travel time, frequency of flights, flexibility, connectivity,

30 Subsections 90(6), 90(7), 90(5A) and 90(5B), 90(8). The relevant tests are set out in Attachment A.

convenience and comfort when compared to business passengers. The manner in which airlines compete to attract leisure and business travellers differs, as does the willingness of these travellers to seek alternatives. As a consequence, the effect of any lessening of competition on these customer segments can differ.

117. The ACCC considers that these characteristics of leisure and business passengers mean that airlines seek to target leisure and business passengers separately through different branding strategies, for example Jetstar targeting leisure customers, and through different fare structures, for example, fully flexible last minute fares. As such, the closeness of competition between different airlines is likely to differ.

118. The ACCC considers that for the purposes of this assessment the relevant areas of competition are likely to include international air passenger transport services between Australia and New Zealand.

119. Within this area of competition, the ACCC has examined the likely effects of the proposed conduct on competition and rivalry on particular routes where necessary.

Trans-Tasman air freight transport services

120. The Applicants have confirmed that freight services, including freighter operations and cargo belly space, are excluded from the Alliance.

121. The ACCC notes that to the extent that scheduling coordination occurs under the Alliance in relation to international air passenger transport services this will have an effect on scheduling of air freight transport services.

122. In its draft determination, the ACCC sought further information from interested parties on whether this raised potential competition concerns.

123. In response the Applicants submitted that there has been no adverse impact, and there is unlikely to be any adverse impact, on competition for air freight transport services.

124. The Applicants submit that Virgin Australia operates a very small proportion of the cargo capacity on the trans-Tasman and therefore the potential for any adverse competitive impact is extremely low.

125. The Applicants further submit that in terms of the market, wide body aircraft provide the bulk of the freight capacity across the trans-Tasman as a whole. Air New Zealand itself only operates wide body services from Auckland along with Emirates, supplemented by the dedicated freighter services operated by Singapore Airlines and Qantas. Virgin Australia does not operate any wide body aircraft across the trans-Tasman at all. There are no wide body operators operating into or out of Wellington and Christchurch.[31]

[31] Virgin Australia & Air New Zealand, Submission in response to the draft determination, 24 July 2013, Annexure A, p.1. The ACCC notes that Emirates operates the route between Sydney and Christchurch and that Christchurch Airport can accommodate wide bodied aircraft.

126. No interested party commented on the effect of the Alliance on trans-Tasman air freight transport services.

127. The ACCC considers that the Alliance is unlikely to have a material impact on the market for trans-Tasman freight transport services, taking into account:

- the small market share held by Virgin Australia;
- the existence of other carriers including Qantas and Emirates, FFCs and specialist freight operators.

128. For this reason the ACCC has not considered this market further in this determination.

Australian domestic air passenger transport services

129. The ACCC has previously recognised that an international aviation alliance could affect competition for the supply of domestic air passenger transport services by directing the onward carriage (i.e. inbound) traffic or feeder (i.e. outbound) traffic to a particular carrier, in this case, Virgin Australia, at the expense of the competitive position of other domestic carriers.[32]

130. Due to this potential impact, the ACCC considers that Australian domestic air passenger transport services is a relevant area of competition for its consideration of the applications for authorisation.

The sale of international travel services

131. In previous determinations in respect of aviation alliances, the ACCC has recognised a separate market for the sale of international travel services, which includes tickets sold directly by airlines and through indirect channels such as travel agents.[33]

132. The ACCC considers that the proposed conduct is likely to have minimal, if any, impact on competition in the market for the sale of international travel services. The ACCC notes there are a range of competitors in this market including travel agencies (online and in shop fronts), direct distribution by other airlines as well as the increasing presence of global internet portals such as Expedia and Webjet.

133. Given the negligible nature of any likely impact, the ACCC has not considered further the effect of the proposed conduct on the sale of international travel services.

[32] ACCC, Determination for applications A91267 and A91268 lodged by Virgin Australia and Singapore Airlines (2011).

[33] ACCC, Determination for applications A91267 and A91268 lodged by Virgin Australia and Singapore Airlines (2011).

The supply of ancillary goods and services

134. The ACCC has considered the impact of the Alliance on the markets for the supply of ground handling, aircraft maintenance, catering and aircraft cleaning. In response to ACCC information requests the Applicants have advised that there is no overlap in relation to the supply of these services, specifically:

- ground handling, as Virgin Australia outsources its ground handling at all ports, and Air New Zealand outsources its ground handling at all Australian ports;
- aircraft maintenance, as Virgin Australia only has facilities in Australia and Air New Zealand only has facilities in New Zealand;
- catering, as Virgin only caters at Australian ports and Air New Zealand only caters at New Zealand ports (where meals are uplifted for both outbound and return journeys); and
- aircraft cleaning, as Virgin engages cabin crew to clean aircraft, and Air New Zealand employs cleaning crews in New Zealand and outsources this task in Australia.

135. No interested party identified any impacts on any market for the supply of any ancillary goods and services arising from the Alliance.

136. Taking into account the information, evidence and submissions before it, including the lack of overlap between Virgin Australia and Air New Zealand and the presence of other third party providers, the ACCC considers that the Alliance is likely to have minimal, if any, impact on competition for the supply of ground handling, aircraft maintenance, catering and aircraft cleaning services. Accordingly, these markets are not considered further in this determination.

The procurement of ancillary goods and services

137. The Alliance extends to the Applicants jointly procuring products and services such as fuel, ground handling services, aircraft maintenance, catering and aircraft cleaning.

138. No interested party has identified any impacts arising from the Applicants undertaking procurement of goods and services jointly in the future.

139. The ACCC has had regard to the likely impact of the proposed conduct on the acquisition of various goods and services that form inputs to the supply of air passenger transport services (in particular, the procurement of aircraft, aviation fuel, catering products and ground handling services).

140. The ACCC has also had regard to:

- the bargaining power of the large corporations that supply many of the inputs coupled with the relatively large number of alternative acquirers of these products; and
- the fact that many of the inputs are acquired on an international basis.

141. The ACCC, taking into account the information, evidence and submissions before it, considers that the Applicants' joint procurement of various goods and services is likely to have minimal, if any, impact on competition in any relevant market. Accordingly, joint procurement is not considered further in this determination.

The future with and without

142. The ACCC compares the likely 'future with and without' to identify and weigh the public benefits and public detriment likely to flow from the proposed conduct.[34]

143. In their supporting submission dated 8 March 2013, the Applicants claim that if authorisation is not granted, they would immediately take steps to unwind the Alliance. In particular, each Applicant would:

- remove its code from the other's services and terminate or renegotiate the interline pricing for access to its domestic network;
- review its network with a view to adjusting capacity where necessary to reflect the likely reduced demand due to the loss of connectivity and distribution provided by the former Alliance partner;
- reschedule services to maximise load factors on its own services even though that may result in wingtip flying with their former Alliance partner;
- take steps to secure access to slots that were surrendered during the term of the Alliance;
- terminate their former Alliance partner's access to its lounges; and
- renegotiate access to reciprocal frequent flyer benefits with their former Alliance partner.

144. Following discussions with the ACCC, the Applicants provided separate supplementary submissions outlining the nature of their operations in the likely future without the Alliance.

145. Virgin Australia submits that in the likely future without the Alliance:[35]

- its ability to offer consumers a competitive international network will be limited;
- there will be less effective competition on the trans-Tasman:
    - — absent the Alliance, both Virgin Australia and Air New Zealand will struggle to compete with the Qantas-Group/Emirates alliance

34 *Australian Performing Rights Association* (1999) ATPR 41-701 at 42,936. See also for example: *Australian Association of Pathology Practices Incorporated* (2004) ATPR 41-985 at 48,556; *Re Media Council of Australia* (No.2) (1987) ATPR 40-774 at 48,419; Re *Medicines* Australia Inc (2007) ATPR 42 – 164; [2007] ACOMPT 4 at 17.

35 Virgin Australia, Submission in relation to Virgin Australia's Counterfactual, 25 June 2013 (Virgin Australia's Supplementary Counterfactual Submission).

— Virgin Australia will be severely impacted due to its limited depth and breadth of schedule while Air New Zealand will struggle to compete due to its limited ability to attract Australian-based passengers and access behind gateway points in Australia. This was the case prior to the Alliance and was part of the strategic rationale for implementing the Alliance.

- Virgin Australia will review the viability of each of its trans-Tasman routes:

  — without the Alliance, Virgin Australia's financial performance will deteriorate and its materially weakened schedule frequency and breadth and network connection offer against Qantas-Group/Emirates will undermine the broader strategic benefits to Virgin Australia of operating on the trans-Tasman. Virgin Australia will have a weaker product offering and have a reduced ability to attract both business and leisure passengers. As a result, Virgin Australia will not grow capacity on the trans-Tasman and will be required to withdraw capacity and services on some routes in accordance with commercial business performance.

  — without the Alliance, the performance of key business markets such as Auckland-Sydney and Auckland-Melbourne will be negatively impacted due to the inability to compete with the Qantas-Group/Emirates frequency offered on such routes. Virgin Australia has limited ability to substantially increase the frequency of its stand-alone trans-Tasman services, as matching the frequency levels of competitors would require significant investment in new aircraft which could not be justified. Virgin Australia may also need to reduce frequencies on other routes in order to reduce any losses and to more profitably redeploy capacity. It may be the case that Virgin Australia capacity withdrawn from the trans-Tasman could more profitably be deployed on other Virgin Australia routes.

- Virgin Australia will review its customer benefit offering (e.g. lounge access) on the trans-Tasman; and

- Virgin Australia would not enter into a code share agreement with Air New Zealand while Virgin Australia operates on the trans-Tasman, regardless of how substantial or insubstantial Virgin Australia's presence is on trans-Tasman routes.

146. Air New Zealand submits that it would make a number of operational changes in the likely future without the Alliance:[36]

a. Termination of code share, frequent flyer program and lounge arrangements

147. Air New Zealand notes that prior to the Alliance, the Applicants were direct competitors on the trans-Tasman and did not code share or have any agreement in relation to frequent flyer benefits and lounge access. Air New Zealand submits that in the likely future without the Alliance it would:

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36 Air New Zealand, Submission in relation to Air New Zealand Counterfactual, 20 June 2013 (Air New Zealand Supplementary Counterfactual Submission)

- revert to the pre-Alliance position from 31 December 2013 (i.e. it would not continue to sell code share with Virgin Australia and would cease frequent flyer program and lounge cooperation on the trans-Tasman);[37] and

- not offer Virgin Australia an interline/special prorate agreement[38] in relation to domestic New Zealand traffic.

b. Cancellation of direct services and wider capacity reductions

148. Air New Zealand considers that the Alliance allows the parties to leverage the combined feed and presence of each Alliance party. In the absence of these benefits in the likely future without the Alliance, Air New Zealand submits that it would:

- discontinue various routes made possible by the Alliance so far;

- reduce frequencies, or down-gauge aircraft on a number of other trans-Tasman routes and exit some poor performing routes either on a year round or seasonal basis;

- as soon as possible (having regard to slot allocations, etc.) retime departures to maximize its own revenue (with a consequent increase in wing-tip flying with Virgin Australia and reduced schedule spread for consumers); and

- immediately cease analysis of any potential new Alliance services.

149. Air New Zealand states that the lack of metal neutrality[39] with a partner airline and reduced online connectivity to Australian domestic destinations would make Air New Zealand's trans-Tasman/Australasian offering less attractive. With a forecast significant reduction in demand, Air New Zealand would need to further adjust capacity to reflect this.

150. Air New Zealand also considers that its lack of a domestic Australian presence in the absence of the Alliance would place it at a significant competitive disadvantage to the Qantas-Group/Emirates alliance.

151. Following the draft determination, KWSG submitted that Virgin Australia (and indeed all airlines flying the trans-Tasman) would wish to review operations on the various trans-Tasman routes in light of any decision not to reauthorise the Alliance. KWSG does not consider that it is appropriate to infer that, absent the Alliance, Virgin Australia would be likely to reduce its pre-Alliance Wellington-Sydney offering and would not seek to enter the Wellington-Melbourne market. Indeed, KWSG considers it likely that Virgin Australia would re-enter the Wellington-Sydney

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[37] Air New Zealand notes that it would continue to carry Virgin Australia codeshare passengers who had already booked and paid for their travel prior to 31 December 2013, and these passengers will receive their usual frequent flyer program and lounge benefits in accordance with their pre-Alliance entitlements.

[38] This term has been defined in the Glossary above.

[39] This term has been defined in the Glossary above.

route and that its majority-owned subsidiary, Tiger, would enter the Wellington-Melbourne route.[40]

ACCC view

152. The ACCC considers that the most likely future without the Alliance will involve a situation where Virgin Australia and Air New Zealand continue to operate on the trans-Tasman as independent competitors.

153. The ACCC notes Virgin Australia's submission that the Alliance is key to its Game Change strategy and the trans-Tasman is a key market for corporate contracts. In light of these submissions, the ACCC considers that Virgin Australia would be likely to continue to operate a number of services on trans-Tasman routes in the future without the Alliance.

154. However, the ACCC also notes Virgin Australia's submission that without the Alliance, it will not be able to offer an effective competitive constraint on the trans-Tasman due to its weaker product offering, materially reduced schedule frequency and the reduction in the breadth of network and connectivity on both sides of the Tasman. In this regard, Virgin Australia submits that:

- the Qantas-Group/Emirates alliance has approximately 47% capacity share serving 12 trans-Tasman routes while Virgin Australia, without the Alliance and based on current operations, would at most only be able to offer services on eight of these trans-Tasman routes (assuming no withdrawal of capacity or service reduction); and

- on the key trans-Tasman routes which are important for Australian corporate contracts, Virgin Australia's comparative shares of total capacity for the year ending June 2012 were:

Sector[41]	Virgin Australia	Qantas-Group/Emirates
AKL-BNE	14.4%	42.8%
AKL-MEL	10.5%	57.9%
AKL-SYD	5.2%	51.2%

155. Having regard to the services that Virgin Australia actually operates itself at the present time, the ACCC accepts that Virgin Australia's trans-Tasman operations in the likely future without the Alliance would be significantly more limited than its key competitors in terms of schedule depth and breadth.

156. The ACCC also notes Virgin Australia's submissions that absent the Alliance, it will review the viability of each of its trans-Tasman routes; will not grow capacity on the

40 KWSG, Submission to the ACCC on the ACCC's draft determination dated 10 July 2013 regarding the application for reauthorisation of an alliance between Virgin Australia and Air New Zealand, 24 July 2013 (KWSG post draft submission), p. 6

41 Information in the table is information provided by Virgin Australia in its Supplementary Counterfactual Submission at p. 3.

trans-Tasman; and will be required to withdraw capacity and services on some routes in accordance with commercial business performance. Virgin Australia has provided the ACCC with confidential information (including financial information) to support these claims.

157. After considering the further confidential information provided, the ACCC accepts that in the likely future without the Alliance, Virgin Australia will review its financial performance on the trans-Tasman. On balance, the ACCC considers it feasible that as a result of any such review, Virgin Australia may not grow capacity on the trans-Tasman and/or may withdraw capacity and services on certain routes in accordance with commercial business performance. Absent the Alliance, the ACCC also considers that Virgin Australia is unlikely to re-enter routes that it has exited as a consequence of schedule optimisation under the 2010 Alliance.

158. Given that the trans-Tasman is a substantial part of Air New Zealand's business which feeds its long haul international and domestic routes, the ACCC considers that Air New Zealand would continue to operate a significant number of services on trans-Tasman routes in the likely future without the Alliance.

159. However, the ACCC notes the Applicants' submissions that absent the Alliance, Air New Zealand:

- would make a number of operational changes, including cancelling direct services and reducing capacity; and
- will be limited in its ability to attract Australian based passengers from behind gateway points in Australia because it has no access to the Australian domestic market beyond possible interline agreements. Any interline agreements that Air New Zealand manages to negotiate will come at greater cost to both Air New Zealand and consumers and leave Air New Zealand at a competitive disadvantage to Qantas-Group/Emirates in competing for passengers requiring access to or from points behind the main Australian gateways.

160. The ACCC has had regard to confidential information provided by Air New Zealand in support of these submissions and considers that in the likely future without the Alliance, Air New Zealand:

- may review the operation of certain services which rely on the combined feed and presence of both Alliance partners; and
- is likely to be at some competitive disadvantage to the Qantas-Group/Emirates alliance due to its weaker sales presence and more limited access to the domestic market in Australia.

161. The ACCC notes the Applicants' submission that their incentive to cooperate in any significant way in the absence of authorisation would be lost because each party would revert to protecting the financial performance of its own trans-Tasman services.

162. Based on the information currently available, the ACCC accepts that the Applicants would have limited commercial incentives to enter into alternative bilateral arrangements with each other in the absence of the Alliance.

163. In relation to other airlines operating on the trans-Tasman, the ACCC considers that Qantas and Jetstar are unlikely to add capacity in the short term, in light of their submissions that there is excess capacity on the trans-Tasman.[42]

164. The ACCC notes that a number of FFCs have entered and exited the trans-Tasman over the past decade, with only Emirates maintaining a constant presence and a significant market share. The ACCC notes the entry of China Airlines on the Auckland-Sydney and Auckland-Brisbane routes from 2011. The ACCC considers that the potential for FFCs to enter trans-Tasman routes, both with and without the proposed conduct, will depend on the broader network wide considerations of FFCs, and will be limited to airports where long-haul aircraft can be accommodated.

Public benefit

165. Public benefit is not defined in the Act. However, the Australian Competition Tribunal (**Tribunal**) has stated that the term should be given its widest possible meaning:

> Public benefit has been, and is given a wide ambit by the Tribunal as, in the language of the QCMA ... "anything of value to the community generally, any contribution to the aims pursued by the society including as one of its principal elements (in the context of trade practices legislation) the achievement of the economic goals of efficiency and progress". Plainly the assessment of efficiency and progress must be from the perspective of society as a whole: the best use of society's resources. We bear in mind that (in the language of economics today) efficiency is a concept that is usually taken to encompass "progress"; and that commonly efficiency is said to encompass allocative efficiency, production efficiency and dynamic efficiency.[43]

166. In considering public benefits, the ACCC considers the extent to which the benefit has an impact on members of the community and the weight that should be given to it, having regard to its nature, characterisation and the identity of the beneficiaries. In relation to cost savings the ACCC will consider who is likely to take advantage of them and the time period over which the benefits are likely to be seen.

167. Consistently with the object of the Act as specified in section 2, public benefit is identified and assessed having regard to its effect on the promotion of competition and the enhancement of the welfare of Australians. The ACCC recognises that public benefits resulting from the Alliance are likely to affect both Australia and New Zealand. However, the nature of some benefits in this case is such that the ACCC has not been able to reliably apportion identified public benefit as between the two countries. Accordingly, the ACCC has considered potential public benefits which arise from the proposed conduct as a whole, consistent with its approach to public detriment.

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42 ACCC, Determination of applications A91332 & A91333 lodged by Qantas Airways Ltd and Emirates, 27 March 2013. The ACCC notes the recent announcement of additional of capacity on the Brisbane – Auckland route by Emirates.

43 *Re 7-Eleven Stores* (1994), ATPR 41-357 at [42,677].

168. As discussed above in **the conduct** section, since the 2010 authorisation, the Applicants have taken steps to implement the Alliance with full coordination commencing in August 2011. The Applicants submit that in the short duration the Alliance has been in operation it has generated the public benefits claimed in 2010, but that in a number of instances the limited duration has not allowed all the benefits to be fully realised.

169. The Applicants submit that the Alliance has delivered, and with reauthorisation will continue to deliver, the following public benefits:

- enhanced products and services;
- cost savings and other efficiencies;
- promotion of competition; and
- stimulation of tourism.

170. The Applicants' specific claims, the views of interested parties and the ACCC's assessment of the likely public benefits from the proposed conduct are set out below.

Enhanced products and services

171. In their 2010 application, the Applicants submitted that the Alliance would result in enhanced products and services, including:

- increased choice of trans-Tasman flights for Virgin Australia and Air New Zealand customers;
- increased network connectivity for Virgin Australia and Air New Zealand customers;
- better schedule spread for Virgin Australia and Air New Zealand customers;
- reciprocal access to lounge and loyalty programs; and
- expected new frequencies.

2010 determination

172. In considering the Alliance in 2010 the ACCC concluded that the Alliance was likely to result in enhanced products and services in the form of:

- increased access to a large number of existing frequencies and destinations (under a single airline code) for the significant number of consumers who prefer to fly with Virgin Australia or Air New Zealand;
- increased connectivity and better scheduling through:
    i. increased online connectivity;

ii. reduced wingtip flying;

- greater loyalty program benefits and increased lounge access for Virgin Australia and Air New Zealand passengers; and
- additional frequencies on a number of routes.

Applicants' submissions

173. In their current application, the Applicants submit that the Alliance has already resulted in public benefits in the form of enhanced products and services and the associated increase in consumer choice. The Applicants note specifically:

- the availability of an additional 628 online connection[44] options for Alliance passengers;
- additional frequencies on Auckland-Adelaide, Auckland-Brisbane, Auckland-Perth, Brisbane-Wellington, Melbourne-Wellington and the addition of some peak period frequencies on Sydney-Wellington;
- a significant reduction of wingtip flying including, providing customers with a greater choice of departure and arrival times on a number of high frequency sectors. For example the Applicants submit that they both previously had flights departing Auckland to Brisbane at the same time of day, and the Alliance has allowed them to spread the departure time of these flights;
- a removal of day of week clashes on low frequency sectors Brisbane-Queenstown and Queenstown-Sydney to provide consumers with a better offering including the ability to have different length stays. For example, Virgin Australia and Air New Zealand previously both had flights on Tuesdays and Saturdays on this route, now they have departures on Monday, Tuesday, Friday and Saturday;
- the ability to earn and burn frequent flyer points across the entire Air New Zealand and Virgin Australia networks including the trans-Tasman, domestic Australia, domestic New Zealand and long haul sectors (excluding sectors to/from the Pacific Islands);
- the ability for Virgin Australia passengers to access Air New Zealand's six international air-side lounges on the trans-Tasman[45] and Air New Zealand's 12 domestic lounges; and the ability for Air New Zealand passengers to access Virgin Australia's eight domestic Australia lounges;
- Air New Zealand upgauged its daily Auckland-Perth service from a Boeing 767 to a Boeing 777 on 3 September 2012; and

[44] An online connection refers to a passenger itinerary of two or more flight segments where connections are made between flights of the same airline or its codeshare partners. The ACCC has considered this in previous determinations, see for example ACCC determination A91227 & A91228 Virgin Blue Airlines Pty Ltd & Air New Zealand, 16 December 2010 and A91247 & A91248 Virgin Blue Airlines Pty Ltd & Etihad, 3 February 2011.

[45] These lounges are located at the following airports: Auckland, Christchurch, Wellington, Melbourne, Sydney and Brisbane.

- the commencement of new seasonal Auckland-Sunshine Coast services and the scheduled commencement of the Christchurch-Perth route for December 2013 to April 2014.

174. The Applicants submit that these benefits could not have been achieved without the Alliance. Unlike a standalone code share agreement, the Alliance's metal neutral revenue allocation model incentivises the carriers to focus on improving revenue across both carriers' trans-Tasman flights without preference to their own operated services. For example, prior to the Alliance, Virgin Australia would have sold a passenger travelling from Adelaide to Auckland, a ticket going via Sydney or Melbourne. Under the Alliance, because there is no revenue impact, Virgin Australia would offer the same passenger a direct flight on Air New Zealand metal.

175. The Applicants claimed public benefits in relation to enhanced products and services is set out in more detail below.

Increased online connections

176. The ACCC has previously recognised that customers' value online connections[46] much more than interline connection options and acknowledged the academic literature in this area.[47]

177. To the extent that an airline alliance replaces interline connection options with online connection options for consumers, this may benefit consumers. These benefits may take several forms, including:

    - removal of the risk of forfeiting non-refundable fares if the first flight in a journey is delayed;
    - increased convenience in not having to collect and bear baggage mid journey (where applicable); and
    - time savings associated with through check (i.e. passengers do not need to allow time for a second check-in, where applicable).

2010 determination

178. In the 2010 determination, the ACCC considered that increased online connection options for consumers were a source of public benefit under the Alliance. However, the ACCC also expressed doubt about the magnitude of public benefit associated with increased online connections under the Alliance given that:

    - there is a very high percentage of origin destination traffic on the trans-Tasman, which suggests that the current trans-Tasman routes meet most customers' travel requirements; and

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46 See footnote 33 above.

47 See, for example, Carlton, D., W. Landes, and R. Posner, 1980, 'Benefits and costs of airline mergers: a case study', *Bell Journal of Economics*, Vol. 11, pp. 65-83; Graham, D. R., D. P. Kaplan and D. S. Stribley 1983, 'Efficiency and competition in the airline industry, *Bell Journal of Economics*, Vol. 14, pp. 118-138; and Brueckner J. K 2003, 'International airfares in the age of Alliances: the effects of codesharing and antitrust immunity', *The Review of Economics and Statistics*, Vol. 85, No. 1, pp. 105-118.

- neither the New Zealand points or the East Coast Australian points have extensive high traffic beyond points.

179. In 2009 around 550,000 of passengers (10%[48]) who travelled the trans-Tasman did so via an Australian connection.

180. The ACCC noted that the vast majority of these reported 550,000 trans-Tasman passengers who utilised an Australian connection in 2009, were likely to already have an online connection option through Qantas, Jetstar or Virgin Australia absent the Alliance.

181. This led the ACCC to conclude that the Alliance only created new online connections for trans-Tasman passengers who utilise connections at both ends of their trans-Tasman journey – that is, connection to a destination within Australia beyond one of the Australian gateways (Sydney, Melbourne, Brisbane, Perth, Adelaide, Cairns, Coolangatta) and connection to a destination in New Zealand beyond the New Zealand gateways (Auckland, Christchurch, Wellington or Queenstown).

182. The ACCC considered that passengers who meet this profile were likely to represent a modest proportion of the numbers submitted by the Applicants. Notwithstanding this, the ACCC accepted that there was some public benefit from increased online connections under the Alliance.

Applicants' submissions

183. In their current application, the Applicants submit that since the Alliance has been implemented, an additional 628 online connection options have become available to Alliance passengers.

184. The Applicants submit that these online connections could not have been achieved without the Alliance. As noted above, the structure of the Alliance means that it is revenue neutral for Virgin Australia to offer passengers that it would otherwise feed onto an indirect Virgin Australia service a direct flight on Air New Zealand metal.

185. The Applicants also submit that some connecting fares have only been made possible following Virgin Australia's migration to SabreSonic in January 2013. Prior to migration, the Applicants submit that Virgin Australia did not have the ability to support the creation of such itineraries and the development of these products was challenging, due to IT incompatibilities.

ACCC view

186. The ACCC notes that the 628 online connection options already provided by the Alliance exceeds the amount anticipated by the Applicants in their initial 2010 application.

187. The ACCC considers that the online connection options created by the Alliance provide benefits for passengers. For example, passengers wishing to travel from Townsville to Hamilton may do so on a single itinerary, utilising Virgin Australia flights from Townsville to Cairns, and Cairns to Auckland, and an Air New Zealand

[48] The ACCC has calculated this figure based on BITRE data for the year ended December 2009 (5 293 501 passengers travelled between Australia and New Zealand).

flight from Auckland to Hamilton. For these passengers online connections provide benefits in the form of removal of the risk of forfeiting non-refundable fares if the first or second flight in their journey is delayed, and the increased convenience of not having to collect baggage in Cairns or Auckland.

188. The Applicants have provided to the ACCC, on a confidential basis, the number of Alliance passengers who have utilised an Air New Zealand connecting flight, the number of Alliance passengers who have utilised a Virgin Australia connecting flight and the number of Alliance passengers who have utilised both a Virgin Australia and Air New Zealand flight in addition to their Alliance journey.

189. The ACCC acknowledges that the Alliance has resulted in increased online connections for passengers on the trans-Tasman. However, as was the case in 2010, the ACCC considers that only a small proportion of trans-Tasman passengers utilise a connection at either end of their trans-Tasman journey that would not be available absent the Alliance.

190. The ACCC considers that to the extent passengers utilise connections that would not be available absent the Alliance, the Alliance is likely to continue to result in public benefits in the form of increased online connections. This benefit takes the form of increased choice for travellers who connect beyond trans-Tasman gateways. The ACCC considers that due to the limited number of passengers that do utilise connections that would not have been available absent the Alliance, the current magnitude of this benefit is small. The ACCC considers that as the number of passengers who utilise connections at either end of their journey increases, this benefit will correspondingly grow. On this basis, the ACCC considers that the Alliance is likely to result in some, likely small, public benefits through the provision of increased online connections in the future.

Better schedule spread

191. Airline alliances can also improve connectivity by spreading their flight schedule in situations where the airlines currently fly wingtip to wingtip. Wingtip flying occurs because there are certain times preferred by a large number of passengers. Absent an alliance, two airlines may prefer to schedule their flights at the most popular departure time. Under an alliance with revenue sharing, their incentives change and they may find the retiming of one flight to be more consistent with joint revenue maximisation.

2010 determination

192. In their 2010 application for authorisation, the Applicants submitted that the Alliance would provide them with the ability and the incentive to undertake significant schedule changes which would optimise the network and benefit all travellers.

193. The ACCC, in the 2010 determination, accepted that under the Alliance the Applicants would have an incentive to review their current schedules with a view to optimising them. The ACCC considered that the removal of some wingtip flying was a likely outcome of this process.

194. While the ACCC accepted that increased schedule spread was a likely source of public benefit under the Alliance, it noted that it was difficult to be definitive about

the extent of this public benefit as the Applicants had not submitted details on how they would modify their schedules under the Alliance.

Applicants' submissions

195. The Applicants submit, in relation to their current application, that under the Alliance they have been able to work together to maximise their total network offering. The Applicants submit that as a result there have been a number of network changes which have resulted in, and will continue to result in, public benefits; namely:

- a significant reduction of wingtip flying, and
- a removal of day of week clashes on low frequency sectors.

196. Table PB.1 below outlines the changes in wingtip flying since the implementation of the Alliance for the Northern Winter scheduling season.

	Pre Alliance NW09			Post Alliance NW11		
	Sectors per season	No. of Wingtip Flights	Wingtip %	Sectors per season	No. of Wingtip Flights	Wingtip %
AKLBNE	952	161	17%	946	0	0%
BNEWLG	600	164	27%	588	0	0%
SYDWLG	594	110	19%	586	0	0%
AKLSYD	1885	268	14%	1712	92	5%
AKLMEL	1051	30	3%	1006	4	0%
AKLOOL	456	52	11%	478	0	0%
BNECHC	643	148	23%	578	36	6%
CHCMEL	742	192	26%	534	29	5%
CHCSYD	784	117	15%	536	24	4%

Table PB.1: source data supplied by the Applicants[49]

[49] The Applicants submit that Sydney – Queenstown has also seen a reduction in wingtip flying however, due to the number of services being operated on this route and the day of week coverage, the Applicants have shown these changes in the removal of day of week clash analysis.

197. Table PB.2 below outlines the corresponding changes in wingtip flying since the implementation of the Alliance for the Northern Summer scheduling Season.

	Pre Alliance NS10			Post Alliance NS12		
	Sectors per season	No. of Wingtip Flights	Wingtip %	Sectors per season	No. of Wingtip Flights	Wingtip %
AKLBNE	1514	267	18%	1598	174	11%
BNEWLG	848	243	29%	866	14	2%
SYDWLG	676	167	25%	756	0	0%
AKLSYD	2340	415	18%	2334	49	2%
AKLMEL	1362	205	15%	1422	49	3%
AKLOOL	736	175	24%	696	4	1%
BNECHC	1106	262	24%	992	302	30%
CHCMEL	738	149	20%	586	26	4%
CHCSYD	900	200	22%	668	67	10%

Table PB.2: source data supplied by the Applicants[50]

198. The Applicants submit that, as a result of the Alliance, there has been:

- the removal of northern winter wingtip flying on Auckland-Brisbane, Auckland-Gold Coast, Auckland-Melbourne, Brisbane-Wellington and Sydney-Wellington;
- the removal of northern summer wingtip flying on Sydney-Wellington;
- a significant reduction on the number of northern winter wingtip flights on Auckland-Sydney, Brisbane-Christchurch, Christchurch-Melbourne and Christchurch-Sydney; and
- a significant reduction on the number of northern summer wingtip flights on Auckland-Brisbane, Auckland-Gold Coast, Auckland-Melbourne, Auckland-Sydney, Brisbane-Wellington, Christchurch-Melbourne and Christchurch-Sydney.

50 The Applicants submit that Sydney – Queenstown has also seen a reduction in wingtip flying however, due to the number of services being operated on this route and the day of week coverage, the Applicants have shown these changes in the removal of day of week clash analysis.

199. The Applicants submit that the relatively high wingtip percentage for northern summer on the Brisbane-Christchurch route reflects operational changes required to meet capacity commitments under the conditions of authorisation and account for growth on the Brisbane-Dunedin and Brisbane-Queenstown routes. Flights to Brisbane-Dunedin and Brisbane-Queenstown affect the departure and arrival time possibilities for Brisbane-Christchurch flights.

200. The Applicants also submit that the Alliance has resulted in the removal of day of week clashes on the Sydney – Queenstown route. The Applicants submit that, prior to the Alliance, each of Virgin Australia and Air New Zealand operated two services a week on the Sydney – Queenstown route. Both airlines operated these services on a Tuesday and a Saturday departing within 30 minutes of each other. The Applicants submit that this day of the week clash and wingtip flying did not reflect higher demand at this time but was due to each airline optimising its schedule operation in isolation. As a consequence, a person wishing to travel on a direct service from Sydney to Queenstown could only fly with Virgin Australia or Air New Zealand on a Tuesday or Saturday, enabling a 3, 4 or 7 night stay. As a result of the Alliance the Applicants adjusted their schedule on the Sydney – Queenstown route to operate services on every day of the week except Thursday.

A*CCC view*

201. In relation to the wingtip flying claims, the ACCC notes on many of these routes, there has been a reduction in the number of sectors flown per season. It is not clear what percentage of the change in wingtip flying is a result of increased schedule spread compared to what can be attributed to simply removing flights. The ACCC considers that to the extent the reduction in wingtip flying is linked to better schedule spread, the Alliance has resulted in, and is likely to continue to result in, greater variation in flight schedules, which is a public benefit to consumers who value greater choice of departure or arrival time.

202. Weighed against this, the ACCC considers that wingtip flying often reflects competition between airlines during peak periods. By aligning flight schedules during peak periods airlines are able to maximise the number of potential customers and, hence, revenues or profits. Thus a reduction in wingtip flying may also evidence a reduction in competition.

203. However, as long as there are rival airlines that are able to step in to meet any unmet demand for peak services under the Alliance, the ACCC recognises that increased schedule spread is a source of public benefit.

204. The ACCC notes that, based on the data supplied by the Applicants, the removal of day of week clashes is limited to the Sydney – Queenstown route.

205. Taking all this information into account, the ACCC considers on balance that the reduction in wingtip flying through increased schedule spread and the removal of day of week clashes is likely to have, and is likely to continue to result in public benefit. However, based on the information provided by the Applicants about their schedule optimisation the ACCC considers that this benefit is likely to be small.

Greater loyalty program benefits

206. The Applicants in their 2010 application submitted that the Alliance will benefit passengers by providing for reciprocal access to loyalty programs. Under the Alliance, members of Air New Zealand's frequent flyer program will be able to earn and use frequent flyer points under Virgin Australia's loyalty program and vice versa.

2010 determination

207. The ACCC has previously accepted that there are public benefits from increased opportunities for passengers of Alliance partners to earn and redeem frequent flyer points on each other's flights.

208. In the 2010 determination, the ACCC accepted that there are public benefits from increased opportunities for passengers of either of the Applicants being able to earn and redeem frequent flyer points on each others' flights.

209. The ACCC accepted that the attractiveness of Virgin Australia's loyalty program was likely to be enhanced under the Alliance and considered that the public benefits from reciprocal access to loyalty programs are likely to accrue to trans-Tasman passengers who:

- under the Alliance, prefer to fly with Virgin Australia or Air New Zealand, rather than Qantas, Emirates or other airlines flying the Trans-Tasman;
- are members of an Alliance loyalty program; and
- value the ability to earn or use frequent flyer points.

Applicants' submissions

210. The Applicants submit that since 26 July 2011, they have offered guests frequent flyer reciprocity on their respective networks. The reciprocal loyalty program access negotiated as a result of the Alliance includes earning and redeeming points across the entire Air New Zealand and Virgin Australia networks including the trans-Tasman, domestic Australia, domestic New Zealand and long haul sectors excluding sectors to/from the Pacific Islands. Such access would not have been agreed without the Alliance.

211. The frequent flyer reciprocity under the Alliance translates to the ability for passengers to earn and burn on over 160,000 more one way services per year. In Year 1, Virgin Australia passengers gained access to frequent flyer benefits on an additional 190,000 Air New Zealand services and Air New Zealand passengers gained access to frequent flyer benefits on an additional 161,000 services compared to the Pre-Alliance Year.

212. The Applicants also submit that there has been a substantial increase in Velocity frequent flyer membership[51] since the implementation of the Alliance.

[51] Velocity is Virgin Australia's loyalty program

ACCC view

213. The Applicants have confidentially provided the ACCC with data to indicate the number of Virgin Australia frequent flyers who have redeemed flights on Air New Zealand and vice versa. Based on this data, the ACCC considers that the Alliance has resulted in public benefits for these customers, but that the overall magnitude of this benefit is small.

214. The ACCC understands that the attractiveness of loyalty programs is defined by the ability to earn and redeem points on a wide range of network options (frequencies and destinations). The ACCC also understands that passengers value the ability to travel for leisure using points earned while travelling for business with their employer's preferred airline.

215. The ACCC remains of the view that the attractiveness of the Applicants' loyalty programs will be significantly enhanced under the Alliance and that the benefits of reciprocal access to loyalty programs are likely to accrue to Alliance passengers who:

- under the Alliance, prefer to fly with Virgin Australia or Air New Zealand, rather than Qantas, Emirates or other airlines flying the Trans-Tasman;
- are members of an Alliance loyalty program; and
- value the ability to earn or use frequent flyer points.

216. While the ACCC considers that the Alliance has delivered small public benefits in the form of loyalty program benefits thus far, the ACCC recognises the limited period the Alliance has been in operation. Therefore, the ACCC remains of the view that, given the large number of frequent flyer members and the range of benefits that might accrue to them, reciprocal access to the Applicants' frequent flyer programs with the Alliance is likely to result in material public benefits compared to the future without the Alliance.

Lounge access

217. The Applicants in their 2010 application submitted that the Alliance will benefit passengers by providing for reciprocal lounge access.

2010 determination

218. In the 2010 determination the ACCC accepted that:

- lounge access was important to business passengers and to the Alliance's plans to better target corporate accounts and business travellers;
- air-side lounges are of greater value to business customers than land-side lounges; and
- the Alliance is likely to provide Air New Zealand with stronger incentives to serve Virgin Blue/Pacific Blue customers on an equal basis under the Alliance than under an access arrangement between rivals.

219. On this basis, the ACCC considered that the public benefits from reciprocal access to Alliance lounges are likely to accrue to trans-Tasman passengers who:

- under the Alliance, prefer to fly with Virgin Australia or Air New Zealand, rather than Qantas, Emirates or other airlines flying the trans-Tasman; and

- are eligible to access lounge facilities.

Applicants' submissions

220. Prior to the Alliance, Virgin Australia customers had no international lounge access in Australia or New Zealand and no domestic lounge access in New Zealand. Similarly, prior to the Alliance, Air New Zealand customers travelling on domestic Australian services had no lounge access.

221. The reciprocal access to the Applicant's respective loyalty programs in relation to Alliance and non-Alliance journeys (excluding the Pacific Islands) negotiated under the Alliance, has (depending on frequent flyer membership tier and/or the fare purchase) allowed:

- Virgin Australia passengers to access Air New Zealand's six international air-side lounges on the trans-Tasman and Air New Zealand's 12 domestic lounges; and

- Air New Zealand passengers to access Virgin Australia's eight domestic Australia lounges.

222. A list of the lounges provided by each airline is set out below.

Air New Zealand	Virgin Australia
Auckland (International and Domestic)	Adelaide
Brisbane International	Brisbane Domestic
Christchurch (International and Domestic)	Canberra
Dunedin	Gold Coast
Hamilton	Mackay
Invercargill	Melbourne Domestic
Melbourne International	Perth
Napier	Sydney Domestic
Nelson	
New Plymouth	

Palmerston North	
Sydney International	
Tauranga	
Wellington (International and Domestic)	
Queenstown	

ACCC view

223. The Applicants provided to the ACCC, on a confidential basis, the number of Airpoint[52] members entering Virgin Australia lounges and the number of Velocity members entering Air New Zealand lounges.

224. Based on this information, the ACCC considers that the Alliance has resulted in public benefits to consumers in the form of reciprocal lounge access, but that the magnitude of these benefits to date has been small. Notwithstanding this, the ACCC remains of the view that public benefits from reciprocal access to Alliance lounges are likely to accrue to trans-Tasman passengers who under the Alliance, prefer to fly with Virgin Australia or Air New Zealand, rather than Qantas, Emirates or other airlines flying the Trans-Tasman who are eligible to utilise lounge facilities. The ACCC considers that as Virgin's Game Change strategy matures, and the number of passengers travelling business class or otherwise having lounge access (for example through paid Virgin Lounge membership) increases the Alliance is likely to result in material public benefits in the future.

Expected new frequencies under the Alliance

225. In their 2010 application for authorisation, the Applicants stated that the Alliance would enable them to increase frequencies by an additional 326 frequencies per annum comprising additional frequencies on Auckland-Coolangatta, Auckland-Perth, Brisbane-Wellington, Melbourne-Wellington and Sydney-Wellington.

2010 determination

226. In 2010, the Applicants advised specifically that they intended to introduce the following:

- Auckland-Adelaide: Daily services from November to and including March and five to six services weekly from April to October. This was up from the seasonal schedule of four to six services per week. It represented an additional 97 frequencies per annum;

- Auckland-Gold Coast: Double daily services from July to and including September and 12 services weekly from October to and including June.

52 Airpoints is Air New Zealand's loyalty program

This was up from up from the seasonal schedule of 11 to 13 services per week. It represented an additional 65 frequencies per annum;

- Auckland-Perth: Year round daily services. This was up from the seasonal schedule of five to seven services per week. It represented an additional 47 frequencies per annum;

- Wellington-Sydney: Double daily services from January to and including April, 13 services weekly from July to and including December and 12 services weekly from May to and including June. This was up from the seasonal schedule of 11 to 14 services per week. It represented an additional 83 frequencies per annum;

- Wellington-Melbourne: Daily services from November to and including April, six services weekly from July to and including October, and five services weekly from May to and including June. This was up from the seasonal schedule of five to seven services per week. It represented an additional 16 frequencies per annum; and

- Wellington-Brisbane: Year round double daily services. This was up from the seasonal schedule of 13 to 14 services per week. It represented an additional 18 frequencies per annum.

227. On this basis, the ACCC accepted in its 2010 determination that the Alliance would result in a number of new trans-Tasman frequencies which would directly benefit passengers.

Applicants' submissions

228. In their current application, the Applicants submit that they:

- have added the additional frequencies proposed on Auckland-Adelaide, Auckland-Perth, Brisbane-Wellington and Melbourne-Wellington routes;

- have increased frequencies under the Alliance by an additional 310 return trips per year on non-Christchurch routes;

- have implemented some additional frequencies in peak periods on Sydney-Wellington. However, there was not the demand for these to be sustained year round;

- have proposed double daily services from July through September and 12 services weekly from October through June on the Auckland-Coolangatta sector. Both Applicants operate on this route and the Applicants have maintained a strong schedule with improved spread as well as up to 13 services per week in the peak months of July, December and January. While the Alliance has not yet reached the anticipated level of services for all months of the year, some of the anticipated demand for these services will have formed part of the growth on related routes such as Christchurch-Coolangatta, Auckland-Brisbane and the new Auckland-Sunshine Coast services;

- have started the new seasonal services from Auckland to the Sunshine Coast twice a week between July and September 2012, and intend to operate these services again in the northern summer 2013 season; and

- will commence a new service on Christchurch-Perth from December 2013 to April 2014.

229. In addition, instead of increasing frequency on Auckland-Perth, Air New Zealand upgauged its daily Auckland-Perth service from a Boeing 767 to a Boeing 777 on 3 September 2012. This will result in approximately 66,430 additional seats (for Year 2 compared with the Pre-Alliance Year). This has also resulted in an improved product being provided to customers with lie flat business class seats and a premium economy offering.

230. The Applicants also note that due to a drop in demand following the Christchurch earthquakes there was a reduction of 465 return trips on Christchurch routes, over the two year period of the Alliance.

ACCC view

231. The ACCC notes that the Applicants introduced the new frequencies proposed in 2010 on three of the six routes, with limited increases in frequency and capacity achieved on two of the remaining three routes. In addition the Applicants have commenced services on the Sunshine Coast – Auckland route and have launched a new service on the Christchurch-Perth route.

232. In response to requests from the ACCC, data supplied by the Applicants indicates that since the implementation of the Alliance the net increase in frequencies has been 227 per annum.[53] The ACCC notes that this figure may have been higher, had it not been for the reduction in frequencies on the Christchurch routes as a result of the Christchurch earthquake.

233. The ACCC considers that it is reasonable that some, but not all, of these increased frequencies may be attributed to the Alliance. In particular, the ACCC considers, based on the confidential information provided by the Applicants, that it is likely the commencement of the Auckland – Sunshine Coast and Christchurch-Perth routes can be attributed to the Alliance. On this basis, the ACCC considers that the frequencies which were added are likely to be of benefit to the public, and may not be sustained absent the Alliance. As a result the ACCC considers that the continuation of the Alliance is likely to result in material public benefits in the form of the increased frequencies remaining available to passengers.

[53] One way scheduled services. Figure represents the difference in the number of scheduled services for the year ending 31 October 2013 against the year ending 31 October 2010 (the pre-Alliance year).

Increased access to each other's frequencies and destinations

234. The ACCC has previously accepted that airline alliances can confer public benefits to Alliance customers by allowing them to access the other airline's schedule and, hence, additional frequencies and destinations.

235. Under the Alliance, Virgin Australia customers have access to 145 Air New Zealand frequencies and Air New Zealand customers have access to 71 Virgin Australia frequencies.

236. Absent the Alliance, a person who holds a Virgin Australia ticket but values the option of switching to an Air New Zealand flight can only switch to an Air New Zealand coded flight by purchasing a separate Air New Zealand fare. Similarly, a person who holds an Air New Zealand ticket but values the option of switching to a Virgin Australia flight can only switch to a Virgin Australia coded flight by purchasing a separate Virgin Australia fare.

237. Under the Alliance, customers can purchase either a Virgin Australia ticket or an Air New Zealand ticket and access any Alliance flight. In other words, under the Alliance, a person who holds a Virgin Australia (Air New Zealand) ticket has the option of switching to an Air New Zealand (Virgin Australia) flight, subject to seat availability, on similar terms as they would face to switch to an alternate Virgin Australia (Air New Zealand) flight.

2010 determination

238. In the 2010 determination, the ACCC considered that the increase in flight choice through the replacement of separate Virgin Australia and Air New Zealand coded frequencies with consolidated Alliance coded frequencies was likely to benefit consumers who:

- under the Alliance prefer to fly with Virgin Australia or Air New Zealand rather than Qantas or any other trans-Tasman airline; and
- value the increased flexibility associated with the greater number of frequencies.

Applicants' submissions

239. The Applicants submit that the implementation of codeshare sales on Alliance routes has allowed each of the Applicants to now offer a full range of flights between 26 airports in New Zealand and 34 airports in Australia.

ACCC view

240. The ACCC notes that according to BITRE data, Virgin Australia and Air New Zealand accounted for around four million (or 51% of) international passenger movements between Australia and New Zealand in the 12 months to February 2013.[54] However, not all of these passengers are likely to have based their decision to fly with Virgin Australia or Air New Zealand on the brand of the airline. The ACCC considers it is likely that most of these passengers based their decision

54 Bureau of Infrastructure, Transport and Regional Economics, Statistical Report: Aviation – International airline activity, August 2012, p.8 and p.10.

to fly with Virgin Australia or Air New Zealand on their preferences for other criteria such as price, timeliness of service, aircraft type or stopover option. Notwithstanding this, the ACCC accepts that a proportion of the passengers who choose to fly Virgin Australia or Air New Zealand likely do so because they have a preference for one of these airlines.

241. Given the number of additional frequencies available to Alliance customers and the number of Australian consumers who are likely to prefer to fly with either Virgin Australia or Air New Zealand, the ACCC considers that increased access to existing frequencies with the proposed conduct is likely to have resulted, and is likely to continue to result in public benefits. However, the magnitude of the benefit depends on the number of consumers who based their decision to fly with Virgin Australia or Air New Zealand on brand rather than other criteria such as price, timeliness of service, aircraft type or stopover options and the ACCC has not been able to reach a view on the magnitude of this benefit.

Overall public benefits from enhanced products and services

242. The ACCC recognises that the enhanced product and service offering under the Alliance is a key source of public benefit. In the 2010 determination, the ACCC considered that the Alliance was likely to materially enhance the Applicants' product and service offering by providing increased access to existing frequencies, increased online connection options, better schedule spread, enhanced value added services and supporting the introduction of new frequencies.

243. Having assessed the information provided by the Applicants and interested parties about the first two years of the operation of the Alliance, the ACCC considers that the Alliance has resulted in:

- material benefits in the form of new frequencies;
- material benefits in the form of loyalty program benefits, and lounge access;
- some benefits in the form of better schedule spread and online connections, although the magnitude of this benefit is small; and
- some benefits in the form of increased access to each other's frequencies, although the ACCC has not been able to reach a view on the magnitude of this benefit.

244. The ACCC considers that, collectively, the enhanced products and services delivered by the Alliance have resulted in a material public benefit.

245. The ACCC accepts that, due to the limited period the Alliance has been in operation, some of these benefits may not have been fully realised. The ACCC considers that this is likely to be the case in relation to benefits associated with lounge access, loyalty program benefits and online connections, and that these benefits may increase as the Applicants are able to sell integrated itineraries following Virgin Australia's migration to the SabreSonic platform.

246. Moving forward, the ACCC considers that it is likely that the Alliance will result in material public benefits in the form of ongoing new frequencies, increased access to each other's frequencies, lounge access and loyalty program benefits. In

addition the ACCC considers that the Alliance is likely to result in small benefits in the form of online connections, and better schedule spread.

Cost savings and efficiencies

247. In their 2010 application, the Applicants submitted that they envisaged that the Alliance would result in cost savings and efficiencies as a result of:

- higher load factors resulting in a lower cost per seat sold;
- joint procurement;
- co-location of certain functions and utilisation of common resources;
- operational optimisation; and
- removal of double marginalisation.

248. In their 2010 application, the Applicants submitted that there were real and immediate cost savings that could be achieved by the Alliance, and noted that sharing frequent flyer lounges and eliminating duplication at overlapping airports is a commonly realised benefit from aviation alliances. In their 2010 application the Applicants provided preliminary estimates of costs savings to the ACCC on a confidential basis.

249. In the 2010 determination, the ACCC accepted that the Alliance was likely to facilitate cost savings with respect to the services covered by the Alliance. The ACCC also remarked that it would be surprising if two substantial businesses such as Virgin Australia and Air New Zealand were not able to achieve some cost savings through joint rationalisation of aircraft operations and support services.

250. The ACCC considered that, in the absence of further information from the Applicants in relation to the Alliance, that the cost savings anticipated by the Applicants were non-trivial but not substantial.

251. Each of the Applicants' current claims in relation to cost savings and efficiencies is considered in more detail below.

Higher load factors resulting in a lower cost per seat sold

2010 determination

252. The ACCC noted in the 2010 determination that it considered that the public benefits associated with increased load factors under the Alliance may be material, but depended on the additional trans-Tasman traffic that the Alliance actually stimulates.

253. In 2010, the Applicants submitted that they estimated the magnitude of the cost savings, in terms of the reduction in cost per seat sold or cost per passenger, from these higher load factors to be broadly in the range of 3-6% per city pair with a few outliers above that.

Applicants' submissions

254. The Applicants submit that increased load factors under the Alliance have resulted in public benefits either directly through greater efficiency (i.e. lower cost per seat sold) or indirectly by supporting greater total output (i.e. increased capacity) and that the overall increase in passenger numbers under the Alliance is likely to have a combination of these effects.

255. For example, a plane has a set number of available seats and if the plane leaves the gate with empty seats, this inventory cannot be stored and is lost. That is, the overall costs of operating the flight are fixed, hence the greater the number of passengers on that flight the more efficient the use of the plane's "perishable" inventory, which is reflected in a lower average cost per seat sold.

256. The Applicants submit that the Alliance has resulted in higher load factors. The load factor on the trans-Tasman increased from the Pre-Alliance Year to Year 1 of the Alliance, at the same time as overall capacity has increased. The increased load factor achieved under the Alliance has resulted in a lower overall average cost per seat sold. In addition, as anticipated, travellers have also benefited indirectly from increased load factors supporting greater total output in the form of new routes and additional frequencies and capacity on existing routes.

ACCC view

257. Based on the data supplied by the Applicants on a confidential basis the ACCC considers that the effect the Alliance has had on load factors on the Alliance routes is unclear.

258. The ACCC considers that, to the extent that the Alliance stimulates additional passenger traffic and results in higher load factors, the Applicants stand to further reduce operating costs. Potentially, this includes servicing routes with higher load factors, using larger aircraft. On this basis, while the ACCC considers that higher load factors have the potential to result in public benefits, based on the information available, the ACCC cannot conclude that these benefits are likely to be a result of the Alliance.

Joint procurement

Applicants' submissions

259. The Applicants submit that they have and will continue to review opportunities for cost savings from joint procurement activities.

260. In November 2012, Air New Zealand announced that from early 2013 it would be moving its Australian ground handling contract to Toll Dnata, who also supply ground handling services for Virgin Australia. The Applicants submit that this move is largely attributable to the Alliance, and that Air New Zealand expects to realise cost savings.

261. The Applicants submit that large scale procurement such as fuel and ground handling are generally contracted for a number of years in advance. As existing arrangements expire, the Applicants expect to be able to capitalise on further cost saving opportunities.

ACCC view

262. The ACCC considers that to the extent that joint procurement leads to cost savings through the avoidance of duplicated fixed costs in procurement, this is likely to result in a public benefit. However, in this case, the magnitude of this benefit is likely to be small.

263. While the Alliance has resulted in some savings through the Applicants jointly procuring goods and services, it is unclear the extent to which these are savings brought about through real efficiencies of joint-procurement. In any case, based on information supplied confidentially to the ACCC, the magnitude of these savings are small relative to the overall operating costs of the Alliance.

Co-location of certain functions and utilisation of common resources

Applicants' submissions

264. The Applicants submit that they have also been able to achieve savings in operational areas. For example, Air New Zealand and Virgin Australia entered into an engine access agreement in December 2011 which enables the parties to pool their spare B777 engines and reduce the overall number of spares required to be held by each airline.

265. The Applicants submit that they are actively engaged in discussions about further cost savings opportunities, such as exploring opportunities to realise improvements and cost savings for other engine types. The cost saving initiatives currently being developed include sharing of knowledge, systems, personnel and joint training and use of Air New Zealand kiosk check in for international flights out of New Zealand and Sydney.

ACCC view

266. The ACCC considers that the utilisation of common resources under the Alliance is likely to have resulted in cost savings but considers that these savings are likely to have been small.

267. To the extent that co-location of functions and utilisation of common resources leads to the cost savings from avoiding duplicated fixed costs in the future, the ACCC considers that this is likely to result in a public benefit. However the ACCC remains of the view that the magnitude of this benefit is likely to be small.

Operational optimisation

Applicants' submissions

268. The Applicants' submit that the optimisation of their combined trans-Tasman network offering under the Alliance has allowed them to achieve cost savings by utilising their fleet in a more cost efficient way. This has created a more efficient network and schedule offering without the associated increase in fixed costs that would be incurred by the Applicants acting independently. For example:

- Virgin Australia is operating the seasonal Dunedin-Sydney and Dunedin-Melbourne services previously operated by Air New Zealand which complements the existing Virgin Australia schedule on Brisbane-Dunedin.

- Air New Zealand becoming the Alliance carrier on the Sydney-Wellington route utilises the market presence of Air New Zealand on this sector, while Virgin Australia has been able to utilise the advantages of its home hub in Brisbane by becoming the Alliance carrier on the Brisbane-Wellington route.

- Air New Zealand's operation of the Auckland-Cairns services allows the Alliance to take advantage of Air New Zealand's sales strength on a sector which is largely sold in New Zealand.

269. The Applicants also submit that the Alliance has enabled more effective handling of flight disruptions, including utilising each other's aircraft (both scheduled and non-scheduled flights) to re-accommodate passengers in a disrupt situation. Such assistance also saves costs. The Applicants submit that potential opportunities currently under review include the sharing of systems, personnel and resources and joint purchasing initiatives that leverage on combined buying power.

ACCC view

270. To the extent that operational optimisation leads to cost savings from avoiding duplicated fixed costs, the ACCC considers that this is likely to result in a public benefit.

271. The ACCC recognises that the Alliance has resulted in the optimisation of the combined trans-Tasman network offering of the Applicants but is unable to reach a conclusion about the magnitude of this benefit.

Removal of double marginalisation

272. Double marginalisation is a situation that occurs where suppliers of vertically related or complementary products each enjoy a degree of market power and independently charge a price which includes a mark-up over their costs and do not take account of the impact on the other firm's profit. [55] The net result is both higher prices and lower profits than if the two firms coordinated their pricing, for example

[55] The ACCC notes that in practice all firms have some degree of market power and charge a price which is above marginal cost. That is, all firms face a downward sloping demand curve.

through vertical integration or a joint venture.

2010 determination

273. In their 2010 application for authorisation, the Applicants stated that the Alliance would create the opportunity for reduced costs for connecting services. In particular it would facilitate more low cost code share inventory, which would enable the parties to offer a more competitive combined fare for connecting services than was possible under an arms-length arrangement.

274. In the 2010 determination, the ACCC:

- noted that, to the extent that either Virgin Australia on the domestic Australian segment or Air New Zealand on the trans-Tasman segment possessed a degree of market power, then the ACCC accepted that double marginalisation could be a problem on complementary flight segments of an itinerary from New Zealand to Australia utilising the services of two or more airlines;

- noted that, to the extent that either Air New Zealand on the domestic New Zealand segment or Pacific Blue on the trans-Tasman segment possessed market power, then double marginalisation could be a problem on complementary flight segments of an itinerary from Australia to New Zealand utilising the services of two or more airlines; and

- accepted that revenue sharing under the Alliance would give the Applicants an incentive to offer fares on complementary flights that incorporate a lower margin than the margin embodied in the fares that Air New Zealand currently offered Qantas under the interline agreement.

275. In its 2010 determination, the ACCC considered that the extent of public benefit arising as a result of the removal or reduction of double marginalisation was likely to depend on:

- the proportion of total trans-Tasman passengers that are expected under the Alliance to purchase onward (complementary) flights beyond current destination points in Australia and New Zealand;

- the degree of market power held by Virgin Blue in the Australian domestic market, Pacific Blue in the trans-Tasman market and Air New Zealand in the trans-Tasman and domestic New Zealand markets. This would be reflected in the magnitude of the mark-up above cost that these airlines realise on specific routes prior to the Alliance; and

- the extent to which the airlines expected these mark-ups would be reduced under the Alliance.

Applicants' submissions

276. The Applicants submit that revenue sharing under the Alliance has provided the Applicants with the incentive to offer cost reflective fares on complementary flights leading to the realisation of the benefits of reduced pro-rate costs and the removal of double marginalisation. As a result, the Applicants have been able to pass through these lower costs on connecting services to consumers via lower fares.

For example, in Year 1, Air New Zealand sold journeys that included a domestic Australian sector at a lower fare level than in the Pre-Alliance Year. In relation to Virgin Australia, New Zealand connectors are not as significant due to the large number of direct flights to key New Zealand ports. Virgin Australia also did not have an interline arrangement with another airline on trans-Tasman routes prior to the Alliance to allow a comparison of the pro-rates available to it.

277. The Applicants submit that the wide spread benefit of these lower fares to consumers is reflected in the fact that Air New Zealand sold additional journeys that included a domestic Australian sector since the commencement of the Alliance.

278. The Applicants submit that some connecting fares have only been made possible following Virgin Australia's migration to SabreSonic in January 2013. Prior to this time, Virgin Australia did not have the ability to support the creation of such itineraries and the development of these products was challenging, due to IT incompatibilities.

ACCC view

279. The Applicants supplied to the ACCC on a confidential basis the number of Alliance passengers who utilised a connection at both ends of their trans-Tasman journey.

280. The ACCC considers that the majority of the trans-Tasman passengers who utilised a connection in Australia in 2012 likely completed their entire journey with Qantas, Jetstar or Virgin Australia. These passengers would therefore not have been subject to double marginalisation on complementary flights.

281. The ACCC considers that all of the Air New Zealand travellers who utilised a connection in New Zealand would have been able to complete their entire journey with Air New Zealand. They therefore would not have been subject to double marginalisation on complementary flights.

282. The ACCC remains of the view that the removal of double-marginalisation under the Alliance is a benefit to trans-Tasman passengers who:

- prefer to travel with one of the Applicants post-Alliance; and
- utilise a connection in Australia or a connection in New Zealand beyond the trans-Tasman gateway destinations that would not be available absent the Alliance.

283. The extent of benefit available to each of these passengers is likely to vary across routes. Air New Zealand has provided confidential data to the ACCC which indicates that the Alliance has reduced pro-rate costs on most routes.

284. The ACCC considers that the removal of double-marginalisation under the Alliance is a benefit to trans-Tasman passengers who prefer to travel with one of the Applicants and utilise a connection in Australia or a connection in New Zealand beyond the trans-Tasman gateway destinations that would not have been available absent the Alliance. However, in light of the confidential information provided by the Applicants, the ACCC considers that the magnitude of this benefit is currently minimal, but is likely to result in small public benefits going forward as the number of passengers utilising such connections grows.

Pass through of cost savings and efficiencies

285. The ACCC considers that cost saving and efficiencies are a public benefit in and of themselves. However, the ACCC gives greater weight to cost savings where they are likely to be passed through to consumers in the form of lower fares.

286. The Applicants submit that average fares have decreased under the Alliance, and have provided confidential data to support this claim. CIAL submit that this claim is misleading because the calculation of 'average fares' does not reflect the price consumers typically pay when travelling. CIAL suggests a more appropriate measure of the change in fare levels would be the median price paid.

287. CIAL also submits that the fares do not take into account the additional charges that passengers pay for luggage, meals and in-flight entertainment.

288. The ACCC notes that at this stage it is difficult to determine whether changes in fares may be attributed to the Alliance.

289. The ACCC considers that the likelihood of cost savings and efficiencies achieved by the Alliance being passed through to consumers will depend on competitive conditions year to year. The ACCC remains concerned that on certain trans-Tasman routes the Alliance may find it more profitable to raise fares rather than lower them. These concerns are discussed in the public detriment section below. The ACCC notes, however, that the proposed conditions of authorisation will go some way toward preserving incentives for pass through of cost savings and efficiencies by the Alliance.

Overall public benefits from cost savings and efficiencies

290. The ACCC considers that it is likely that the Alliance has delivered cost savings and efficiencies, and that the continuation of the Alliance will result in further cost savings and efficiencies. However, as noted above, in most instances the magnitude of these cost savings are small relative to the overall operating costs of the Alliance.

291. The Applicants submit that many of the cost savings achievable under the Alliance could not be fully realised in the first 18 months of implementation and are still to come. These include cost savings that will be delivered over time from better fleet planning and operational changes and cost savings from improved or more efficient contractual arrangements with suppliers.

292. The ACCC considers that the Alliance may result in further cost savings over the medium term, however the ACCC considers that the cost savings and efficiencies likely to be delivered by the Alliance in the future are not likely to be significant. On this basis the ACCC considers that the cost savings and efficiencies generated by the Alliance are likely to result in some, likely small, public benefits.

Promotion of competition

293. In their 2010 application, the Applicants submitted that the Alliance will strengthen Virgin Australia for ex-Australia outbound travel on the trans-Tasman, and the overall position of Virgin Australia vis-a-vis the Qantas Group.

294. In the 2010 determination, the ACCC:

- accepted that the Alliance was likely to enhance the Applicants' product and service offering, and may lead to lower fares (to the extent that cost savings and efficiency gains are passed through to consumers);
- considered that this had the potential to trigger a competitive reaction from the Qantas Group;
- acknowledged that the Alliance gave Virgin Australia an ability to offer additional trans-Tasman frequencies and domestic connections in New Zealand;
- noted that the central issue was whether, by enabling these additional frequencies and connections, the Alliance stimulates a more vigorous competitive response in the business traveller segment of the trans-Tasman market than would occur absent the Alliance; and
- considered that, while it was early days, Virgin Australia's new business model appeared to be helping to win corporate and government customers in Australia from Qantas.

295. In considering whether the Alliance is likely to result in a public benefit through generating a competitive response in the future, the ACCC has used the same framework as in the 2010 assessment. The ACCC considers that a competitive response to the Alliance may be generated on either the trans-Tasman routes or on domestic Australian routes, both of which are considered in more detail below.

296. The Applicants submit that the enhanced product and service offering under the Alliance allows them to achieve a better competitive position on the trans-Tasman and more generally within Australasia against the Qantas Group. The Applicants submit that for Virgin Australia this is due to the fact that the trans-Tasman is a key market for corporate contracts and that, without the Alliance, Virgin Australia cannot match Qantas' trans-Tasman product in terms of frequency and schedule or frequent flyer and lounge benefits. The Applicants submit that for Air New Zealand, the Alliance addresses limitations to its stand alone competitive offering such as a lack of access to onward connections in Australia, a lack of effective marketing presence within Australia, and a lack of effective Australian sales and distribution channels.

297. As discussed above under the headings 'enhanced products and services' and 'cost savings and efficiencies', the ACCC considers that the Alliance has resulted in enhanced products and services and some cost savings and efficiencies in its first two years of operation, and that these are likely to continue in the future.

298. The ACCC also notes the largely complementary nature of the Virgin Australia and Air New Zealand domestic networks. As discussed in the **background** section, Virgin Australia has a large Australian domestic presence but no operations in New Zealand, while the reverse is true for Air New Zealand. The ACCC considers that the network offered by the Alliance is greater than either airline could have offered alone and that the Applicants may be able to leverage this integrated network to attract passengers who otherwise might not have flown with either Virgin Australia or Air New Zealand. The ACCC also considers that the Alliance will give each airline greater access to sales and distribution channels. For example it will enable

Air New Zealand to market Alliance flights within New Zealand, and for Virgin Australia to market the same flights within Australia. The ACCC notes that Air New Zealand is likely to have a greater sales presence in New Zealand, and Virgin Australia is likely to have a greater sales presence in Australia.

299. The ACCC also notes that the main competitor to the Alliance – the Qantas Group – has domestic networks in Australia and New Zealand,[56] whereas Virgin Australia only has an Australian domestic network and Air New Zealand only has a domestic network in New Zealand.

300. Accepting that the Alliance is likely to result in an enhanced product and service offering, the key question is whether the Alliance has stimulated a more vigorous competitive response on the trans-Tasman, particularly in relation to business travellers, than would occur absent the Alliance, and whether this is likely to continue in the future.

Promotion of competition on trans-Tasman routes

301. The Applicants submit that since the authorisation of the Alliance there has been a competitive response in the form of frequent and aggressive tactical pricing activity. For example, comparing the period from January to August 2010 with the same period in 2012, there has been an increase in the total frequency of tactical sales activity on the Auckland-Sydney route. In particular the Applicants submit that, Qantas, Jetstar and Emirates increased their sales activity over that period. The Applicants consider that the Auckland-Sydney route is representative of the increased tactical sales activity across other trans-Tasman sectors due to each airline generally releasing network wide sales.

302. The Applicants also submit that the Alliance has resulted in a competitive response in the form of the entry of China Airlines onto Auckland-Brisbane in 2011 and its expansion onto Auckland-Sydney in October 2012. Jetstar and Emirates have also expanded their trans-Tasman operations. The Applicants note that there have been substantial increases in capacity by Emirates (13.3%), Jetstar (5.2%), LAN (4.2%) and Qantas (2.1%) on the trans-Tasman from the Pre-Alliance Year to Year 1. Since November 2012, Jetstar has increased capacity further with an additional aircraft to its New Zealand based fleet.

303. As the ACCC notes in the **public detriments** section below, decisions to enter routes or add capacity by a FFC are primarily made with reference to the viability of the long haul component of its service (international into Australia) before deciding whether to extend that service into New Zealand. On this basis, the ACCC considers that it is unlikely that the expansion by the FFCs can be attributed to a competitive response to the Alliance. The ACCC considers that it is unclear whether the increases by Jetstar and Qantas are a competitive response to the Alliance, or simply reflect the continuation of the historical trend of capacity additions on the trans-Tasman.

304. The Applicants submit that the Alliance has enabled Virgin Australia to access more of the corporate segment than would otherwise be the case and that they have seen significant growth in corporate revenue as a result of the Alliance.

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56 Jetstar operates four domestic New Zealand services between Auckland and Wellington/Christchurch/Queenstown; and between Christchurch and Queenstown.

305. The Applicants also submit that the Alliance has enabled them to retain significant corporate contracts and attract new corporate contracts which might previously have been signed with Qantas. This is due to the greater scope of benefits available to consumers under the Alliance than could be offered by the Applicants on their own and has allowed Virgin Australia to quickly and efficiently provide customers with a stronger product offering in competition with the Qantas Group promoting competition for air travel within and to/from Australia and giving Australian travellers the choice of a second Australian based international airline.

306. The ACCC considers that it is reasonable to conclude that the Alliance, through increasing the breadth and depth of services offered by the Applicants, may have been a factor in the Alliance attracting and retaining corporate customers on the trans-Tasman, including customers that may have otherwise signed with Qantas. In this regard, the ACCC notes that the Applicants have provided, on a confidential basis, some evidence to substantiate this claim.

307. The ACCC considers that the Alliance, through providing the Applicants with domestic networks on both sides of the trans-Tasman, may make it a stronger competitor to the Qantas Group, and therefore has the potential to trigger further competitive responses from the Qantas Group.

308. While the Alliance increases the attractiveness of the combined offering, it also removes competition between Virgin Australia (the third largest player) and Air New Zealand (the largest player), including in the business traveller segment of the trans-Tasman market. The extent to which this will mitigate the pro-competitive effect of the Alliance will depend on the likely strength of the individual offerings of Virgin Australia and Air New Zealand in the likely future without the Alliance.

309. In this regard, the ACCC notes Virgin Australia's submissions that it would be severely impacted in the future without the Alliance, due to its limited depth and breadth of schedule, and that Air New Zealand's ability to attract Australian-based passengers and access behind gateway points in Australia will be diminished.

310. Virgin Australia also submits that without the Alliance its financial performance will deteriorate and will need to review its schedule with a view to rationalising less profitable services. On this basis, the ACCC considers that Virgin Australia is unlikely to have a compelling offer on the trans-Tasman absent the Alliance, particularly in relation to the business traveller segment.

311. The ACCC notes that Virgin Australia has adopted a strategy of creating a 'virtual network' through alliances with international carriers such as Singapore Airlines, Etihad and Air New Zealand. This has formed a key element to Virgin Australia's Game Change strategy, designed to attract higher yield corporate and business passengers while remaining attractive to leisure passengers. Virgin Australia submits that its Game Change strategy is designed to improve its network and product in order to expand its passenger base and challenge its closest competitor Qantas across more market segments, providing enhanced choice and competition for all Australian passengers.

312. As discussed under the heading **enhanced products and services** above, the Alliance provides Virgin Australia passengers with access to international lounges and increased earning and redemption options through Virgin Australia's frequent flyer program. The result of these enhanced services is that Virgin Australia is in a

better position to compete for corporate customers on the trans-Tasman than it otherwise would have been absent the Alliance.

313. The ACCC therefore considers that the Alliance is likely to have improved, and is likely to continue to strengthen, Virgin Australia's ability to contest the business traveller segment of the trans-Tasman, and that this is likely to result in material public benefits. To the extent that the Alliance is attractive to corporate customers, the ACCC accepts that the Alliance may increase competitive pressure on Qantas in the market for business passengers, meaning the Alliance could also benefit Qantas passengers as a result of Qantas' response to this competitive pressure.

Promotion of competition on Australian domestic routes

314. The Applicants also submit that the Alliance facilitates them competing more effectively with the Qantas Group for both leisure and business passengers throughout Australasia, including in the Australian domestic market.

315. In market inquiries undertaken by the ACCC, a number of large customers of Virgin Australia indicated that Virgin Australia's corporate offer is considerably more attractive now than it was two years ago. They attribute this to better lounge access, a better frequent flyer program and incidental improvements such as faster disembarking times.

316. The ACCC understands that corporate customers may contract separately for their domestic and trans-Tasman travel requirements, and that these contracts are generally non-exclusive in nature. The ACCC understands that corporate customers primarily take into account the initial domestic fare schedules and the discount from domestic fare schedules in making decisions about contracting with airlines. However, the ACCC also understands that this varies across corporate customers and depends on the individual travel needs of those customers. Based on additional confidential information, the ACCC understands that for some corporate customers the Applicants' Alliance offering may be important.

317. Therefore the ACCC considers that it is not clear precisely what impact the Alliance has had on the attractiveness of Virgin Australia to domestic Australian corporate customers, given that customers may acquire the domestic and trans-Tasman components separately and non-exclusively. The ACCC accepts that some customers may have a preference for bundling domestic and trans-Tasman travel with a single provider, and for these customers the Alliance may hold more significance.

318. However, the ACCC notes that the Alliance forms part of Virgin Australia's Game Change strategy which is designed to attract higher yield corporate passengers. The strategy is intended to improve Virgin Australia's network and product in order to expand its passenger base and challenge Qantas across more market segments, providing enhanced choice and competition for all Australian passengers.

319. The ACCC considers that the Game Change strategy has resulted in a competitive response from the Qantas Group on domestic Australian routes. To the extent the virtual networks, including the Alliance, contribute to the Game Change strategy and enable Virgin Australia to better compete with the Qantas Group domestically, the ACCC considers that it is likely that this will generate further competitive

responses. On this basis, the ACCC considers that the Alliance is likely to result in public benefits, but as the contribution the Alliance makes to the Game Change strategy is uncertain, the ACCC is unable to determine the magnitude of this benefit.

Conclusion on promotion of competition benefits

320. The ACCC considers that the Alliance, through increasing the breadth and depth of services offered by the Applicants, may have been a factor in the Alliance attracting and retaining corporate customers on the trans-Tasman, including customers that may have otherwise signed with Qantas. The ACCC considers that the Alliance, through providing the Applicants with domestic networks on both sides of the trans-Tasman, may make it a stronger competitor to the Qantas Group, and therefore has the potential to trigger further competitive responses from the Qantas Group. This is likely to result in public benefit.

321. The ACCC also considers that Virgin Australia's Game Change strategy has resulted in a competitive response from the Qantas Group on domestic Australian routes. However the contribution the Alliance makes to the Game Change strategy is uncertain. Therefore the ACCC is unable to determine the magnitude of this benefit in relation to the domestic Australian market.

Stimulation of tourism

322. In their 2010 application, the Applicants submitted that the stimulation of passenger traffic on the trans-Tasman under the Alliance will also stimulate tourism.[57] In particular, the Applicants submit that the Alliance is likely to increase the attractiveness of Australia for New Zealanders when choosing a travel destination within the region. The ACCC notes that New Zealand is Australia's largest inbound market with 1.1 million New Zealand tourists visiting Australia in year ended December 2012, representing around 20% of total inbound tourist arrivals to Australia.[58]

323. The Applicants submit that the key drivers of incremental tourists as a result of the Alliance will arise from:

- the improved product offered by the Alliance;
- the increased competition in the Australasian market and greater consumer choice via the creation of a second comprehensive Australasian network in competition with the Qantas Group;
- incentives to jointly promote travel on Alliance services on a metal neutral basis and; and

[57] Applicants' *Submission in response to interested party submissions*, 26 July 2010, page 8.
[58] Tourism Research Australia, International Visitors in Australia – results of International Visitor Survey – December 2012.

- the Alliance's improved distribution channels.[59]

324. Specifically, the Applicants suggested that tourism in destinations beyond the East Coast Gateways, including the Northern Territory, Western Australia and South Australia, would benefit.

325. The ACCC has noted previously in a number of airline alliance authorisations that there are a wide range of factors which influence tourism demand for Australia as a destination, including general purchasing power in source countries, the relative cost of other destinations, the total cost of visiting Australia (land as well as air component) and the perceived quality of Australia as a destination.[60]

326. In 2010, the ACCC accepted that stimulation of tourism is a potential source of public benefit under the Alliance. The ACCC considered that the principal ways in which the Alliance is likely to stimulate tourism is through:

- increased passenger traffic as a result of enhanced products and services and, potentially, lower fares to the extent that, on balance, the Alliance promotes rather than lessens competition and the Applicants pass through cost savings and efficiency gains to consumers; and

- exploitation of synergies through joint rather than separate tourism promotion activity.

Stimulation of tourism through an enhanced product and service offering and increased passenger traffic

327. In the 2010 determination, the ACCC accepted that the Alliance makes it more convenient for travellers who wish to travel beyond trans-Tasman gateway destinations in Australia and New Zealand to do so.

328. However the ACCC considered that the number of origin-destination combinations where the Alliance creates a new online connection option (rather than an alternative online connection option) is likely to be very small given that there are already reasonably extensive point to point origin-destination options between New Zealand and East Coast Australia and neither the New Zealand airports or the East Coast Australian airports have extensive, high traffic beyond points.

329. The Applicants submit that New Zealand is Australia's largest source of inbound tourism. There was A$2.1 billion in total spend from New Zealand travellers to Australia in 2011 and the Tourism 2020 strategy estimates that New Zealand tourism has the potential to grow to between A$3.4 billion and A$4.2 billion in total expenditure by 2020.[61]

330. The Applicants submit that the Alliance has resulted in increased passenger traffic on Alliance services and increased online connections and that the Alliance has

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59 Submission *in support of the Application for Authorisation of the Virgin Blue and Air New Zealand Australasian Airline Alliance*, 4 May 2010, page 50-51.

60 ACCC Determination for applications A91097 and A91098 lodged by Air New Zealand Limited and Air Canada, January 2009, page 23.

61 Virgin Australia & Air New Zealand, Submission in support, 7 March 2013 citing Tourism Australia.

and will continue to allow for increased short haul tourism and long haul dual destination tourism.

331. The Applicants consider that an important characteristic of long haul international tourists to Australia is their propensity to take the opportunity to visit other destinations at the same time. In order to attract dual destination travel it is important to be able to offer extensive domestic Australian and New Zealand networks.

332. The Applicants submit that the Alliance has these characteristics and both partners are committed to development of fare products which support these objectives. Such products are technically possible following Virgin Australia's migration to SabreSonic and the Rivera revenue accounting platform. Prior to migration, Virgin Australia did not have the ability to support settlement of such itineraries and the development of these products was challenging, due to IT incompatibilities.

333. The ACCC remains of the view that the increased online connection options under the Alliance are also available to long-haul international passengers. This has the potential to confer tourism benefits to Australia and New Zealand to the extent that the Alliance makes it easier for potential visitors to plan an Australia and New Zealand trip.

Stimulation of tourism through joint tourism promotion

334. The Alliance provides the opportunity for the Applicants to exploit synergies through joint promotion of tourism.

335. In the 2010 determination, the ACCC considered that the realisation of tourism-related public benefit in practice will depend on the strength of incentives for the Applicants to jointly promote tourism under the Alliance as well as their level of commitment to such joint promotion.

336. The ACCC accepted that, under the Alliance, the Applicants have an incentive to jointly operate their activities in respect of tourism promotion. The ACCC has been provided with confidential cost information in respect of this claimed benefit.

337. The Applicants submit that:

- they both have relationships with Tourism New Zealand (**TNZ**) and regional New Zealand tourism organisations. Together they support the Alliance network by ensuring that both airlines maximise airtime within TNZ activity;
- the Alliance's ability to jointly host familiarisation groups and media has expanded these marketing arrangements so that new, non-gateway destinations can now be showcased to the consumer. For example, in September 2012 the Alliance undertook a joint marketing venture with Tourism Western Australia for Broome. Air New Zealand transported a familiarisation group to Perth while Virgin Australia carried them from Perth to Broome;
- another example of a joint marketing endeavour made possible under the Alliance was the Seniors Card promotion with AAT Kings & Tourism

Tasmania. The prize-winners were awarded a ticket from New Zealand to Hobart. Air New Zealand carried passengers across the Tasman while Virgin Australia carried passengers to Hobart;

- examples of marketing investment by the Applicants are the "Just 3 hours away" winter campaigns in 2011 and 2012 and "The Kiwi Sceptics" campaigns in 2012. The work has gained considerable attention in Australia, with Kiwi Sceptics recognised globally in creative awards, and indications that consideration of New Zealand, Air New Zealand and Virgin Australia has grown as a result;

- the Alliance actively works with TNZ to promote and stimulate tourism to New Zealand. The Alliance advises TNZ of all planned sales so that it is easy for TNZ to leverage off the tactical fares the Alliance has on offer and promote New Zealand to the travelling public. As an Alliance Air New Zealand and Virgin Australia are able to provide TNZ with greater opportunity to promote New Zealand due to the strength and reach of the combined Alliance network;

- since the implementation of the Alliance, the Applicants have been able to utilise their marketing spend for the trans-Tasman more efficiently than was possible prior to the Alliance;

- through the Joint Sales Team, the Applicants have conducted regular coordinated marketing campaigns to stimulate travel on the trans-Tasman and educate the public about the Alliance;

- in addition to the joint awareness activity, the Alliance has been to market three times with specific Alliance retail campaigns. The "Bromance Sale" was in market in two bursts in 2011 to celebrate the launch of the Alliance and the "Friends with benefits" sale in 2012 to leverage the 1 year anniversary of the partnership. The campaigns included a tactical offer and key messaging reinforced the consumer benefits of better flight times and reciprocal loyalty rewards; and

- in relation to general retail marketing, since the 2010 authorisation the Applicants have conducted a minimum of one proactive retail marketing campaign per month. For the second half of the 2012 financial year there were up to two proactive retail campaigns per month. These campaigns have been promoted on television, press, online and electronic mail.

Conclusion on tourism benefits

338. Overall, the ACCC accepts that the Alliance has the potential to stimulate tourism spend in Australia (and New Zealand). The revenue sharing arrangement underpinning the Alliance provides a strong incentive for the Applicants to pursue joint marketing opportunities.

339. The ACCC considers that the extent of tourism benefits realised under the Alliance will be highly (positively) correlated with the additional trans-Tasman traffic that may be stimulated under the Alliance. The ACCC accepts that, on balance, the Alliance is likely to have an overall stimulatory effect on trans-Tasman traffic. On

this basis, the ACCC considers that the Alliance is likely to generate some small tourism-related public benefits.

ACCC conclusion on public benefits

340. The ACCC considers that in the two years the Alliance has been in operation it has resulted in material public benefits in the form of enhanced products and services (particularly through new frequencies) and the promotion of competition on trans-Tasman routes. In addition the ACCC considers that the Alliance has resulted in small public benefits in the form of cost savings and efficiencies and the stimulation of tourism.

341. The ACCC accepts that due to the limited period the Alliance has been in operation, there may be some public benefits that are yet to be fully realised.

342. In light of this, the ACCC considers that moving forward, the Alliance is likely to result in:

- material public benefits in the form of enhanced products and services. These products and services are comprised of loyalty program benefits, lounge access, and new frequencies (each of which the ACCC considers will be material benefits going forward) and increased online connections and better schedule spread (which the ACCC considers will result in small public benefits going forward). Increased access to existing frequencies may also form a public benefit, however based on the evidence available, the ACCC cannot conclude the magnitude of this benefit;

- material public benefit in the form of the promotion of competition on trans-Tasman routes, particularly in relation to the business traveller segment. The ACCC considers that this benefit is likely to manifest in a competitive response from the Qantas Group to the improvement in products and services of the Alliance on these routes. To a lesser extent the ACCC considers that the Alliance is likely to result in a similar public benefit in the domestic Australian market, however is unable to reach a conclusion as to the extent to which the Alliance contributes to the increased competitiveness of Virgin Australia;

- small public benefits in the form of cost savings and efficiencies. These small benefits are likely to be derived from joint procurement, co-location of certain functions, utilisation of common resources and the removal of double marginalisation. The ACCC also considers that operational optimisation and high load factors may deliver efficiencies for the Alliance. However, based on the evidence available, the ACCC cannot conclude that high load factors are a likely benefit of the Alliance; and is unable to reach a conclusion on the magnitude of the benefit resulting from operational optimisation; and

- small public benefits in the form of stimulating tourism spend in Australia.

343. Taken together, the ACCC is satisfied that the Alliance would, or would be likely to, result in material public benefits.

Public detriment

344. As discussed in the section **ACCC approach to evaluation**, the Act requires the ACCC to consider the detriment to the public, including detriment constituted by any lessening of competition that would result, or is likely to result from the proposed conduct.

345. Public detriment is also not defined in the Act but the Tribunal has given the concept a wide ambit, including:

> …any impairment to the community generally, any harm or damage to the aims pursued by the society including as one of its principal elements the achievement of the goal of economic efficiency.[62]

346. The Applicants submit that the Alliance results in no anti-competitive detriment. In this regard, the Applicants note that the Alliance has led to a decrease in the combined average fares of the Applicants and has not resulted in an anti-competitive withholding of capacity on the trans-Tasman generally or on any individual route.

347. The Applicants submit that the trans-Tasman is a highly competitive market characterised by substantial capacity and strong fare competition, and that the Alliance faces strong competition on the trans-Tasman in the form of new entry and expansion and the expansion of existing carriers, including on the individual routes subject to the capacity conditions (e.g. the entry of Jetstar on Queenstown-Sydney and the entry of China Airlines on Auckland-Brisbane).

348. The Applicants' specific submissions, the views of interested parties and the ACCC's assessment of the likely public detriments are set out below.

Public detriment likely to arise from a lessening of competition

Trans-Tasman air passenger transport services

349. New Zealand is Australia's largest international origin/destination market, with a total of 4.6 million passenger movements in the year ended February 2013.

350. Virgin Australia and Air New Zealand overlap with respect to international air passenger transport services on nine routes between Australia and New Zealand. Virgin Australia and Air New Zealand both currently operate on the following routes:

i. Auckland-Sydney

ii. Auckland-Melbourne

iii. Auckland-Brisbane

iv. Christchurch-Sydney

[62] *Re 7-Eleven Stores* [1994] ATPR 41-357 at 42,683.

v. Christchurch-Melbourne

vi. Christchurch-Brisbane

vii. Auckland-Gold Coast

viii. Queenstown-Sydney

ix. Brisbane-Queenstown.

351. However, this is in the context of the Alliance having been in operation for over two years. What is relevant for assessing competitive detriment going forward is the extent to which the two airlines would be actual or potential competitors absent the Alliance.

352. Virgin Australia and Air New Zealand have also each flown a number of additional routes in the period before the Alliance was first authorised in 2010 and since. The routes that were overlap routes between 2010 and 2013 that only one of the Applicants now operates services on are Wellington-Sydney, Wellington-Brisbane, Dunedin-Sydney, Dunedin-Melbourne, Dunedin-Brisbane and Auckland-Cairns.

353. The ACCC has examined whether the Alliance is likely to result in public detriments on the trans-Tasman by:

(a) giving Virgin Australia and Air New Zealand an increased ability and incentive to unilaterally raise airfares or reduce or limit growth in capacity; and/or

(b) increasing the risk of coordinated conduct among competing airlines on the trans-Tasman and specifically the Alliance and the Qantas Group-Emirates alliance.

354. The ACCC has assessed the unilateral and coordinated effects of the Alliance having regard to the likely future with the Alliance as compared to the likely future without the Alliance.

Unilateral effects

355. The Alliance gives Virgin Australia and Air New Zealand the ability to coordinate their price and service decisions on the trans-Tasman. Therefore, absent effective competition from other airlines, the Applicants may have an increased incentive to unilaterally raise prices on overlap routes as a result of internalising customer switching between them. These price rises could occur through the Alliance unilaterally raising fares without removing Alliance capacity on trans-Tasman routes by offering:

- higher priced fare schedules:[63] with the Alliance, fare schedules are set with regard to the Qantas-Group/Emirates alliance and FFCs (where applicable). Without the Alliance, fare schedules would be set with regard to the Qantas-Group/Emirates alliance, FFCs (where applicable) and Virgin Australia or Air New Zealand (as applicable);

[63] A fare schedule refers to a table of prices offered for a particular route based on fare class (i.e. Y, B, M, etc) and fare type (i.e. Seat, Seat plus bag, etc.).

- lower frequency or lower discount tactical fares:[64] with the Alliance, the frequency and depth of any discount provided by tactical fares offered is decided with regard to tactical fare offerings from the Qantas-Group/Emirates alliance and FFCs (where applicable). Without the Alliance, the frequency and depth of any discount provided by tactical fares would be decided with regard to the offerings of the Qantas-Group/Emirates alliance, FFCs (where applicable) and Virgin Australia (or Air New Zealand); and/or
- less availability of lower priced fares within a fare schedule: for example, while reductions in wing-tip flying may confer a benefit in terms of greater schedule availability, they may also result in high capacity utilisation of flights during peak times. This may manifest itself as a reduced availability of lower priced fares through the operation of the Applicants' revenue management system.

356. Absent effective constraint by other airlines, competitive detriment could also occur as a result of the Applicants unilaterally reducing, or slowing the rate of, their capacity growth on trans-Tasman routes:

- Without the Alliance, Virgin Australia (or Air New Zealand) would compete through the expansion of capacity with the Qantas Group/Emirates alliance, Air New Zealand (or Virgin Australia) and FFCs (where applicable). With the Alliance, the Applicants compete through the expansion of capacity with regard to only the Qantas Group/Emirates alliance and FFCs (where applicable); and
- The effect of slower capacity growth will be to make seats scarcer, which is likely to result in higher fares over the longer term.

357. The ACCC considers the spare capacity available to airlines that compete with the Applicants is important when considering the extent to which unilateral effects are likely to arise as a result of the Alliance. The ACCC considers that over the longer term excess capacity available to rival airlines operating on overlap routes makes it less likely that the Applicants could profitably raise fares unilaterally unless they were to reduce or limit future growth in their capacity for the purpose of achieving higher average airfares. If airlines have excess capacity available to them and one airline or an alliance raises its prices it is possible that it would lose sales to the other airline or alliance such that any attempt to unilaterally raise prices may be unprofitable. The extent to which this may occur in the future with the Alliance will depend on, amongst other things, the closeness of competition between airlines and the value of an airline's or alliance's lost sales. Therefore, the ACCC has used airline load factors as a guide to available capacity on various routes. This has informed the assessment below in the context of each particular group of trans-Tasman routes.

358. In assessing the likelihood that the Alliance will find it profitable to unilaterally reduce or limit growth in capacity, the ACCC has considered:

(a) whether the services of Virgin Australia and Air New Zealand are close substitutes;

[64] Tactical fares are provided as a short term response to competitors' offerings and/or lower than expected demand.

(b) the competitive constraint imposed by other airlines or alliances in the market (or on the route); and

(c) the likelihood of timely entry or expansion in the market (or onto the route) if the Alliance attempted to reduce or limit growth in capacity (in order to raise airfares).

Whether the services of Virgin Australia and Air New Zealand are close substitutes

359. The ACCC considers Virgin Australia and Air New Zealand to be relatively close substitutes. This is based on the following considerations:

(a) both airlines offering similar levels of service (with Virgin Australia increasingly offering higher levels of service, and Air New Zealand introducing basic fare class products which compete with LCCs);

(b) both airlines sell flights to overlapping trans-Tasman destinations, where flights may leave at similar times;

(c) both airlines now have a focus on targeting business customers; and

(d) both airlines have an ability to price discriminate to cater to both leisure and business customers.

Competitive constraint imposed by other airlines

360. The ACCC has had regard to the ability and incentive of rival airlines to competitively constrain Virgin Australia and Air New Zealand. This is discussed in more detail below in the context of each particular group of trans-Tasman routes.

Likelihood of timely entry or expansion

Expansion plans of key competitors

361. The ACCC considers that new entry by existing Australian or New Zealand airlines not already operating on the trans-Tasman is unlikely to occur in the foreseeable future on a scale necessary to provide a competitive constraint.

362. In relation to recent new entry, the ACCC notes China Airlines entry on two trans-Tasman routes: Auckland-Brisbane in 2011 and Auckland-Sydney in 2012. This airline has experienced a relatively rapid capacity increase for the year ending February 2013 (up to 2.1% on Auckland-Sydney and 8.2% on Auckland-Brisbane).

363. The decision to enter by a FFC is unlikely to be determined solely by the existence of economic profits on the trans-Tasman routes. A FFC would first need to examine the viability of the long haul component of its service (into Australia) before deciding whether to extend that service into New Zealand.

364. The ACCC notes Qantas and Emirates submissions to the ACCC concerning their alliance and the likelihood of the Qantas Group/Emirates alliance adding capacity in the short term. In summary, Qantas and Emirates consider that there is excess capacity in the trans-Tasman market. Qantas's submissions to the ACCC suggest that it does not plan to increase its capacity on trans-Tasman routes in the short-medium term.

Barriers to entry and expansion

365. The potential barriers to new entry and expansion on the trans-Tasman routes considered include:[65]

- regulatory restrictions on route capacity;
- access to airport landing slots and airside services; and
- airport limitations in accommodating long haul aircraft.

366. The trans-Tasman operates as a Single Aviation Market, with Australian and New Zealand designated airlines able to set their own capacities and frequencies. FFCs are able to enter where there are unutilised fifth freedom rights although some air services agreements regulate capacity and routes. Overall, the ACCC considers that the regulatory regime is a low barrier to entry.

367. Other practical barriers may prevent an airline from expanding on the relevant routes in the short term. For example, if an airline is unable to negotiate landing slots at relevant airports. The ACCC understands that generally airports relevant to the trans-Tasman are not currently slot constrained so this is unlikely to be a longer term barrier to entry.[66]

368. FFCs are unlikely to be able to commence services on the majority of trans-Tasman city pair routes due to limitations at the New Zealand airports in accommodating the wide body aircraft which FFCs generally operate on long haul routes. This will not affect routes between Australia-Auckland and Australia-Christchurch. Entry by FFCs is discussed further below in relation the competition assessment of the major Auckland and Christchurch routes.

Coordinated effects

369. Another potential source of competitive harm from the Alliance is that it may increase the risk of coordinated conduct among multiple airlines on the trans-Tasman routes or on a specific route. Coordinated conduct is essentially about airlines recognising and accommodating their mutual interdependence (explicitly or tacitly) by not competing as aggressively as they otherwise would.

370. By reducing the main players on the trans-Tasman to two players of similar scale, the Alliance may have a better ability to:

- engage in price coordination: with the Alliance, the Applicants only need to have regard to the Qantas-Group/Emirates alliance and FFCs (where applicable) when setting fare schedules. This may facilitate the Applicants (or the Qantas-Group/Emirates alliance) leading prices upwards, with the expectation that the Qantas-Group/Emirates alliance (or the Alliance as applicable) will follow. Without the Alliance, price leadership is less likely to be successful given the existence of three

[65] Other barriers to new entry relate to sunk costs, route size and network economies.

[66] The ACCC acknowledges that Sydney international airport faces slot constraints that may result in increased barriers to entry for an airline seeking to fly between Sydney and ports in New Zealand – see The Australian Government and Government of NSW, *Joint Study on aviation capacity for the Sydney region,* 2 March 2012.

independent competitors on the trans-Tasman routes with divergent scale, scope of operations and likely facing divergent incentives.

- slow capacity growth: with the Alliance, the Alliance only needs to have regard to the Qantas-Group/Emirates alliance and FFCs (where applicable) when making capacity decisions. These capacity decisions may relate to the number of schedules on a particular route, or the purchase of planes over the longer term. Given the level of market concentration with the Alliance, the Applicants and Qantas-Group/Emirates may be able to signal to each other to limit capacity growth, given their mutual interests in doing so. Without the Alliance, any tacit agreement to limit capacity growth is less likely to be successful given the existence three independent, competitors with divergent scale, scope of operations and likely facing divergent incentives.

371. In assessing whether the Alliance increases the risk of coordinated conduct, the ACCC has considered:

(a) the extent to which the markets under consideration have characteristics that are likely to make them conducive to coordinated conduct;

(b) the extent to which the markets under consideration have characteristics that are likely to undermine coordinated conduct; and

(c) what the Alliance changes, given the above, in regard to the likelihood of successful coordination of pricing and/or capacity decisions amongst competitors in the relevant markets.

372. The ACCC considers that the markets under consideration have the following characteristics that are likely to make them conducive to coordinated conduct:

- a small number of airlines operating on in the relevant markets;
- frequent interaction between the Applicants and Qantas-Group/Emirates, across a number of trans-Tasman routes (which may facilitate the learning of behaviours and provides the scope for retaliation);
- a symmetry of product offerings and market share for both the Alliance and the Qantas Group/Emirates alliance;
- the small size and high frequency of transactions;
- transparency of each airlines' price and short term capacity decisions, which allows airlines to more easily signal increased prices and detect deviations from the coordinated level; and
- low likelihood of new entry on the trans-Tasman in response to increases in price;
- where applicable, a limited likelihood of FFCs increasing capacity on the routes in a timely manner in response to a reduction in capacity.

373. The ACCC considers that the markets under consideration also have the following characteristics that are likely to undermine coordinated conduct:

- in regard to the purchase of aircraft, the lumpiness, costs, and long lead time of these purchases, and the difficulty of knowing where a competitor is likely to deploy any new aircraft in its network;

- in regard to flight schedules, airlines tend to make decisions about scheduling with regard to their impact on its broader network. A decision to coordinate on one route may cause disruptions elsewhere on the network, which may make such decisions difficult or costly to execute in practice;

- FFCs are less likely to participate in any coordinated conduct in regard to capacity, given that their decisions are driven by their wider network considerations;

- Air New Zealand, Qantas Group/Emirates and Virgin Australia have different incentives in other markets (for example, Virgin Australia and Qantas compete in the domestic Australian market, whereas Air New Zealand does not); and

- the operation of any ACCC capacity condition which will act to limit the extent to which airlines can limit capacity growth through tacit coordination.

374. Given the various characteristics that make coordination more or less likely on the trans-Tasman, the ACCC has considered what the Alliance changes, and how this may impact on the likelihood of various forms of coordinated conduct occurring.

375. The ACCC notes that with the Alliance there are two independent groups operating on the trans-Tasman, the Applicants and Qantas-Group/Emirates (as well as FFCs on some routes). Without the Alliance there would be three independent competitors operating on the trans-Tasman - two large, full service operators in the Qantas Group/Emirates alliance and Air New Zealand - and a smaller operator, Virgin Australia.

376. The ACCC has therefore considered whether, as a smaller independent operator on the trans-Tasman, Virgin Australia may be more likely to disrupt coordination without the Alliance, decreasing the risk of coordination relative to the market structure with the Alliance.

377. Given its asymmetric market share on the trans-Tasman in the world without the Alliance, Virgin Australia may have less incentive to participate in any coordinated conduct on price or capacity. Rather, in the face of some form of coordination, it may consider it a more profitable strategy to engage in competitive behaviour to increase its market share.

378. In contrast, with the Alliance, there will be greater symmetry between the market presence, operations and cost structures of the Applicants and the Qantas Group-Emirates alliance. This increased symmetry makes it more likely that these airline groups would have similar incentives to coordinate on prices and/or capacity.

379. The ACCC considered the issue of Virgin Australia acting as a maverick[67] in its 2010 authorisation. In that assessment, it had regard to fare data analysis that suggested Virgin Australia had historically wielded price influence disproportionate to its market share on the trans-Tasman.[68] However, the ACCC considered that Virgin Australia was unlikely to be as effective as a maverick in the future. This view was reached based on Virgin Australia's changed business model (the Game Change strategy) and its historically poor financial performance on the trans-Tasman.

380. In this assessment, as in 2010, there is conflicting information about the likely behaviour of Virgin Australia absent the Alliance, and whether it would be reasonable to expect it to behave as it did prior to the 2010 alliance on the trans-Tasman.

381. The ACCC notes Virgin Australia's submission that absent the Alliance it would reduce capacity and frequencies. If Virgin Australia were a significantly smaller operator without the Alliance, this would undermine its ability to act as an effective maverick.

382. In response to the draft determination, the Applicants submit[69] that there is no evidence of any adverse co-ordinated effects. They submit that the market experience is not consistent with the existence of coordinated effects on the trans-Tasman for the following reasons:

- such behaviour is not reflected in the fare or capacity outcomes of the Alliance
- the trans-Tasman is a highly competitive, dynamic market with low barriers to entry and expansion. It has a history of frequent innovation by all carriers and is subject to instability in demand levels as a result in external shocks (eg, earthquakes) and dramatic fluctuations in costs (eg, fuel)
- different carriers have different cost bases and differentiated products
- Air New Zealand, Qantas Group/Emirates and Virgin Australia have different incentives in other markets and any ability to coordinate on scheduling decisions would involve consideration of the different impacts on each airline's broader network offering which would increase the cost/difficulty of coordination and
- unsold seats on a departing plane are worthless. Once capacity is in the market (and there is substantial capacity in the trans-Tasman market), the commercial pressure to sell seats would likely swamp any theoretical gains from setting fares high. The trans-Tasman has a history of demand for trans-Tasman air passenger services being consistently supported by

[67] A maverick is a firm with a relatively small market share in a particular industry that is considered a vigorous and effective competitor and which generally drives significant aspects of competition, such as pricing, innovation and/or product development.
[68] ACCC, Determination in relation to applications A91227 & A91228 lodged by Virgin Blue Airlines Pty Ltd and Ors, 16 December 2010, p. 91 at [5.442].
[69] Virgin Australia & Air New Zealand, Submission in response to the draft determination, 24 July 2013

substantial capacity growth and there is currently excess capacity across the trans-Tasman overall as well as on particular routes.

383. The ACCC's views on the likelihood of coordinated conduct are discussed further in the context of each group of routes below, with regard to the factors discussed in this section.

Carriers operating on the trans-Tasman

384. A profile of the carriers operating on the trans-Tasman is detailed in the **Background** section above.

385. In addition to the material outlined above, the ACCC notes that the airlines operating on the trans-Tasman have particular characteristics that impact upon the type of competitive constraint they are likely to have on the Alliance.

386. In relation to the Qantas Group, the ACCC considers that there are differences between the operations of Qantas and Jetstar. In the ACCC's view Qantas is likely to provide the strongest competitive constraint on time-sensitive business/corporate customers. The ACCC considers that Qantas operates as a premium carrier on the trans-Tasman and accordingly is unlikely to lead discounting on fares.

387. Jetstar on the other hand is likely to provide the strongest competitive constraint on non-time sensitive leisure customers. Jetstar appears more likely to engage in tactical pricing. Accordingly, the ACCC considers that Jetstar is more likely to operate as a constraint on the Alliance's leisure fares and tactical pricing decisions while Qantas is likely to provide a closer constraint on the Alliance's premium fare segment offering.

388. At present Emirates operates flights at peak times on some major routes (for example, Auckland-Sydney) on the trans-Tasman. While Emirates is unlikely to expand capacity in response to price signals on the trans-Tasman, as deployment considerations are driven by considerations at Emirates' Dubai hub and the broader Qantas-Emirates network, the ACCC notes that when it deploys capacity on a route it adds a considerable number of available seats to the route because of the size of the aircraft it flies.

389. The newly formed Qantas Group-Emirates alliance makes the extent of capacity likely to be deployed on the trans-Tasman uncertain as the ACCC considers that Emirates, as part of the alliance with Qantas, will act in a way to maximise profit across the trans-Tasman for that alliance. Further, Emirates planes may face less 'down time' in Australia if the Qantas Group-Emirates alliance is able to further optimise its network as a result of that alliance.

390. In relation to the likely competitive constraint posed by FFCs on the trans-Tasman, the ACCC notes that the decision for a FFC to operate services on the trans-Tasman as an extension of its international services to Australia is typically opportunistic and linked to the carrier's broader network considerations. One consequence of this is that, just as it may be opportunistic for a FFC to enter a trans-Tasman route, it equally may be opportunistic for a FFC to exit the route in response to a change in demand or supply conditions elsewhere in a FFC's network. This explains the pattern of entry and exit by FFC on the trans-Tasman over the last decade.

Submissions in relation to services on the trans-Tasman

391. The Applicants submit that the Alliance will allow them to be a more vigorous and effective competitor than the two airlines would be acting independently.[70] They submit that the Alliance has provided an improved service offering. In a future with the Alliance, they submit that it will continue to provide customers with an improved service offering, including a greater depth of network schedules than would be available absent the Alliance.[71]

392. The Applicants also submit that average Alliance fares have decreased as a result of the Alliance. They note that where there have been increases in Virgin Australia fares, these have been a result of schedule optimisation and rebalancing of Virgin capacity on certain routes.[72] The Applicants submit that any increase in Virgin fares is also a result in part of the increased offering by Virgin of the full range of fare classes that it was unable to offer prior to the Alliance.[73]

393. In relation to capacity on the trans-Tasman, the Applicants submit that Alliance capacity has grown by 5% from the year ending 31 October 2010 to the year ending 31 October 2012 on non-Christchurch routes and by 10.1% over the same period.[74]

394. The Applicants strongly contend that rather than removing a competitor on the trans-Tasman, the Alliance has and will continue to result in a stronger competitor to the Qantas Group than would be the case without the Alliance.[75]

395. NZ Airports submit that authorising the Alliance without capacity conditions will inhibit the natural competitive dynamics of the trans-Tasman. It submits that in the absence of a capacity condition that has a growth factor in line with market growth, there are clear and easily recognised economic incentives driving the carriers to restrict capacity on routes with limited competitive constraint.[76] NZ Airports is concerned with the Applicants ability to exercise market power on particular routes. On a trans-Tasman level NZ Airports notes that the Applicants delivered a significantly higher rate of growth when acting independently than they have under the Alliance.[77]

396. CIAL initially submitted that it supported reauthorisation of the Alliance for a further period of three years, subject to the conditions requiring the Applicants to maintain a base level of capacity with a growth factor on the trans-Tasman as a whole, and maintain and grow capacity on individual routes, including the Christchurch-Brisbane/Melbourne/Gold Coast/Sydney routes. CIAL also submitted that capacity conditions are required as, since the Alliance commenced operating, average fares have increased, consumer demand on the above routes have not been met and material competition concerns have been raised.

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70 Virgin Australia & Air New Zealand, Submission in Support, 8 March 2013, p.32.
71 Virgin Australia & Air New Zealand, Submission in Support, 8 March 2013, p.33.
72 Virgin Australia & Air New Zealand, Submission in Support, 8 March 2013, p.34.
73 Virgin Australia & Air New Zealand, Submission in Support, 8 March 2013, p.34.
74 Virgin Australia & Air New Zealand, Submission in Support, 8 March 2013, p.33.
75 To the extent that the Alliance has pro-competitive aspects, the ACCC's view on the magnitude of these has been addressed in the Public Benefits section of this Determination.
76 NZ Airports, Submission to the New Zealand Ministry of Transport, 3 May 2013, p.2.
77 NZ Airports, Submission to the New Zealand Ministry of Transport, 3 May 2013, p.5.

397. CIAL subsequently made a supplementary submission indicating that the concerns raised in its earlier submission had primarily been dealt with by further confidential information provided by Air New Zealand.[78]

398. DIAL also made submissions regarding reauthorisation of the Alliance only with capacity conditions and noted that absent a requirement to increase capacity on the trans-Tasman the Applicants would have the incentive to reduce capacity. DIAL indicates that the rate of capacity growth on the trans-Tasman for Virgin Australia and Air New Zealand prior to the Alliance was on average 6.3% and since the 2010 Alliance has slowed to 2.5%.[79] DIAL's submission after the draft determination supported the ACCC's inclusion of the Dunedin-Sydney and Dunedin-Melbourne routes as part of the proposed condition. It strongly contested the Applicants' proposed changes to the structure of the condition in the draft determination.

399. KWSG submits that other than the Qantas Group-Emirates alliance and the fact that the Alliance is in operation, nothing in the market is relevantly different today on the Wellington routes from how it was when the ACCC issued its final decision in 2010. It submits that the level of concentration on the trans-Tasman has the potential to deliver detrimental competitive outcomes. In its submission it notes the duopoly and monopoly nature of the various Wellington routes and the fact that Emirates and other FFCs are not a competitive constraint on the airlines flying in and out of Wellington.[80] In light of these potential anticompetitive harms, the KWSG supports conditional reauthorisation. KWSG's submission after the draft determination supported this view and provided further reasons as to why it considers that in the future without the Alliance the Applicants would compete on the three Wellington routes.

400. Emirates submits that the Alliance has the overall highest share of passengers on the trans-Tasman. It notes the ACCC's assessment of the ability of the Alliance and other airlines to constrain the Qantas Group-Emirates alliance, and submits that absent capacity conditions, it is not clear that Qantas Group or Emirates would constrain the Alliance.[81] Further, Emirates submits that the trans-Tasman is a highly competitive market and attributes Alliance fare reductions to that competition rather than the public benefits that the Applicants have claimed.[82]

401. Qantas submits that the trans-Tasman is characterised by excess capacity and competitive market behaviours. It notes however that the Alliance will result in a high degree of overlap and monopoly operations on several route including Brisbane-Dunedin, Brisbane-Wellington, Auckland-Cairns, Adelaide-Auckland and Perth-Auckland. Qantas also queries the extent to which pro-competitive outcomes have arisen as a result of the Alliance or as a result of market conditions and demand. [83]

402. Following the draft determination, the Applicants reiterated that the Alliance will continue to face a strong competitive constraint from Qantas, Jetstar and Emirates.

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78 Christchurch International Airport Limited, Further submission to the ACCC, 13 June 2013.

79 Dunedin International Airport Limited, Submission to the New Zealand Ministry of Transport, 3 May 2013, p.4.

80 Key Wellington Stakeholders, Submission, 26 April 2013, pp.4-5

81 Emirates, Submission in relation to Virgin Australia and Air New Zealand Applications for authorisation A91362 & A913636, 12 April 2013, p.3

82 Emirates, Submission, p. 4

83 Qantas Airways Ltd, Submission in relation to Virgin Australia and Air New Zealand applications for authorisations A9162and A91363. p.1

The Applicants submit that Jetstar poses a significant constraint on the Alliance, irrespective of its inclusion in the Qantas Group/Emirates Alliance. Further, the Applicants submit that Jetstar has a strong Australian and New Zealand domestic network, great brand presence, and has shown its ability to rapidly deploy and expand in response to market opportunities.[84]

Passenger and capacity shares

403. According to data provided by BITRE, in the year ended February 2013, seven airlines operated services across the trans-Tasman on over twenty routes. A total of 4,633,076 passengers flew between destinations in Australian and New Zealand with total capacity on all routes of 8,114,956 seats. In this period, 72% of passengers travelled for leisure and 16% travelled for business.[85]

Table D.1: Airline share (%) of total capacity, seats flown Australia-New Zealand, year ended February[86]

Airline	2011	2012	2013
Air New Zealand	35.0	35.4	35.4
Virgin Australia	17.1	15.0	15.4
Air New Zealand-Virgin Australia	52.1	50.4	50.8
Qantas	21.6	21.4	21.5
Emirates	13.3	14.0	14.4
Jetstar Airways	9.6	10.4	9.4
Qantas Group-Emirates	44.5	45.8	45.3
LAN Airlines	2.0	2.0	1.8
China Airlines	0.2	1.1	1.7
Aerolineas Argentinas	1.3	0.9	0.3
Royal Brunei Airlines	0.1	0.0	0.0
Total (%)	100.0	100.0	100.0
Seats ('000)	7,747.8	8,076.0	8,114.9

Note: This data includes all seats flown between Sydney Melbourne, and Brisbane to Auckland and Sydney to Christchurch. It therefore includes seats occupied by origin/destination passengers, seats occupied by transit passengers and unoccupied seats.

404. This data shows a number of changes to the aggregate capacity for the airlines operating on the trans-Tasman. Significantly, the shares for the Alliance and Qantas Group-Emirates have remained largely stable for the three years, although there have been changes to capacity shares overall, with the Alliance losing 1.3% over the period and the Qantas Group-Emirates increasing its share by 1.8%.

405. There have been noticeable changes to the FFCs operators on the trans-Tasman, with the exit of Royal Brunei Airlines in 2010, Aerolineas Argentinas' exit in 2012 and the entry of China Airlines in 2011.

[84] Virgin Australia & Air New Zealand, Submission in response to the draft determination, 24 July 2013.

[85] For the purposes of this determination the ACCC has considered leisure passengers to incorporate those passengers with a purpose of travel of either 'holiday' or 'visit friend or relative'. Business passengers incorporate those passengers with a purpose of travel of either 'business' or 'convention'. The remaining passengers had a purpose of travel of 'employment', 'education', 'exhibition', 'not stated' or 'other'.

[86] Information provided by the Bureau of Infrastructure, Transport and Regional Economics (BITRE) based on airline supplied data.

Table D.2: Airline number of total seats ('000') flown Australia-New Zealand, year ended February[87]

Airline	2011	2012	2013
Air New Zealand	2,718,482	2,852,070	2,873,078
Virgin Australia	1,312,560	1,221,052	1,260,264
Air New Zealand-Virgin Australia	4,031,042	4,073,122	4,133,342
Qantas	1,671,575	1,721,848	1,742,019
Emirates	1,034,514	1,129,774	1,167,345
Jetstar Airways	741,000	833,799	758,802
Qantas Group-Emirates	3,447,089	3,685,421	3,668,166
LAN Airlines	152,852	159,762	149,024
China Airlines	13,868	89,030	138,736
Aerolineas Argentinas	97,318	68,666	25,688
Royal Brunei Airlines	5,667	0	0
Seats ('000)	7,747.8	8,076.0	8,114.9

Note: This data includes all seats flown between Sydney, Melbourne and Brisbane to Auckland and Christchurch. It therefore includes seats occupied by origin/destination passengers, seats occupied by transit passengers and unoccupied seats.

406. At the trans-Tasman level, for the year ending February 2013, the Alliance provided Virgin Australia and Air New Zealand with 4,133,342 seats flown. The Qantas Group had 2,500,821 of the total seats flown on the trans-Tasman for the same period. Adding Emirates to this total, the Qantas Group-Emirates alliance flew 3,668,166 for the period.

407. The data shows that in terms of actual seats flown, the Alliance has increased the overall number of available seats flown by 102,300 from its February 2011 total. Qantas' seats flown for the three year period ending February 2013 increased in terms of total seats by 70,444 and Jetstar's fluctuated with an increase in the year ending February 2012 but returning to similar levels for the year ending February 2013 as it flew in the year ending February 2011. Emirates' seats flown for the period, on the other hand, have steadily increased, as has China Airlines' seats flown.

408. The following table sets out passenger shares by percentage based on passenger card data from the Department of Immigration and Citizenship over the last five years ending February.

Table D.3: Airline share (%) of total origin/destination passengers, Australia-New Zealand, year to February[88]

Airline	2009	2010	2011	2012	2013
Air New Zealand	41.1	37.8	39.9	41.3	41.0
Virgin Australia	13.4	17.1	16.5	15.0	16.9
Air New Zealand-Virgin Australia	**54.5**	**54.9**	**56.4**	**56.4**	**57.9**
Qantas	22.9	20.6	20.6	20.1	19.6

87 Information provided by the Bureau of Infrastructure, Transport and Regional Economics (BITRE) based on airline supplied data.

88 Information provided by the Bureau of Infrastructure, Transport and Regional Economics (BITRE) based on passenger card data collected and compiled by the Department of Immigration and Citizenship (DIAC).

Jetstar Airways	7.1	11.1	10.4	11.0	10.3
Emirates	11.4	9.9	9.7	9.3	8.9
Qantas Group-Emirates	**41.4**	**41.7**	**40.8**	**40.4**	**38.8**
LAN-Chile	0.8	0.9	0.6	0.7	0.7
China Airlines	0.0	0.0	0.2	0.8	0.9
Aerolineas Argentinas	0.5	0.5	0.6	0.4	0.2
Royal Brunei Airlines	0.7	0.7	0.1	0.0	0.0
Other	2.0	1.3	1.5	1.3	1.4
Total (%)	100.0	100.0	100.0	100.0	100.0
Passengers ('000)	*4,100.6*	*4,338.4*	*4,497.6*	*4,582.0*	*4,633.1*

409. At the trans-Tasman aggregate level, the Applicants have a joint market share of around 58% of passengers flown compared to 39% for Qantas/ /Emirates, and 3% for the remaining FFCs.[89]

410. The data demonstrates that there has been movement in the Alliance share over the last four years, with an overall increase of 3.4 percentage points.

411. The Qantas-Group/Emirates alliance has lost market share over the last four years. Qantas has seen a 3.3 percentage point share decrease in the four year period. Jetstar has increased from a percentage share of 7.1% in the year ending February 2009 to 10.3% in the year ending February 2013. Emirates' market share has decreased by 2.5 percentage points between the year ending February 2009 to February 2013.

412. China Airlines entry has not resulted in a market share that corresponds to its capacity share in aggregate on the trans-Tasman routes. As a FFC, China Airlines can only deploy aircraft suitable for its long haul services into Australia and beyond. It is therefore limited as to the minimum amount of capacity that it can add when it enters a route. This likely explains the discrepancy between China Airlines passenger market share (which is relatively low) as opposed to the capacity that it has added to trans-Tasman services. The ACCC also notes that the passenger figures for this period do not account for transit passengers.

[89] By share of passengers carried, February 2013.

Airfares on the trans-Tasman routes

413. The ACCC has had regard to fare data provided by the Applicants, and has considered changes in fares since the implementation of the Alliance. The ACCC notes that average airfares across the trans-Tasman change from year to year as a result of a number of factors that are unrelated to the Alliance, such as changes in input costs (e.g. jet fuel) and extraordinary demand events.

414. The ACCC notes the Applicants' submission that average Alliance fares across the trans-Tasman have decreased since the Alliance was implemented. Having regard to confidential information provided by the Applicants, the ACCC considers that there has been little if any material change to the Alliance's average airfares across the Tasman since the implementation of the Alliance.

415. While airfare data can be instructive in terms of assessing anticompetitive effects, in this instance, the ACCC considers that it is difficult to reach a definitive view of the likely impact of the Alliance on airfares.

416. For example, there have been a number of extraordinary demand events since the 2010 authorisation, such as the Christchurch earthquakes and the Chilean ash cloud and, holding other factors constant, these events would tend to put downward pressure on airfares. Conversely, the Applicants have provided the ACCC with evidence of increases in their jet fuel costs since the implementation of the Alliance, which, holding other factors constant, would tend to put upward pressure on airfares.

417. The difficulties in reaching a view on the available fare data is exacerbated by the fact that fares have only been jointly set by the Applicants since October 2011. Given all the issues referred to above, the ACCC has not been able to place any significant weight on the airfare data provided. Notwithstanding, the ACCC notes that there does not appear to be a discernible anticompetitive increase in the average Alliance fares on the trans-Tasman.

Effect on competition on trans-Tasman routes

2010 authorisation

418. In 2010, the ACCC considered both unilateral effects and coordinated effects on competition on trans-Tasman routes.

419. In terms of unilateral effects, the ACCC concluded in 2010 that the Alliance was likely to result in material detriments on the following trans-Tasman routes (which together accounted for around 12% of trans-Tasman passenger traffic in April 2010):

- Wellington – Sydney (Virgin Australia, Air New Zealand, Qantas operating)
- Wellington – Melbourne (Air New Zealand, Qantas operating)
- Wellington – Brisbane (Virgin Australia, Air New Zealand operating)
- Dunedin – Brisbane (Virgin Australia, Air New Zealand operating)

420. The ACCC also considered that, based on the information available at the time, the effect of the Alliance on competition on the Auckland-Brisbane (13% of the trans-

Tasman) and Queenstown-Sydney (1% of the trans-Tasman) routes was uncertain.

421. In terms of coordinated effects, in 2010 the ACCC focused on two important sources of constraint on coordination that may be affected by the Alliance:

- the effect of the Alliance on market concentration on the trans-Tasman – concluding that increased market concentration by itself was unlikely to significantly enhance the likelihood of coordinated effects under the Alliance and that it would need to have regard to other factors that were present and likely to impact any increased ability and incentive to coordinate with the Alliance; and

- the effect of the Alliance on maverick conduct on the trans-Tasman – concluding that the change in the business model Pacific Blue planned to employ on the trans-Tasman combined with its recent poor financial performance suggested that Pacific Blue's influence as a maverick on trans-Tasman routes would weaken with or without the Alliance.

422. In light of this, the ACCC took the view that it was unlikely that the Alliance would substantially increase the likelihood of coordinated conduct on trans-Tasman routes.

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423. The ACCC has examined the potential impact of the Alliance on competition on the various routes constituting the trans-Tasman.

424. The tables below set out which airlines currently operate on each trans-Tasman route. The routes are divided into 'major routes' and 'minor and seasonal' routes.

Table D.4: Trans-Tasman routes (blue indicates Virgin/Air New Zealand Alliance, red indicates Qantas Group/Emirates alliance, and grey represents third party airlines)[90]

Route	Air New Zealand	Virgin Australia	Qantas	Jetstar	Emirates	LAN	China Airlines
Main routes							
Auckland-Sydney	X	X	X	X	X	X	X
Auckland-Melbourne	X	X	X	X	X		
Auckland-Brisbane	X	X	X		X		X
Christchurch-Sydney	X	X	X	X	X		
Christchurch-Melbourne	X	X		X			
Christchurch-Brisbane	X	X					
Wellington-Sydney	X		X				
Wellington-Melbourne	X		X				
Wellington-		X					

90 Data sourced from BITRE international scheduled passenger flights and seats by airline, for year ending February 2013.

Brisbane		X					

Route	Air New Zealand	Virgin Australia	Qantas	Jetstar
Minor and Seasonal Routes				
Auckland-Adelaide	X			
Auckland-Cairns	X			X
Auckland-Gold Coast	X	X	X	X
Auckland-Perth	X			
Christchurch-Gold Coast		X		X
Dunedin-Brisbane	X			
Hamilton-Brisbane				
Queenstown-Melbourne	X		X	X
Queenstown-Sydney	X	X	X	X
Queenstown-Brisbane	X	X	X	
Rotorua-Sydney	X			
Auckland – Sunshine Coast	X			
Dunedin - Melbourne		X		
Dunedin - Sydney		X		
Sydney – Hamilton[91]				

425. However, it is important to note that this table reflects current operations under the Alliance. What matters for the assessment of competitive effects is where the two airlines would be likely to compete in the future absent the Alliance.

Major routes

426. The ACCC has assessed the ability and incentive of Virgin Australia and Air New Zealand under the Alliance to unilaterally increase fares, decrease capacity and/or engage in coordinated conduct on the major routes. These are the routes between Auckland-Sydney/Melbourne/Brisbane, Christchurch-Sydney/Melbourne/Brisbane and Wellington-Sydney/Melbourne/Brisbane. Together these routes account for 84.7% of capacity on the trans-Tasman for the year ending February 2013.

427. The ACCC has assessed the likely competitive harm on these groupings of routes. It has undertaken this assessment against a likely future without the Alliance in which Virgin Australia reviews its service offering on a number of routes and withdraws capacity from those routes that are less profitable for it. Absent the

91 The ACCC notes that no airline is currently operating services on this route.

Alliance, the ACCC considers that Virgin Australia is unlikely to be as significant a competitor as Air New Zealand and the Qantas-Group/Emirates alliance. The ACCC also considers that, absent the Alliance, Virgin Australia is unlikely to re-enter the routes that it has exited as part of the Applicants' schedule optimisation. The ACCC has also had regard to the likely impact of the capacity condition imposed on the Qantas-Group/Emirates alliance in relation to the Sydney-Auckland, Melbourne-Auckland, Brisbane-Auckland and Sydney-Christchurch routes.

<u>Minor routes</u>

428. The remaining trans-Tasman routes can be grouped as minor and the ACCC has undertaken its assessment of the Applicants' ability and/or incentive to unilaterally decrease capacity and/or engage in coordinated conduct on these routes based on the following characteristics:

- routes on which the Applicants overlap
- routes on which one of the Applicants operates and there is a competitor also operating and
- routes on which only one of the Applicants operates and no competitor operates

429. The ACCC's assessment has also taken into account the likelihood of entry or exit by the Applicants operating independently, absent the Alliance.

430. These routes include routes that the airlines operate seasonally.

Major trans-Tasman routes

431. As noted above the major trans-Tasman routes include:

The Auckland routes (56.6% of total trans-Tasman capacity)[92]:

1. Auckland-Sydney (25.8% of total trans-Tasman capacity)
2. Auckland-Melbourne (16.3% of total trans-Tasman capacity)
3. Auckland-Brisbane (14.4% of total trans-Tasman capacity)

The Christchurch routes (15.3% of total trans-Tasman capacity):

1. Christchurch-Sydney (8.5% of total trans-Tasman capacity)
2. Christchurch-Melbourne (3.8% of total trans-Tasman capacity)
3. Christchurch-Brisbane (3% of total trans-Tasman capacity)

The Wellington routes (12.8% of total trans-Tasman capacity):

1. Wellington-Sydney (6% of total trans-Tasman capacity)

[92] The percentage of total trans-Tasman capacity is for the year ending February 2013 and is based on airline supplied data provided by BITRE.

2. Wellington-Melbourne (3.8% of total trans-Tasman capacity)

3. Wellington-Brisbane (3% of total trans-Tasman capacity)

The Auckland routes

432. For the year ending February 2013, the major Auckland routes accounted for 56.5% of capacity on the trans-Tasman.

Auckland-Sydney

433. The Applicants, the Qantas/Group-Emirates alliance and two other airlines[93] operate on this route, which in February 2013 accounted for 2,092,878 of total trans-Tasman (around 25.8%) capacity with 11% of passengers travelling between Sydney and New Zealand travelling for business purposes and 34% for leisure purposes.[94] The remaining passengers fall into various categories including, travel for educational purposes.

434. The table below demonstrates that, combined, the Applicants share of total seat capacity was 38.6% on this route for the year ended February 2013.

Table D.5 – Airline share (%) of total capacity, seats flown for AKL-SYD, year ended February

Airline	2011	2012	2013
Air New Zealand	29.5	32.2	34.1
Virgin Australia	6.2	5.7	4.6
combined Alliance Total	35.7	37.8	38.6
Emirates	16.4	16.5	16.9
Jetstar	6.0	5.5	5.2
Qantas Airways	30.1	29.5	28.9
combined Qantas Group/Emirates alliance Total	52.6	51.5	51.0
Aerolineas Argentinas	4.6	3.2	1.2
China Airlines	0.0	0.0	2.1
LAN Airlines	7.2	7.5	7.1
Total (%)	100.0	100.0	100.0
Seats ('000)	2131.8	2140.3	2092.9

Auckland-Melbourne

435. The Applicants and the Qantas Group-Emirates alliance operate on this route, which in February 2013 accounted for 1,322,318 seats or 16.3% of total trans-Tasman traffic. For the year ending February 2013, 10% of passengers travelling between Melbourne and New Zealand travelled for business purposes and 35% for leisure.[95]

436. The table below demonstrates that, combined, the Applicants' share of total seat capacity was 40.8% on this route for the year ending February 2013.

[93] Aerolineas Argentinas has ceased operating services on this route from 1 July 2012.
[94] See definition of purpose of travel categories in footnote 85.
[95] See definition of purpose of travel categories in footnote 85.

Table D.6 – Airline share (%) of total capacity, seats flown for AKL-MEL, year ended February

Airline	2011	2012	2013
Air New Zealand	34.2	31.8	31.2
Virgin Australia	11.9	10.4	9.7
combined Alliance Total	46.0	42.3	40.8
Emirates	20.7	20.7	22.5
Jetstar	2.5	9.4	9.3
Qantas Airways	30.7	27.6	27.3
combined Qantas Group/Emirates alliance Total	54.0	57.7	59.2
Total	100.0%	100.0%	100.0%
Seats ('000)	1101.7	1249.9	1322.3

Auckland-Brisbane

437. The Applicants, the Qantas Group-Emirates alliance and China Airlines operate services on this route, which accounted for a total capacity of 1,167,616 or 14.4% of total trans-Tasman capacity. For the year ending February 2013, 5% of passengers who travelled between Brisbane and New Zealand travelled for business purposes and 40% for leisure.[96]

438. The data for this route shows that the combined Alliance capacity share was 49.1% of total route capacity in the year ending February 2013.

Table D.7 – Airline share (%) of total capacity, seats flown for AKL-BNE, year ended February

Airline	**2011**	**2012**	**2013**
Air New Zealand	41.2	36.5	31.7
Virgin Australia	13.8	12.8	17.4
combined Alliance Total	55.0	49.3	49.1
Emirates	21.1	23.1	22.1
Qantas Airways[97]	21.7	19.6	20.6
combined Qantas Group/Emirates alliance Total	42.8	42.7	42.7
China Airlines	0	7.9	8.2
Royal Brunei Airways	0.6	0	0
Total (%)	100.0	100.0	100.0
Seats ('000)	943.6	1,120.0	1,167.6

Competition assessment of the Auckland routes

Unilateral effects

439. The ACCC has examined the likely impact of the Alliance on the three main Auckland routes: Auckland – Sydney, Auckland – Melbourne and Auckland – Brisbane.

96 See definition of purpose of travel categories in footnote 85.

97 Jetstar also operated 1 flight in both the year ending February 2012 and February 2013, which rounds to 0.0% share

440. On the Auckland-Melbourne route, the Alliance reduces the number of independently determined price/service offerings from three to two (that is, the Alliance on the one hand, and the Qantas Group-Emirates alliance on the other). On the other two Auckland routes, there are additional services available to consumers from FFCs (that is, China Airlines on the Auckland-Brisbane route and both China Airlines and LAN on the Auckland-Sydney route).

441. The extent of competitive constraint offered by these FFCs needs to be viewed in light of their relatively limited schedules and frequencies, which are driven by the FFCs' broader network considerations. As a result of this, the ACCC is of the view that FFCs are likely to have only limited ability and incentive to respond to any attempt by the Alliance to reduce or limit growth in capacity on the routes under consideration. This was also the view reached by the ACCC when considering the application for authorisation in relation to the Qantas-Group/Emirates alliance.[98] However, given that the presence of an FFC increases capacity on a route, the ACCC considers that decisions by FFCs to deploy capacity will have some effect on the capacity and pricing decisions of incumbent airlines on the route. Therefore, the ACCC considers that the FFCs will provide some constraint on the Alliance to the extent that, as part of broader network considerations, it is feasible for an FFC to deploy capacity on the Auckland routes.

442. On this basis, the ACCC considers that the major competitive constraint on the Alliance will, for the foreseeable future, come from the Qantas-Group/Emirates alliance on the Auckland routes.[99] For example on Auckland-Melbourne, the Qantas Group has gained capacity share with strong growth by Jetstar between the years ending February 2011 and 2013 (it went from 2.5% to 9.3%). Over the same period, the combined capacity share of Virgin Australia and Air New Zealand decreased from 46% to 40.8%.

443. As noted above, Virgin Australia/Air New Zealand currently account for between 38% and 49% of the seats flown on each of the Auckland routes. Virgin Australia accounts for between 4.7% on Auckland-Sydney and 17.4% on Auckland-Brisbane. The ACCC notes that rivalry, particularly for business customers, is likely to be closest between Air New Zealand and the Qantas Group in the absence of the Alliance. In this regard, the ACCC notes that Virgin Australia's current market share is relatively small especially on the Sydney and Melbourne routes.

444. The ACCC notes that the Qantas-Group/ Emirates alliance is subject to a capacity condition on these routes. This requires the Qantas-Group/Emirates alliance to maintain an aggregated base level capacity on the three Auckland routes and Christchurch-Sydney. The capacity condition limits the manner in which the Qantas-Group/Emirates alliance could otherwise profitably reduce capacity on the Auckland routes.

445. The ACCC considers that the independent FFCs (China Airlines and LAN) would be unlikely to increase capacity on the route in response to the Alliance partners raising fares. However, as noted above the ACCC has taken into account the

[98] ACCC, *Determination- Applications for Authorisation A91332-A91333 lodged by Qantas and Emirates*, 27 March 2013, p.103 at [501]

[99] The ACCC notes that authorisation for the Qantas-Group/Emirates alliance expires in 2018. Absent the Qantas-Group/Emirates alliance the ACCC considers that the major competitive constraint will come from the Qantas Group, and to a lesser extent, from Emirates.

ability of FFCs to add capacity which may act as a constraint on the Auckland routes.

446. Absent the Alliance, the ACCC considers that Virgin Australia's capacity share may be relatively small compared to Qantas-Group/Emirates and Air New Zealand on the Auckland routes and in particular, Auckland-Sydney and Auckland-Melbourne. The ACCC therefore considers that absent the Alliance Virgin Australia is likely to be less of a constraint on the other competitors on the Auckland-Sydney and Auckland-Melbourne routes. The Qantas Group would only have to add a relatively small amount of capacity to replace the constraint lost by the Alliance on these two routes.

447. In relation to the Auckland-Brisbane route, and in light of Virgin Australia's hub at Brisbane airport, Virgin Australia has a greater presence and presents a stronger potential competitive constraint on the route in the future without the Alliance. The ACCC notes that this route was subject to a condition under the 2010 authorisation. The ACCC considered that the likely competition effect on this route was uncertain. In 2010 it was concerned about the ability of the Alliance partners to raise prices or reduce capacity having regard to the existing competitive constraints. In 2010 the ACCC considered that the Alliance was likely to be less constrained by Qantas in terms of pricing constraint than by Jetstar operating on a route. Jetstar was not (and still does not) operate on the Auckland-Brisbane route.

448. Since the 2010 authorisation, China Airlines has entered Auckland-Brisbane and Emirates has recently announcement that it is increasing capacity on the route.[100] The ACCC considers that the combination of Qantas-Group/Emirates and China Airlines may provide some constraint on the Alliance.

449. The ACCC has also assessed the likelihood of timely entry into the trans-Tasman as a constraint on the Alliance.

450. The ACCC has previously acknowledged that entry into the trans-Tasman and expansion on to additional routes is possible, although such entry is more likely on some city pair routes than others.[101] The ACCC notes that the trans-Tasman operates as a Single Aviation Market, with Australian and New Zealand designated airlines able to set their own capacities and frequencies.

451. However, other than the currently operating carriers, the ACCC is not aware of any other Australian or New Zealand designated airlines which would be able to enter in a timeframe and on a scale necessary to provide a competitive constraint.

452. While the ACCC acknowledges that there are a number of international carriers with unexercised fifth freedom rights that could participate on the trans-Tasman, the ACCC does not consider that their entry in response to an attempt by the Alliance to reduce or limit growth in capacity is likely to be timely or sufficient on the grounds that the decision for entry by an international carrier is unlikely to be determined by the existence of economic profits resulting from the exercise of market power by the Alliance on the trans-Tasman routes. In addition to the factors

[100] See http://www.emirates.com/english/about/news/news_detail.aspx?article=1223102&offset=0 (last accessed 6 June 2013) - Emirates will deploy an A380 to the route which will increase capacity by of 1,890 seats a week.

[101] ACCC, Determination for applications A91227 and A91228 lodged by Virgin Australia and Air New Zealand (2010), p. 69.

discussed regarding FFCs above, a carrier in this position would also need to examine the viability of the long haul component of its service (international into Australia) before deciding whether to extend that service into New Zealand.

453. The ACCC is not aware of any certain plans by FFCs not currently operating on the trans-Tasman to enter. However, the ACCC notes China Airlines recent entry on two of the Auckland routes: Auckland-Brisbane in 2011 and Auckland-Sydney in 2012. This airline has experienced a relatively rapid capacity increase for the year ending February 2013 (up to 2.1% on Auckland-Sydney and 8.2% on Auckland-Brisbane).

454. The ACCC notes the Applicants' submissions that there is currently excess capacity on the trans-Tasman routes. The ACCC also notes that previously, Qantas and Emirates' have submitted that there is excess capacity on the Auckland routes.[102] The ACCC considers that if there is excess capacity on the Auckland routes:

- it may be commercially rational for airlines to remove capacity from that route; and
- it is more likely that routes with excess capacity will be less commercially viable than routes with optimal, or a shortage of, capacity.

455. In this regard, the ACCC notes Virgin Australia's submission that it is likely to review its service offerings on a range of trans-Tasman routes and reduce or withdraw capacity where necessary for commercial viability if the Alliance is not authorised.[103]

456. Taking these factors and Virgin Australia's submission on the likely future without the Alliance, into account the ACCC considers that, absent the Alliance, one potential scenario is that Virgin Australia's schedule and network offering on the trans-Tasman would be less competitive relative to Qantas or Air New Zealand.

457. Therefore while the Alliance has the result of reducing the number of Australian and New Zealand designated airlines from three to two on the Auckland routes, the ACCC considers that the Alliance is unlikely to have a significant impact on competition on these routes. This is due to the fact that the ACCC considers that Virgin Australia's stand alone offering in the world without the Alliance is unlikely to be as strong an offering as Air New Zealand and the Qantas Group on some, but not all, of the major Auckland routes. The ACCC notes Virgin Australia's submission that, absent the Alliance, its schedule would return to a limited, low frequency schedule driven by aircraft utilisation. Specifically, on the three main Auckland routes, it has indicated that its schedule frequency would:

- on the Auckland-Sydney route, return to one scheduled flight a day as compared to the Applicants' combined total of six flights;
- on the Auckland-Melbourne route, be one scheduled flight a day as compared to the Applicants' combined total of five flights; and

[102] ACCC, *Determination- Applications for Authorisation A91332-A91333 lodged by Qantas and Emirates*, 27 March 2013.

[103] Virgin Australia's Supplementary Counterfactual Submission

- on the Auckland-Brisbane route, be two scheduled flights a day as compared to the Applicants' combined total of four flights.[104]

458. The ACCC further notes that Virgin Australia presently accounts for 9.3% of combined capacity on these routes, and that the limited frequencies offered by Virgin Australia on the Auckland-Sydney and Auckland-Melbourne routes would make it relatively more difficult for it to compete for corporate customers, particularly if Virgin Australia were to reduce capacity levels further in response to the current conditions on the route (which is characterised by the airlines as suffering from excess capacity).

459. The ACCC notes that the three main Auckland routes account for more than 50% of total trans-Tasman capacity and are significant routes for an airline to fly if it is seeking to compete on the trans-Tasman and specifically if it intends to compete for business and corporate customers.

460. The ACCC notes that Virgin Australia has made extensive submissions on the importance of corporate customers to its business moving forward. Given the higher prevalence of business passengers on the Auckland routes, the ACCC does not rule out the possibility that Virgin Australia may choose to increase frequencies on the Auckland routes to attract these customers, at least returning to the number of frequencies it operated prior to entering into the Alliance.

461. Based on the information available, the ACCC has formed the view that it is unlikely that Virgin Australia would be as strong a competitor against Air New Zealand and the Qantas Group on the major Auckland routes in the world without the Alliance. The ACCC notes that, in addition to the Qantas-Group/Emirates alliance's presence on the three routes, on the Auckland-Sydney and Auckland-Brisbane routes the Alliance faces competition from FFCs. Further, the Qantas-Group/Emirates alliance's capacity condition limits that alliance's ability to reduce capacity on the three Auckland routes. The ACCC's view is that the competitive effect of the Alliance on Auckland-Brisbane is uncertain, although the additional confidential information provided by the Applicants after the draft determination has indicated that absent the Alliance Virgin is unlikely to be as strong a competitive constraint against the other major airlines on that route. As a consequence, the ACCC considers that the Alliance is unlikely to significantly increase the Applicants' ability to unilaterally reduce capacity or raise prices on the three major Auckland routes.

<u>Coordinated effects</u>

462. The tables set out earlier show that Qantas/Jetstar and Virgin Australia/Air New Zealand supply the vast majority of capacity on the Auckland routes and they have relatively similar offerings. It is arguable that this creates a strong incentive for Qantas/Jetstar and Virgin Australia/Air New Zealand to co-ordinate their conduct. To the extent that coordination could occur, the ACCC considers that it would occur through a common strategy to limit growth in capacity or by price leadership.

463. The ACCC has considered the extent to which the Alliance is likely to increase the likelihood of coordinated conduct on the Auckland routes. As noted in the

[104] Virgin Australia, Supplementary evidence on the importance of the Alliance to competition for corporate and high frequency travellers in Australia and on the trans-Tasman, 3 July 2013, pp.10-11.

coordinated effects section, there are a number of factors which suggest that there is a risk of coordinated conduct across the trans-Tasman.

464. To the extent that Virgin Australia would have divergent incentives absent the Alliance, this may decrease any risk of coordinated conduct amongst competing airlines on the trans-Tasman. In this regard, the ACCC notes submissions by Virgin Australia that absent the Alliance it is likely to have a reduced presence on the trans-Tasman, including the Auckland routes.

465. The ACCC also notes the lack of evidence of any coordinated conduct over the two years of the Alliance with capacity growth occurring over that time.

466. Taking all of the above into account, the ACCC considers that there is an increased risk of coordinated conduct occurring in regard to price and capacity as a result of Alliance over the longer term, which results in public detriment. However, the extent of the public detriment arising as a result of an increased risk of coordinated conduct is uncertain. Therefore, the ACCC proposes to closely monitor the Alliance and the conduct of the airlines operating on the trans-Tasman over the period of the authorisation. The ACCC may take this into account when considering future authorisation applications and the weight to be given to the balance of benefits and detriments in any future application.

Conclusion on public detriments on the Auckland routes

467. As noted above, the ACCC has reached the view that the Alliance is unlikely to significantly increase the Applicants' ability and incentive on Auckland-Sydney, Auckland-Melbourne and Auckland-Brisbane to unilaterally reduce capacity or increase prices when compared to the likely future without the Alliance.

468. The ACCC recognises that there are factors that increase the risk of coordinated conduct on the Auckland routes over the longer term as a result of the Alliance. The ACCC considers that the Alliance increases the risk of coordination, which results in public detriment. However, the extent of the public detriment arising as a result of an increased risk of coordinated conduct is uncertain. Given the significant anticompetitive detriment that can result as a consequence of coordinated conduct, the ACCC will closely monitor the Alliance in relation to assessing any increased likelihood of coordination.

The Christchurch routes

469. For the year ending February 2013, the major Christchurch routes accounted for 15.3% of capacity on the trans-Tasman.

Christchurch-Sydney

470. The Applicants and the Qantas Group-Emirates alliance operate on this route, which for the year ending February 2013 accounted for 690,566 seats (around 8.5% of total trans-Tasman traffic) with 11% of passengers who travelled between

Sydney and New Zealand travelling for business purposes and 34% for leisure purposes.[105]

471. The table below demonstrates that, combined, the Applicants had a 29.2% share of capacity on the route for the year ending February 2013.

Table D.8 – Airline share (%) of total capacity, seats flown for CHC-SYD, year to February

Airline	2011	2012	2013
Air New Zealand	23.5	23.3	23.1
Virgin Australia	10.3	7.7	6.1
combined Alliance Total	33.8	31.0	29.2
Emirates	32.6	36.2	37.4
Jetstar	16.8	16.0	15.5
Qantas Airways	16.8	16.8	17.9
combined Qantas Group/Emirates alliance Total	66.2	69.0	70.8
Total	100.0	100.0	100.0
Seats ('000)	785.6	711.8	690.6

Christchurch-Melbourne

472. The Applicants and Jetstar operate on this route, which for the year ending February 2013 accounted for 309,700 seats or 3.8% of total trans-Tasman traffic. In the year ending February 2013, 10% of passengers travelling between Melbourne and New Zealand travelled for business purposes and 35% for leisure.[106]

473. The table below demonstrates that, combined, the Applicants had a 63% share of capacity on this route for the year ending February 2013.

Table D.9 – Airline share (%) of total capacity, seats flown for CHC-MEL, year to February

Airline	2011	2012	2013
Air New Zealand	34.8	36.8	40.3
Virgin Australia	27.6	24.9	22.7
combined Alliance Total	62.4	61.7	63.0
Jetstar[107]	37.6	38.	36.9
combined Qantas Group Total	37.6	38.3	37.0
Total	100.0	100.0	100.0
Seats ('000)	383.7	332.2	309.7

Christchurch-Brisbane

474. The Applicants and the Qantas Group operate services on this route, which accounted for a total capacity of 280,086 or 3% of total trans-Tasman capacity for the year ending February 2013.For the year ending February 2013, 5% of

[105] See definition of purpose of travel categories in footnote 85.
[106] See definition of purpose of travel categories in footnote 85
[107] Qantas flew a single outbound service in the year ending February 2013 which rounds to 0.1% share.

passengers travelled for business purposes between Brisbane and New Zealand and 40% for leisure.[108]

475. The data for this route shows that the combined Virgin-Air New Zealand capacity share for the year ending February 2013 was 98.6% on this route. In January 2012, Jetstar announced its complete withdrawal from this route and it ceased operations on the route in March 2012. Qantas flew one flight in July 2011.[109]

Table D.10 – Airline share (%) of total capacity, seats flown for CHC-BNE, year to February

Airline	2011	2012	2013
Air New Zealand	28.1	34.20	45.6
Virgin Australia	42.5	37.9	53.0
combined Alliance Total	**70.6**	**72.1**	**98.69**
Qantas Airways	0	0.05	0
Jetstar	29.4	27.89	1.4
Total (%)	100.0	100.0	100.0
Seats ('000)	434.08	364.02	280.08

Competition assessment of the Christchurch routes

Unilateral effects

476. The ACCC has examined the likely impact of the Alliance on the three main Christchurch routes: Christchurch-Sydney, Christchurch-Melbourne and Christchurch-Brisbane.

477. On the Christchurch-Brisbane route, the Alliance reduces the number of independently determined price/service offerings from two to one (that is, Virgin Australia and Air New Zealand to the Alliance). On the other two Christchurch routes, the Alliance results in a reduction from three to two: the Alliance and Jetstar on Christchurch-Melbourne and the Alliance and Qantas, Jetstar and Emirates on Christchurch-Sydney.

478. The ACCC acknowledges that the Christchurch routes have been impacted by a reduction in demand as a result of the earthquakes in Christchurch in 2011. The ACCC understands that Australian visitors to Christchurch for holiday purposes have declined by more than 85,000 or 40% for the year ending June 2010 to June 2012.[110] However, the ACCC also notes that load factors on the Christchurch routes have generally been high for the airlines operating on these routes and that this may indicate unmet demand.[111]

479. The ACCC notes Virgin Australia's submission that it is likely to review its service offerings on a range of trans-Tasman routes and reduce or withdraw capacity

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108 See definition of purpose of travel categories in footnote 85.

109 Airline supplied BITRE data for year ending February 2013.

110 Virgin Australia & Air New Zealand, Submission in support, p.14 referencing Statistics New Zealand *International Travel and Migration Statistics* at www.stats.gov.nz.

111 Christchurch International Airport Ltd, Submission on Application for re-authorisation of Australian Airline Alliance by Virgin Australia & Air New Zealand, 26 April 2013, p. 4.

where necessary for commercial viability if the Alliance is not authorised.[112] The ACCC considers that, absent the Alliance, Virgin Australia's schedule and network offering on the trans-Tasman is likely to reflect a more limited competitive offering relative to that provided by Qantas and Air New Zealand, specifically for business passengers.

480. In relation to the Christchurch-Sydney route, the ACCC notes Virgin Australia's capacity share is relatively low (6.1% for the year ending February 2013) and considers that, absent the Alliance, Virgin Australia is unlikely to be as strong a competitor against Air New Zealand and the Qantas Group. As with the Auckland routes, the ACCC considers that the closest rivalry is likely to be between Air New Zealand and Qantas-Group/Emirates on the Christchurch-Sydney route. Emirates has significant, if lumpy, capacity available on this route as a consequence of the nature of FFC deployment. The ACCC has also had regard to the operation of the capacity condition on the Christchurch-Sydney route which will limit the Qantas Group-Emirates alliance from reducing capacity on this route below the level required. The ACCC notes that the capacity available on the route suggests that the Alliance would be constrained by the relevant Qantas Group-Emirates offerings on the Christchurch-Sydney route.

481. Jetstar is the only competitor to the Alliance on the Christchurch-Melbourne route. The ACCC considered in the draft determination that Jetstar is likely to offer a limited constraint to any reduction in capacity by the Alliance on that route. In 2010 the ACCC was of the view that Jetstar operating on this route was likely to provide a sufficient constraint on the Alliance. Having regard to Virgin Australia's changing product offering as part of the Game Change strategy and its shift away from operating as a low cost carrier, the ACCC considered in the draft determination that Jetstar is likely to act as less of a constraint on the Alliance in the future and that therefore the Alliance is likely to face limited competitive constraint on this route. The ACCC therefore proposed to add a capacity condition to this route.

482. Following the draft determination, the Applicants submit that the Christchurch-Melbourne route is one that Jetstar competes strongly on, having close to 40% capacity share. They submit that the overwhelming majority of passengers on the route are holiday or VFR passengers (approximately 83%) and as a result are highly price sensitive. Jetstar provides strong competition on such a leisure route and is a proven and effective competitor.[113]

483. The ACCC has taken into account the Applicants' submissions about the competitive constraint posed by Jetstar on the Christchurch-Melbourne route. However taking into account the dominant position of the Alliance on the route and potential competition between the Alliance partners absent the Alliance, the public statements from the Qantas-Group that they are unlikely to add capacity in the foreseeable future, and the differentiated product offering of Jetstar, the ACCC remains of the view that Jetstar is unlikely to be in a sufficient position to constrain the Alliance on this route.

484. In relation to Christchurch-Brisbane, the ACCC notes that the Applicants are the only operators on this route since Jetstar's exit. The ACCC is not aware of any planned re-entry by Jetstar or Qantas on this route and notes the Qantas Group

112 Virgin Australia & Air New Zealand, Submission in relation to Virgin Australia's Counterfactual, 25 June 2013.

113 Virgin Australia & Air New Zealand, Submission in response to draft determination, Annexure B, p.8

statements to the effect that it does not intend to increase capacity on the trans-Tasman in the next five years.

485. Accordingly, and in contrast to the position in 2010, the Alliance is likely to face limited competitive constraint on the Christchurch-Brisbane route and consequently the ACCC is imposing a capacity condition in relation to this route.

486. In relation to entry by an FFC, the ACCC notes CIAL's submission that because of ASAs negotiated by Australia with FFC countries there is limited access to Christchurch as a destination point for FFCs which limits new entry by this class of carrier.[114] CIAL notes that in many instances ASAs require that only one point beyond Australia may be served or a specified port is named, usually Auckland. CIAL notes that there are a number of ASAs between Australia and governments in Asia that have restrictive flying opportunities to Christchurch via Australia.[115] This is consistent with the ACCC's understanding of beyond point ASA capacity available to FFCs into New Zealand via Australia. The ACCC also notes that a FFC is likely to have less incentive to enter a Christchurch route given the relative size of these routes as compared to Auckland and also the reduction in demand on Christchurch routes following the 2011 earthquakes. The ACCC considers that even if there was FFC entry on Christchurch-Brisbane or one of the other two routes, for the reasons discussed earlier the ACCC does not consider that an FFC is likely to pose the same level of competitive constraint as the Qantas Group-Emirates on the Alliance.

487. Overall, the ACCC remains of the view that the Alliance is unlikely to increase the ability and incentive of the Applicants to unilaterally reduce or limit growth in capacity on the Christchurch-Sydney route. However, the ACCC considers that the Alliance is likely to face limited competitive constraint on Christchurch-Melbourne and no immediate competitive constraint on Christchurch-Brisbane. Therefore on these routes, the ACCC considers that the Alliance is likely to give the Applicants an increased ability and incentive to raise price, or reduce capacity or service, and that this will result in public detriment.

Coordinated effects

488. The ACCC has considered the extent to which the Alliance is likely to increase the risk of coordinated conduct on the Christchurch routes. As noted in the **coordinated effects** section above, there are a number of factors which suggest that there is a risk of coordinated conduct on the trans-Tasman routes.

489. To the extent that Virgin Australia would face divergent incentives absent the Alliance, this may decrease any risk of coordinated conduct amongst competing airlines on the trans-Tasman. In this regard, the ACCC notes submissions by Virgin Australia that absent the Alliance it is likely to have a reduced presence on the trans-Tasman.

490. For Christchurch-Sydney and Christchurch-Melbourne, the ACCC considers that there is unlikely to be entry for the reasons discussed above in paragraphs 470 – 480, to disrupt any increased incentive for the Alliance and the Qantas Group-Emirates alliance to coordinate. As with its assessment of the Auckland routes, the

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[114] CIAL, Submission, p.15
[115] CIAL, Submission, p.15

ACCC does not have any evidence of coordinated conduct on the Christchurch routes during the period of the 2010 authorisation.

491. The ACCC considers that there is an increased risk of coordinated conduct occurring in regard to price and capacity as a result of Alliance over the longer term, which results in public detriment. However, the extent of the public detriment arising as a result of an increased risk of coordinated conduct is uncertain. Therefore, the ACCC proposes to closely monitor the Alliance throughout the period of authorisation.

Conclusion on public detriments on the Christchurch routes

492. The ACCC considers that the Alliance is likely to increase the ability and the incentive of Virgin Australia and Air New Zealand to reduce capacity on the Christchurch-Melbourne and Christchurch-Brisbane routes in the future with the Alliance when compared to the future without the Alliance. In the ACCC's view, there is insufficient competitive constraint to prevent a unilateral decrease in capacity on these routes. The ACCC considers that the Alliance is likely to result in public detriment on the Christchurch-Brisbane/Melbourne routes.

493. The ACCC recognises that there are factors that increase the risk of coordinated conduct on the Christchurch-Sydney and Christchurch-Melbourne routes as a result of the Alliance. However, the ACCC does not have any evidence of this having occurred. The ACCC considers that the Alliance may increase the risk of coordinated conduct over the longer term given the competitive dynamics and structure of these two routes and accordingly will monitor the Alliance in relation to coordinated effects.

The Wellington routes

494. For the year ending February 2013, the major Wellington routes accounted for 12.8% of capacity on the trans-Tasman.

Wellington-Sydney

495. Air New Zealand and Qantas Airways operate services on this route, which accounted for a total capacity of 459,152 or 6% of total trans-Tasman capacity in the year ending February 2013. Of the travellers between Sydney and New Zealand approximately 11% were travelling for business purposes in 2013 and 34% for leisure purposes.[116]

496. The table below demonstrates that the Alliance's share of capacity was 48.7% on this route in the year ending February 2013.

[116] See definition of purpose of travel categories in footnote 53.

Table D.11 – Airline share (%) of total capacity, seats flown for WLG-SYD, year to February

Airline	2011	2012	2013
Air New Zealand	35.1	39.1	48.7
Virgin Australia	15.0	10.7	0
combined Alliance Total	50.1	49.8	48.7
Qantas Airways	49.8	50.2	51.3
Jetstar	0	0.4	0
combined Qantas Group Total	49.8	50.6	51.3
Total (%)	100.0	100.0	100.0
Seats ('000)	393.5	463.7	459.2

Wellington-Melbourne

497. Air New Zealand and Qantas Airways operate services on this route, which accounted for a total of 239,977 or 3.8% of total trans-Tasman capacity for the year ending February 2013. Of the travellers between Melbourne and New Zealand approximately 8% were travelling for business purposes in 2013 with 18% travelling for leisure and 51% nominating 'other' as the reason for travel.[117]

498. The table below demonstrates that the Alliance, through Air New Zealand, had approximately 50.6% of capacity on this route for the year ending February 2013.

Table D.12 – Airline share (%) of total capacity, seats flown for WLG-MEL, year to February

Airline	2011	2012	2013
Air New Zealand	50.2	50.1	50.6
Qantas Airways	49.8	49.9	49.4
Total (%)	100.0	100.0	100.0
Seats ('000)	196.9	231.1	239.9

Wellington-Brisbane

499. Virgin Australia and Air New Zealand were the only two airlines operating on this route in the year ending February 2013. Air New Zealand reduced its capacity on the route significantly over the period. The route accounted for a total capacity of 260,900 or 3% of total trans-Tasman capacity. For the year ending February 2013, 5% of passengers travelled for business purposes between Brisbane and New Zealand and 40% for leisure.[118]

Table D.13 – Airline share (%) of total capacity, seats flown for WLG-BNE, year to February

Airline	2011	2012	2013
Air New Zealand	45.5	30.9	0.1
Virgin Australia	54.5	69.1	99.9
Total (%)	100.0	100.0	100.0
Seats ('000)	240.4	254.1	260.9

117 See definition of purpose of travel categories in footnote 82.
118 See definition of purpose of travel categories in footnote 82.

Competition assessment of the Wellington routes

Unilateral effects

500. The ACCC has examined the likely impact of the Alliance on the three main Wellington routes: Wellington-Sydney, Wellington-Melbourne and Wellington-Brisbane.

501. On the Wellington-Brisbane route, the Alliance reduces the number of independently determined price/service offerings from two to one (that is, Virgin Australia and Air New Zealand competing independently on the one hand to the Alliance on the other). On the Wellington-Sydney route, the Alliance reduces the number of independently determined price/service offerings from three to two (that is, the Alliance on the one hand, and the Qantas Group-Emirates alliance on the other). Virgin Australia has removed its aircraft from the Wellington-Sydney route as a result of schedule optimisation under the 2010 authorisation and Air New Zealand has exited Wellington-Brisbane for the same reason. The Alliance has not changed the number of independently determined price/service offerings on the Wellington-Melbourne route.

502. The Wellington routes were three of the six nominated routes under the 2010 authorisation, that is, the Applicants were required to maintain and grow capacity on these routes as against the scheduled capacity on the routes for the base year.[119]

503. In 2010, the ACCC considered that, on the Wellington-Sydney route, Qantas was unlikely to provide a sufficient competitive constraint on the route and it was unlikely to deploy Jetstar on the route. The ACCC reached the view that the Alliance would have the incentive and ability to raise fares or reduce capacity.[120]

504. In relation to the Wellington-Melbourne route, in 2010 the ACCC believed that there were reasonable grounds to consider that, absent the Alliance, Virgin Australia might enter the route and concluded that the Alliance would remove a significant competitive constraint by removing the threat of entry by Virgin Australia.[121]

505. In 2010, the Wellington-Brisbane route was a monopoly route for the Alliance, although both Applicants operated services on the route. The ACCC concluded that the Alliance would face limited competitive constraint and would have the ability and incentive to raise fares, reduce capacity or otherwise reduce their service offering.[122]

506. In relation to Virgin Australia's withdrawal of its aircraft from the Wellington-Sydney route, the ACCC notes the Applicants' submission that Virgin Australia's exit from this route was part of the Alliance's schedule optimisation strategy as it would make use of Air New Zealand's market presence on this route and give Virgin

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119 Year ending 31 October 2010 – see Capacity Condition to Determination for applications for authorisation A91227 & A91228 lodged by Virgin Blue Airlines Pty Ltd and Others, dated 16 December 2010.

120 ACCC, Determination in relation to applications A91227 & A91228 lodged by Virgin Blue Airlines Pty Ltd and Ors, 16 December 2010, pp. 81-82.

121 ACCC, Determination in relation to applications A91227 & A91228 lodged by Virgin Blue Airlines Pty Ltd and Ors, 16 December 2010, pp. 82-83.

122 ACCC, Determination in relation to applications A91227 & A91228 lodged by Virgin Blue Airlines Pty Ltd and Ors, 16 December 2010, p. 83.

Australia the opportunity to concentrate its efforts on the Wellington-Brisbane route, making use of Virgin's Brisbane hub.[123]

507. In response to the draft determination, KWSG submits that absent the Alliance, Virgin Australia (and indeed all airlines flying the trans-Tasman) would wish to review operations on the various trans-Tasman routes in light of any decision not to reauthorise the Alliance. KWSG submits that it is most likely that absent the Alliance, Virgin Australia would seek to re-enter the Wellington- Sydney route and that its majority-owned subsidiary, Tiger, would enter the Wellington-Melbourne route.

508. With respect to the Wellington - Brisbane route, KWSG submits that if the Alliance is not re-authorised, it agrees with the ACCC that Virgin Australia would continue to operate services on the Wellington-Brisbane route, and expects that Air New Zealand may be likely to re-enter this route. Further, KWSG submits that in response to Air New Zealand's entry onto the Wellington-Brisbane route, it expects that, given capacity and demand considerations, Virgin Australia will withdraw some of its services in each direction between Wellington-Brisbane so that it would operate at a similar frequency to Air New Zealand. The likely future without the Alliance on the Wellington-Brisbane route, according to KWSG, is therefore that each of Air New Zealand and Virgin Australia will operate a similar frequency, including some "wingtip" services, as it had existed before the Alliance was authorised.[124]

509. In relation to Wellington-Sydney, given the close competitive rivalry between the product offering of Qantas and Air New Zealand, the ACCC considers that if Virgin Australia were to seek to re-enter the route absent the Alliance it would be unlikely to provide as significant a competitive offering as Qantas and Air New Zealand. The ACCC considers that the size of the Wellington-Sydney route and Virgin Australia's intention to reduce its capacity and review its schedule absent the Alliance may diminish Virgin Australia's incentives to re-enter and compete on this route, without the Alliance, especially for government and corporate customers.

510. In contrast to the view it reached in 2010, the ACCC considers that the Alliance is unlikely to have significant unilateral effects on the Wellington-Sydney route when compared to the likely future without the Alliance. In reaching this view, the ACCC has had regard to Virgin Australia's incentives in relation to likely re-entry and specifically the likelihood of it being able to strongly compete for corporate and government accounts on this route absent the Alliance. The ACCC has also had regard to Jetstar's ad hoc deployment on the route (1 service) in the 12 months ending February 2013 which indicates that Qantas may deploy Jetstar in contrast to the information provided to the ACCC in 2010. However, the ACCC considers that this is unlikely to indicate a future pattern of deployment of Jetstar on the route.

511. In relation to Wellington-Melbourne, the ACCC considers that, absent the Alliance, Virgin Australia is unlikely to enter this route. In reaching this view, the ACCC has had regard to the submission of KWSG and information provided by the Applicants. This view contrasts with the ACCC's 2010 view and is based on the likely future without the Alliance that would see Virgin Australia review its schedule and capacity on the trans-Tasman. The Wellington-Melbourne route has similar characteristics to the Wellington-Sydney route to the extent that both have strong

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123 Virgin Australia & Air New Zealand, Submission in support, p.26.

124 KWSG, Submission in response to the draft determination, 24 July 2013, pp. 6-7.

demand from government and corporate passengers. The ACCC considers that, absent the Alliance, Virgin Australia is likely to have a less strong service offering for corporate and business passengers on this route compared to Qantas and Air New Zealand and therefore considers that it will have a reduced incentive to enter absent the Alliance.

512. The ACCC notes that there are no other airlines operating on the Wellington-Brisbane route to constrain the Alliance's price, capacity and service decisions on this route. The ACCC notes the KWSG's submission that it has no information to suggest that Qantas or Jetstar would enter the Wellington-Brisbane route and notes that neither has flown the route in a number of years.[125] As Virgin Australia has a hub at Brisbane airport and given its existing presence on the Wellington-Brisbane route, the ACCC considers that it is likely, absent the Alliance, that Virgin Australia would continue to operate on this route. The ACCC considers that Air New Zealand may be likely, absent the Alliance, to seek to re-enter the Wellington-Brisbane route given it operated on this route prior to the Alliance and taking into account its strong product offering to corporate and government customers.

513. As a result the ACCC considers that the Alliance is likely to materially enhance the Applicants' ability and incentive to raise price or reduce service on the Wellington-Brisbane route and is retaining a capacity condition for this route.

514. The ACCC considers that entry by a FFC on any of the Wellington routes is unlikely as Wellington Airport cannot physically accommodate the wide bodied aircraft typically operated by FFCs.

515. The ACCC considers that the Alliance is unlikely to significantly alter the extent of competition on the Wellington-Melbourne route. On the Wellington-Sydney route, Virgin Australia's competitive offering is likely to be limited, if any, absent the Alliance such that the Alliance will not significantly alter the ability or incentive of the Alliance to reduce capacity on this route. In relation to Wellington-Brisbane, the ACCC considers that the Alliance is likely to increase the Applicant's ability and incentive to unilaterally reduce capacity and raise fares given the limited competitive constraint faced by the Applicants.

Coordinated effects

516. The ACCC has considered the extent to which the Alliance is likely to increase the likelihood of coordinated conduct on the Wellington routes. As noted in the coordinated effects section, there are a number of factors which suggest that there is a risk of coordinated conduct on the trans-Tasman routes.

517. To the extent that Virgin Australia would have divergent incentives absent the Alliance, this may decrease any risk of coordinated conduct amongst competing airlines on the trans-Tasman. In this regard, the ACCC notes submissions by Virgin Australia that absent the Alliance it is likely to have a reduced presence on the trans-Tasman. The ACCC considers that the Alliance will not result in an increased risk of coordinated conduct on the Wellington-Brisbane route as Virgin Australia is the only airline operating on the route. On Wellington-Melbourne, the ACCC considers that given the absence of Virgin Australia on the route, the Alliance is unlikely to change the incentives of the airlines operating on this route to coordinate. Given the ACCC's views on the lack of likely re-entry by Virgin

[125] Key Wellington Stakeholders Group, Submission, p.11.

Australia absent the Alliance the ACCC considers that the Alliance is unlikely to significantly alter the risk of coordination on the Wellington-Sydney route. The ACCC considers that to the extent that the Alliance increases the risk of coordination on the Wellington-Sydney route, this results in public detriment.

518. The ACCC also notes an absence of any evidence of coordinated conduct during the period of the 2010 authorisation.

Conclusion on public detriments on the Wellington routes

519. The ACCC considers that the Applicants are likely to face a similar level of competitive constraint with or without the Alliance on Wellington-Melbourne and Wellington-Sydney. The ACCC considers that the Alliance is likely to result in the Applicant's having the ability and incentive to unilaterally reduce capacity on Wellington-Brisbane and that this is likely to result in public detriment.

Minor trans-Tasman routes

520. There are eleven minor trans-Tasman routes and 3 seasonal routes which include:

- Auckland-Adelaide (~1% of total trans-Tasman capacity)[126]
- Auckland-Cairns (1.3% of total trans-Tasman capacity)
- Auckland-Gold Coast (4% of total trans-Tasman capacity)
- Auckland-Perth (2.4% of total trans-Tasman capacity)
- Christchurch-Gold Coast (1.1% of total trans-Tasman capacity)
- Dunedin-Sydney (>1% of total trans-Tasman capacity)
- Dunedin-Melbourne (>1% of total trans-Tasman capacity)
- Dunedin-Brisbane (1% of total trans-Tasman capacity)
- Hamilton-Brisbane (0% of total trans-Tasman capacity)
- Hamilton-Sydney (0% of total trans-Tasman capacity)
- Queenstown-Sydney (2.1% of total trans-Tasman capacity)
- Queenstown-Melbourne (1.1% of total trans-Tasman capacity)
- Queenstown-Brisbane (0.5% of total trans-Tasman capacity)
- Rotorua-Sydney (>1% of total trans-Tasman capacity)

[126] The percentage of total trans-Tasman capacity is for the year ending February 2013.

Minor overlap routes

521. Virgin Australia and Air New Zealand overlap on three of the minor trans-Tasman routes. These are: Auckland-Gold Coast, Queenstown-Sydney and Queenstown-Brisbane. These three routes account for approximately 6.6% of capacity on the trans-Tasman for the year ending February 2013.

522. In its assessment of the minor overlap routes, the ACCC has considered the extent to which the Alliance is constrained by other carriers, including the likelihood of entry, the size of the route and available capacity.

Auckland-Gold Coast

523. The Applicants and Jetstar operate on this route, which in the year ending February 2013 accounted for 322,992 seats(around 4% of total trans-Tasman traffic) with 3% of passengers travelling between the Gold Coast and New Zealand travelling for business purposes and 44% travelling for leisure.[127]

524. The table below demonstrates that, combined, Virgin Australia and Air New Zealand had 62.8% of capacity for the year ending February 2013.

Table D.14 – Airline share (%) of total capacity, seats flown for AKL-OOL, year to February

Airline	2011	2012	2013
Air New Zealand	22.9	25.4	25.4
Virgin Australia	38.7	38.4	37.4
combined Alliance Total	61.5	63.8	62.8
Jetstar	38.3	36.2	37.2
Qantas Airways	0.2	0.0	0.1
combined Qantas Group Total	38.5	36.2	37.2
Total	100.0	100.0	100.0
Seats ('000)	336.2	326.3	323.0

Queenstown-Sydney

525. The Applicants and the Qantas Group operate services on this route, which accounted for a total capacity of 178,355 or 2.1% of total trans-Tasman capacity. Of the travellers between Sydney and New Zealand approximately 11% were travelling for business purposes and 34% for leisure purposes.[128]

526. The table below demonstrates that, combined, Virgin Australia and Air New Zealand had 49.7% of capacity on this route in the year ending February 2013.

[127] See definition of purpose of travel categories in footnote 82.
[128] See definition of purpose of travel categories in footnote 82.

Table D.15 – Airline share (%) of total capacity, seats flown for ZQN-SYD, year to February

Airline	**2011**	**2012**	**2013**
Air New Zealand	31.8	35.1	30.9
Virgin Australia	29.7	22.3	18.8
combined Alliance Total	**61.5**	**57.4**	**49.7**
Qantas Airways	38.6	37.4	28.2
Jetstar	0	5.2	22.2
combined Qantas Group Total	**38.6**	**42.6**	**50.4**
Total (%)	100.0	100.0	100.0
Seats ('000)	122	137	178

Queenstown - Brisbane

527. The Applicants and Qantas Airways operate services on this route, which accounted for a total capacity of 40,029 or 0.5% of total trans-Tasman capacity. Of the passengers travelling on this route for the year ending February 2013, 5% of passengers travelled for business purposes between Brisbane and New Zealand and 40% for leisure.[129]

528. The table below demonstrates that, combined, Virgin Australia and Air New Zealand had 92.3% of capacity on this route in the year ending February 2013.

Table D.16– Airline share (%) of total capacity, seats flown for ZQN-BNE, year to February

Airline	**2011**	**2012**	**2013**
Air New Zealand	63.7	44.4	22.6
Virgin Australia	24.3	45.6	69.6
Total combined Alliance	**88.0**	**90.0**	**92.3**
Qantas Airways	12.0	9.90	7.7
Total (%)	100.0	100.0	100.0
Seats ('000)	34050	36644	40029

Competition assessment of the minor overlap routes

Unilateral effects

529. The ACCC has examined the likely impact of the Alliance on the three minor overlap routes: Auckland-Gold Coast, Queenstown-Sydney and Queenstown Brisbane.

530. On all three overlap routes the Alliance reduces the number of independently determined price/service offerings from three to two (that is, Virgin Australia, Air New Zealand and Qantas/Jetstar to the Alliance and Qantas/Jetstar). However, the ACCC notes that the Alliance has the dominant capacity share on Queenstown-Brisbane. In the likely future without the Alliance, the ACCC considers that Virgin Australia and Air New Zealand would be likely to compete strongly on the Queenstown-Brisbane route.

[129] See definition of purpose of travel categories in footnote 85.

531. In 2010 the ACCC considered that, in relation to the Auckland-Gold Coast route, Jetstar was likely to act as a competitive constraint. In reaching this view, the ACCC had regard to empirical analysis that indicated that Jetstar's entry onto the Auckland-Gold Coast route had the effect of reducing Air New Zealand fares by around 5% to 7%.

532. The ACCC notes the Applicants' submission that the Auckland-Gold Coast route is highly price sensitive given the leisure passenger presence on the route.[130] While the ACCC notes that Jetstar targets leisure passengers, the Alliance provides the Applicants with greater than 60% of capacity on the route and capacity only increased by 2.4% for the 24 months to 31 October 2012. The ACCC has had regard to the changing nature of Virgin Australia's product offering under the Game Change strategy and even though the route is characterised by price sensitive leisure travel, the ACCC considers that Jetstar is likely to operate as less of a constraint on the Alliance in the future.

533. Following the draft determination the Applicants submit that both Jetstar and Qantas operate on the Auckland - Gold Coast route, with Jetstar having a significant 37.2% of total capacity by seats flown. Jetstar provides strong competition to the Alliance, and Qantas (either itself or via Jetstar) could readily expand faster on the route. [131] The Applicants also submit that the Auckland-Brisbane route, and to an extent, Auckland-Maroochydore, are viable substitutes for consumers and further constrain the incentive and ability of the Applicants to raise prices on the Auckland Gold-Coast route. A significant proportion of the traffic on Auckland – Brisbane travels beyond, usually by road, to the Gold Coast.

534. Further, the Applicants submit that Virgin Australia's product improvements as part of its Game Change strategy do not mean that price competition from Jetstar has no competitive constraint upon the Alliance. The high proportion of Air New Zealand's more price-competitive value options ('Seat', 'Seat & Bag' fares) and Virgin Australia's more price-competitive value options ('Saver Lite' and 'Saver' fares) sold by the Alliance is evidence that Virgin Australia, and the Alliance more broadly, still competes on price with Jetstar.[132]

535. The ACCC has taken into account the Applicants' submissions about the competitive constraint posed by Jetstar on this route. The ACCC acknowledges that Auckland-Brisbane in particular may be considered by some customers to be a substitute for Auckland – Gold Coast. However, the ACCC considers that neither of these routes is a perfect substitute for the Auckland-Gold Coast route and if a passenger wishes to travel south of Coolangatta these routes are poor substitutes. The ACCC also notes that the level of constraint provided by China Airlines (the only additional competitor on the Auckland-Brisbane route) in the face of any reduction in capacity by the Applicants on the Auckland-Gold Coast route is likely to be imperfect as China Airlines is an FFC and therefore operates within the more limited schedule and frequency offering that result from broader network considerations.

536. Taking into account the dominant position of the Alliance on the route, public statements from the Qantas-Group that they are unlikely to add capacity in the

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[130] Virgin Australia & Air New Zealand, Submission in support, Annexure I, p.34

[131] Virgin Australia & Air New Zealand, Submission in response to draft determination, Annexure B, pp.5.

[132] Virgin Australia & Air New Zealand, Submission in response to draft determination, Annexure B, pp.5-7

foreseeable future, and the differentiated product offering of Jetstar, together with the ACCC's observations as to the high load factors on the route, the small increase in capacity over the life of the Alliance and the fare increases that have been recently observed, the ACCC remains of the view that Jetstar is unlikely to sufficiently constraint the Alliance on this route. The ACCC considers that the Applicants are likely to have an increased ability to unilaterally reduce capacity and/or raise fares and consequently it is adding a capacity condition to the route.

537. In relation to Queenstown-Sydney, this route was subject to a condition under the 2010 authorisation that required the Alliance to maintain scheduled capacity, subject to a growth factor. In 2010, Jetstar did not operate on this route and the ACCC was concerned about the extent of the competitive constraint on the Alliance.

538. In assessing the Queenstown-Sydney route now, the ACCC acknowledges that this route accounts for a relatively small percentage of capacity on the trans-Tasman as a whole. Nonetheless, the ACCC notes that capacity on the Queenstown-Sydney route increased by 18.1% in the 24 months to 31 October 2012. The ACCC also notes that the Qantas Group has a 50.4% capacity share on this route which increased significantly with Jetstar's entry in December 2011 and its relatively rapid capacity gain in the period since its entry (Jetstar has increased its capacity share to 22.2% on this route). While Queenstown-Sydney was a route of concern in the ACCC's 2010 authorisation, the ACCC considers that the combined Qantas Group offering with both the Qantas Airways and Jetstar brands and the strong overall capacity increase on this route has mitigated the ACCC's 2010 concern to the extent that the ACCC now considers that the Alliance is likely to face competitive constraint from the Qantas Group. Accordingly, the ACCC considers that it is unlikely that the Alliance will have a significantly increased ability or incentive to unilaterally raise price or reduce service on the Queenstown-Sydney route.

539. The ACCC considers that the Alliance is unlikely to be constrained on the Queenstown-Brisbane route given its combined capacity share of 92.3%. While the ACCC acknowledges that Qantas could deploy more capacity on the route, it considers that the route is too small to make this decision a commercially attractive one (absent any other factors that would increase Qantas' incentive to add capacity). In this regard, the ACCC notes Kiss Travel International's submission that the Alliance has resulted in increased fares on this route and notes that Qantas only flies seasonal services between June and August.[133]In the ACCC's view, the Alliance is likely to have an increased incentive to raise price or reduce service levels without a sufficient competitive response from Qantas.

Coordinated effects

540. The ACCC has considered the extent to which the Alliance is likely to increase the likelihood of coordinated conduct on the minor overlap routes. As noted in the coordinated effects section, there are a number of factors which suggest that there is a risk of coordinated conduct on the trans-Tasman routes.

541. To the extent that Virgin Australia faces divergent incentives absent the Alliance, this may decrease any risk of coordinated conduct amongst competing airlines on the trans-Tasman. In this regard, the ACCC notes submissions by Virgin Australia

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[133] Kiss Travel International Submission, 18 March 2013, p.1

that absent the Alliance it is likely to have a reduced presence on the trans-Tasman.

542. The ACCC considers that there is an increased risk of coordinated conduct occurring in regard to price and capacity as a result of Alliance, particularly in relation to the Queenstown-Sydney route, which results in public detriment. However, the extent of the public detriment arising as a result of an increased risk of coordinated conduct is uncertain. Therefore, the ACCC proposes to closely monitor the Alliance throughout the period of authorisation.

Conclusion on public detriments on the minor overlap routes

543. The ACCC considers that the Alliance is likely to increase the ability and the incentive of Virgin Australia and Air New Zealand to reduce capacity on the Auckland-Gold Coast and Queenstown-Brisbane routes. In the ACCC's view, there is insufficient competitive constraint to prevent a unilateral decrease in capacity on these routes and that the Alliance is likely to result in a public detriment on these two routes.

544. The ACCC recognises that there are factors that increase the risk of coordinated conduct on Queenstown-Sydney as a result of the Alliance. However, the ACCC does not have any evidence of this having occurred. The ACCC considers that the Alliance may increase the risk of coordinated conduct on this route given its competitive dynamics and structure and accordingly will monitor the Alliance in relation to coordinated effects.

Minor routes with Alliance partner and competitor airlines

545. There are three trans-Tasman routes on which only one of the Applicants operates with a competitor airline. These routes account for approximately 5.4% of capacity on the trans-Tasman for the year ending February 2013.

546. In its assessment of these routes, the ACCC has considered the extent to which the Applicants would otherwise compete absent the Alliance and whether the Alliance is constrained by other carriers.

Auckland-Cairns

547. Air New Zealand and Jetstar both operate services on this route, which accounted for 105,651 seats or 1.3% of total trans-Tasman capacity. Of the travellers between Cairns and New Zealand approximately 2% were travelling for business purposes in 2013, 32% for leisure and 51% nominate 'other' as the reason for travel.[134]

548. The table below demonstrates that the Alliance had 72.3% of capacity on the route in the year ending February 2013.

Table D.17– Airline share (%) of total capacity, seats flown for AKL-CNS, year to February

Airline	2010	2011	2012
Air New Zealand	62.3	62.2	72.3
Virgin Australia	37.7	11.1	0

[134] See definition of purpose of travel categories in footnote 85.

combined Alliance Total	100	73.3	72.3
Jetstar	0	26.7	27.70
Total (%)	100.0	100.0	100.0
Seats ('000)	93.2	106.8	105.6

Christchurch-Gold Coast

549. Air New Zealand and Jetstar both operate services on this route, which in the year ending February 2013 accounted for 85,948 passengers (around 1.1% of total trans-Tasman capacity) 3% of passengers travelling between the Gold Coast and New Zealand travelling for business purposes and 44% travelling for leisure.[135]

550. The table below demonstrates that the Alliance had 30.3% of capacity on the route in the year ending February 2013.

Table D.18– Airline share (%) of total capacity, seats flown for CHC-OOL, year to February

Airline	2011	2012	2013
Air New Zealand	40.4	34.5	30.3
Jetstar	59.6	65.5	69.7
Total	100.0	100.0	100.0
Seats ('000)	61.8	65.8	85.9

Queenstown-Melbourne

551. Air New Zealand, Qantas Airways and Jetstar operate services on this route which accounted for a total capacity of 85,684 or 1.1% of total trans-Tasman capacity. For the year ending February 2013, 10% of passengers travelling between Melbourne and New Zealand travelled for business purposes and 35% for leisure.[136]

552. The table below demonstrates that, combined, Virgin Australia and Air New Zealand had 34.4% of capacity on this route in the year ending February 2013.

Table D.19– Airline share (%) of total capacity, seats flown for ZQN-MEL, year to February

Airline	2011	2012	2013
Air New Zealand	55.4	34.3	34.4
combined Alliance Total	**55.4**	**34.3**	**34.4**
Qantas Airways	21.6	9.3	3.4
Jetstar	22.9	56.3	62.2
combined Qantas Group Total	**44.5**	**65.6**	**65.6**
Total (%)	100.0	100.0	100.0
Seats ('000)	34.8	65.7	85.7

135 See definition of purpose of travel categories in footnote 85.
136 See definition of purpose of travel categories in footnote 85.

Competition assessment of the minor routes with Alliance partner and competitor

Unilateral effects

553. The ACCC has examined the likely impact of the Alliance on the three minor routes on which one Applicant operates with a competitor: Auckland-Cairns, Christchurch-Gold Coast and Queenstown-Melbourne.

554. On Christchurch-Gold Coast and Queenstown-Melbourne, the Alliance does not affect the number of independently determined price/service offerings. The ACCC does not consider it likely that Virgin Australia would enter these routes absent the Alliance. On the Auckland-Cairns route, the Alliance potentially reduces the independently determined price/service offerings from three to two (that is Virgin Australia, Air New Zealand and Jetstar on the one hand as opposed to the Alliance and Jetstar) depending on whether Virgin Australia is likely to re-enter this route absent the Alliance.

555. The ACCC notes that on the Auckland-Cairns route, Virgin Australia exited this route at the end of October 2011. Before exiting the route it flew two services a week depending on seasonality. The Applicants submit that the decision to remove Virgin Australia metal from the route was based on the strength of Air New Zealand's offering on the route which was largely sold at the New Zealand point of sale, alignment with Air New Zealand's long haul connections and Air New Zealand's fleet flexibility which allowed it to swap A320 for wide body aircraft in peak demand.[137]

556. The ACCC notes Virgin Australia's submission that absent the Alliance it is likely to review its service offerings on a range of trans-Tasman routes and reduce or withdraw capacity where necessary for commercial viability.[138] Balanced against this the ACCC considers that Virgin Australia operated on the Auckland-Cairns route prior to the commencement of the Alliance, and that it may be a viable route for it to re-enter considering that Air New Zealand (which is the major carrier on this route) operates with a similar cost base. Based on the evidence available, the ACCC considers that Virgin Australia may choose not to re-enter this route absent the Alliance. The ACCC also notes Jetstar's entry on the route in April 2011 and has had regard to its view in 2010 that entry by Jetstar was likely to constrain the Alliance given that Jetstar was likely to operate as an independent LCC.

557. In relation to the Christchurch-Gold Coast route, the ACCC does not consider it likely that the Applicants would be likely to compete absent the Alliance as Virgin Australia is unlikely to enter the Christchurch-Gold Coast route. The ACCC also notes the thinness of this route and Jetstar's capacity share of 69.7%. The ACCC considers that the significant capacity Jetstar has deployed on this route will mean that it will likely constrain the Alliance moving forward. On this basis, the ACCC considers it unlikely that the Alliance will increase the Applicants' incentives or ability to raise price or reduce service on this route.

558. The ACCC notes that Air New Zealand only has 34.4% of capacity on Queenstown-Melbourne and that the Applicants would be unlikely to compete

137 Virgin Australia, Response to Information Request dated 17 April 2013, question 5, 14 May 2013.

138 Virgin Australia & Air New Zealand, Submission in relation to Virgin Australia's Counterfactual, 25 June 2013.

absent the Alliance. It also notes that Qantas/Jetstar combined have 65.6% of capacity. As with the Christchurch-Gold Coast route, the ACCC considers that Jetstar's considerable market share on this route will mean that it will likely constrain the Alliance moving forward. Therefore, the ACCC considers it unlikely that the Alliance will increase the Alliance's incentives or ability to unilaterally raise price or reduce service on this route.

Coordinated effects

559. The ACCC has considered the extent to which the Alliance is likely to increase the likelihood of coordinated conduct on these minor routes. As noted in the **coordinated effects** section, there are a number of factors which suggest that there is a risk of coordinated conduct on the trans-Tasman routes.

560. To the extent that Virgin Australia faces divergent incentives absent the Alliance, this may decrease any risk of coordinated conduct amongst competing airlines on the trans-Tasman. In this regard, the ACCC notes submissions by Virgin Australia that absent the Alliance it is likely to have a reduced presence on the trans-Tasman. Further, the ACCC notes that Virgin Australia currently does not operate on any of these routes and given the ACCC's views on the lack of likely entry by Virgin Australia absent the Alliance this is unlikely to change.

561. The ACCC also notes an absence of any evidence of coordinated conduct.

562. Taking into account the above, the ACCC considers that, while there may be an increased risk of coordinated conduct occurring in regard to price and capacity as a result of Alliance on the trans-Tasman, the risk is less on the Auckland-Cairns, Christchurch-Gold Coast and Queenstown-Melbourne routes.

Conclusion on public detriments on the minor routes with Alliance partner and competitor

563. The ACCC considers that the Alliance is unlikely to increase the ability and the incentive of Virgin Australia and Air New Zealand to reduce capacity on Auckland-Cairns, Christchurch-Gold Coast or Queenstown-Melbourne.

Minor monopoly routes

564. The Applicants operate on seven minor trans-Tasman routes that are monopoly routes:

- Dunedin – Brisbane/Sydney/Melbourne
- Auckland – Adelaide/Perth/Sunshine Coast and
- Rotarua – Sydney.

565. Virgin Australia is the only carrier which operates on the Dunedin – Brisbane/Sydney/Melbourne routes. The Dunedin routes accounted for less than 2% of trans-Tasman capacity in the year ending February 2013.

Dunedin – Sydney

566. Virgin Australia is currently the only airline operating on this route. For the year ending February 2013 the route accounted for 3,845 seats (less than 1% of total trans-Tasman traffic). Virgin Australia operates this route on a seasonal basis with flights only being offered in January and December in 2013.

Table D.20 – Airline share (%) of total capacity, seats flown for DUD-SYD, year to February

Airline	2011	2012	2013
Air New Zealand	100.0	13.5	0.0
Virgin Australia	0.0	86.5	100.0
combined Alliance Total	100.0	100.0	100.0
Total	100.0	100.0	100.0
Seats ('000)	6.6	7.5	6.1

Dunedin – Melbourne

567. Virgin Australia is currently the only airline operating on this route. For the year ending February 2013 the route accounted for 3,999 seats (less than 1% of total trans-Tasman traffic). Virgin Australia operates this route on a seasonal basis with flights only being offered in January and December in 2013.

Table D.21– Airline share (%) of total capacity, seats flown for DUD-MEL, year to February

Airline	2011	2012	2013
Air New Zealand	100.0	16.1	0.0
Virgin Australia	0.0	83.9	100.0
combined Alliance Total	100.0	100.0	100.0
Total	100.0	100.0	100.0
Seats ('000)	4.0	7.3	6.1

Dunedin-Brisbane

568. In the year ending February 2013, only Virgin Australia operated services on this route (although both Applicants previously operated), which accounted for a total capacity of 79,190 or 1% of total trans-Tasman capacity. Of the passengers travelling on this route for the year ending February 2013, 5% of passengers travelled for business purposes between Brisbane and New Zealand and 40% for leisure.[139]

Table D.22 – Airline share (%) of total capacity, seats flown for DUD-BNE, year to February

Airline	2011	2012	2013
Air New Zealand	17.4	16.2	0
Virgin Australia	82.6	83.8	100
Total (%)	100.0	100.0	100.0
Seats ('000)	77.7	76.2	79.1

[139] See definition of purpose of travel categories in footnote 82.

569. The Brisbane - Dunedin route was a route of concern in the ACCC's consideration of the Alliance in 2010. The ACCC considered that it was unclear whether the level of capacity on the route provided an incentive for a new entrant, such as Jetstar, if Virgin Australia and Air New Zealand raised fares or reduced capacity. It concluded that given the limited competitive constraint faced by the Applicants on the this route, Virgin Australia and Air New Zealand had the incentive and ability to raise fares, reduce capacity or otherwise reduce their service offering.

570. Since the implementation of the Alliance, Air New Zealand has ceased operating services on all three Dunedin routes, with the Alliance instead increasing the frequencies offered by Virgin Australia. The Applicants have indicated this is a result of scheduling optimisation under the Alliance.

571. Following the draft determination, the Applicants submit that in light of the fact that the Dunedin-Melbourne route has always been a single operator route, the Alliance will not result in any competitive detriment on this route. Further, the Applicants note that over the years, three different carriers have operated these routes as sole operators and all have struggled to make them viable, despite the absence of any competitor. At present, the Alliance only operates services on this route in the months of December and January, which are typically the peak travel months of the year, and during this period the Alliance only operates two services per week.

572. The Applicants further submit that capacity conditions would prevent them from shifting capacity away from marginal routes or increasing capacity on better performing routes if demand continues to worsen or if this capacity can better be deployed elsewhere.

573. Further, following the draft determination, the Applicants also submit that on the Dunedin - Sydney route, which comprises less than 1% of trans-Tasman traffic, there is no evidence to suggest that the Alliance has had an anti-competitive effect. Further, they submit that similar competitive conditions exist on this route, as on the Dunedin-Melbourne route which makes it unlikely that there would be an increase in the Applicants' incentives or ability to unilaterally raise price or reduce service in the future.[140]

574. Following the draft determination and in response to consultation on the Applicants' proposal for the capacity condition, DIAL submits that the ACCC should maintain the capacity condition it proposed in the draft determination. DIAL is not in favour of the Applicants' proposal and specifically considers it important that the condition covers Dunedin-Sydney and Dunedin-Melbourne.

575. While the ACCC acknowledges the thinness, and in some instances the seasonal nature, of the Dunedin routes, it considers that the Applicants face limited competitive constraints on these routes. Absent the Alliance, the ACCC considers that there is little likelihood of entry by another operator given the thinness of the Dunedin-Sydney/Melbourne routes. It is unlikely that more than one airline would operate on these routes at any given time. However, the ACCC notes that Air New Zealand also operated on the Dunedin-Brisbane route prior to the Alliance and that, absent the Alliance, Air New Zealand may consider re-entering the Dunedin-Brisbane route. For this reason the ACCC considers that the Alliance is likely to result in detriment on the Dunedin-Brisbane route. The ACCC considers that the Alliance is likely to have the incentive and ability to raise fares, reduce capacity or

[140] Virgin Australia & Air New Zealand, Submission in response to the draft determination, 24 July 2013.

otherwise reduce their service offering on the Dunedin-Brisbane route, and it is not clear that the Alliance would face competition from entry by Jetstar or Qantas. However, on the Dunedin-Sydney/Melbourne routes, the ACCC considers that in light of the size of these routes and the fact that historically they have been monopoly routes, the Alliance is unlikely to change the level of competition on these two routes.

576. Air New Zealand is the only carrier which operates on the Auckland – Adelaide/Perth/Sunshine Coast routes and the Rotarua – Sydney route. The ACCC has considered in relation to these routes whether absent the Alliance, Virgin Australia might have entered the routes offering competition to Air New Zealand. Taking into account Air New Zealand's strong position of incumbency and its ability and incentive to compete aggressively to maximise passenger traffic to New Zealand, combined with the thinness of a number of these routes, and Virgin Australia's submissions relating to its strategies absent the Alliance, the ACCC considers it unlikely that Virgin Australia would enter these routes absent the Alliance. On this basis they are not considered further in this determination.

577. Since the ACCC examined the Alliance in 2010, Virgin Australia has ceased operating on the Hamilton – Sydney/Brisbane routes, leaving no airline operating services to Hamilton. Virgin Australia exited these routes in August 2010 and October 2012 respectively, citing lack of demand for the services. Given the thinness of the routes, Virgin's inability to continue operating and the apparent long term lack of interest by Air New Zealand, it is unclear whether any airline would commence services on these routes, with or without the Alliance. On this basis the ACCC does not consider that Alliance will have any effect on competition for services to Hamilton, and these routes are not considered further in this determination.

Conclusion on public detriments in relation to trans-Tasman air passenger transport services

578. The Alliance would result in a combined Virgin Australia-Air New Zealand market share of around 50.8% of the seats flown between Australia and New Zealand, based on BITRE data for the 12 months ending February 2013.

579. The ACCC has assessed the public detriments that arise or are likely to arise as a result of the Alliance having regard to the two forms of competitive harm that the Alliance could result in: unilateral and coordinated effects.

580. In relation to unilateral effects, taking into account the current market conditions and the Applicants' submissions on the counterfactual, the ACCC considers that, absent the Alliance, Virgin Australia's schedule and network offering on the trans-Tasman is likely to reflect a more limited competitive offering, particularly on the business orientated routes which Virgin Australia has indicated are most likely to be negatively impacted absent the Alliance.

581. Therefore while the Alliance has the result of reducing the number of Australian and New Zealand designated airlines from three to two on the Auckland and Wellington routes, the ACCC considers that the Alliance is unlikely to have a significant impact on competition on most of these routes (with the exception of Wellington-Brisbane). In reaching this view, the ACCC has had regard to Virgin Australia's submission that its stand alone offering in the likely future without the

Alliance is unlikely to be as strong as the offerings of Air New Zealand and the Qantas Group on these routes, which have a high proportion of business travellers.

582. On a number of the minor routes, for example Christchurch-Gold Coast, Queenstown-Melbourne, Auckland-Cairns and Auckland Perth, the ACCC considers Virgin Australia is unlikely to continue to compete or enter these routes absent the Alliance. On the other routes, the ACCC considers that, absent the Alliance, Virgin Australia is likely to continue to operate services. On these routes the ACCC has identified that the Applicants may have an increased incentive and ability to raise prices or reduce levels of service. On a number of these routes the ACCC considers that the limited market share of the Alliance, combined with the constraining effect of the presence of the Qantas Group on the route, or the thin nature of the route, will mean that the competitive detriment as a result of competition lost by the creation of the Alliance is likely to be minimal.

583. On the remaining routes, the ACCC considers that the significant market share of the Alliance and/or little or no presence by the Qantas Group, means that it is likely that the Applicants will have an increased ability and incentive to unilaterally reduce Alliance capacity on these routes to make seats more scarce, which in turn is likely to result in higher fares as compared to the future without the Alliance in which the Alliance partners would likely compete with each other. The ACCC considers that the routes on which this concern arises are:

- Christchurch-Melbourne
- Christchurch-Brisbane
- Wellington-Brisbane
- Queenstown-Brisbane
- Auckland-Gold Coast
- Dunedin-Brisbane.

584. The ACCC is of the view that the Alliance is likely to result in significant anti-competitive detriment on the six routes identified above However, the ACCC considers that the overall magnitude of harm from the Alliance unilaterally decreasing capacity or increasing fares on those routes, having regard to their size, is likely to be small relative to the trans-Tasman as a whole.

585. In respect of coordinated effects, the ACCC considers that there are a number of factors (including predominantly the small number of airlines operating on the relevant routes) that suggest there is a risk of coordinated behaviour on the trans-Tasman. Specifically, the ACCC notes that with the Alliance in place, there are only two major independently determined price/service offerings on the trans-Tasman of similar size (that is, Virgin Australia/Air New Zealand and Qantas-Group/Emirates). Absent the Alliance, Virgin Australia would be a smaller third player with potentially divergent incentives which might disrupt coordination.

586. The ACCC considers that the Alliance may increase the risk of coordinated conduct on trans-Tasman routes and that this results in public detriment. However, the extent to which coordination is likely to result is unclear. Accordingly, the ACCC intends to closely monitor the Alliance and the conduct of the airlines

operating on the trans-Tasman over the period of the proposed conduct to assess whether coordination is likely to be occurring.

587. Accordingly, the ACCC is imposing an information reporting condition under clause 3 of the condition of authorisation to assist it in assessing coordinated and unilateral effects during the term of the authorisation.

Australian domestic air passenger transport services

588. The ACCC has previously recognised that an international aviation alliance could affect competition in the market for domestic air passenger transport services in Australia by directing domestic on-carriage or feeder traffic to a particular carrier, at the expense of the competitive position of other domestic carriers.[141]

589. The Alliance is likely to impact the Australian domestic market through domestic on-carriage traffic from Air New Zealand being directed to Virgin Australia, giving Virgin Australia greater access to the passengers arriving in Australia on Air New Zealand flights.

590. The Applicants submit that domestic networks are outside of the scope of the Alliance except to the extent that a particular service is part of a connecting service across the trans-Tasman. In this regard, the ACCC notes that the volume of passengers that would constitute feeder traffic for Virgin Australia would therefore be limited to those passengers travelling as part of an Alliance connecting flight.

591. The ACCC also notes that passengers may opt to purchase the domestic leg of their journey separately and further that most demand on trans-Tasman routes can be accommodated on direct services.

592. The ACCC considers that feeder traffic from Air New Zealand's trans-Tasman flights being directed to Virgin Australia is likely to result in minimal, if any, public detriment in the domestic air passenger transport services market because of the relatively small volume and because of the dominant position of Qantas in the domestic Australian market.

ACCC conclusion on public detriment

593. In relation to unilateral effects, taking into account the current market conditions and the Applicants' submissions on the counterfactual, the ACCC considers that, absent the Alliance, Virgin Australia's schedule and network offering on the trans-Tasman is likely to reflect a more limited competitive offering, particularly on the business orientated routes which Virgin Australia has indicated are most likely to be negatively impacted absent the Alliance.

594. The ACCC is of the view that the Alliance is unlikely to have a significantly increased ability or incentive to unilaterally reduce or limit capacity (in order to raise airfares) on the majority of trans-Tasman routes, including a number of the largest

[141] ACCC, Determination for applications A91267 and A91268 lodged by Virgin Australia and Singapore Airlines (2011).

routes (Auckland-Sydney, Auckland-Melbourne, Auckland-Brisbane, Christchurch-Sydney, Wellington-Sydney and Wellington-Melbourne).

595. The ACCC considers that the Alliance is likely to result in public detriment through its effect on competition on a number of routes comprising the market for trans-Tasman air passenger transport services. The ACCC is of the view that the Alliance is likely to result in public detriment on the following trans-Tasman routes (which together account for approximately 16% of the trans-Tasman air passenger services market):

- Christchurch-Melbourne
- Christchurch-Brisbane
- Wellington-Brisbane
- Queenstown-Brisbane
- Auckland-Gold Coast
- Dunedin-Brisbane.

596. The ACCC considers that the Alliance creates a market structure on the trans-Tasman that increases the risk of coordination by Qantas-Group/Emirates and the Applicants. Absent the Alliance, the ACCC considers that Virgin Australia would be a third and smaller operator on the trans-Tasman, with potentially divergent incentives that could disrupt coordination. Through removing Virgin Australia as an independent competitor on the trans-Tasman, the ACCC considers that the Alliance has increased the risk of coordination, which results in public detriment. However, the extent of the public detriment arising as a result of an increased risk of coordinated conduct is uncertain. Given the significant anticompetitive detriment that can result as a consequence of coordinated conduct, the ACCC intends to closely monitor the Alliance to assess whether coordination is occurring.

Balance of public benefit and detriment

597. In general, the ACCC may grant authorisation if it is satisfied that, in all the circumstances, the proposed conduct is likely to result in a public benefit, and that public benefit will outweigh any likely public detriment, including any lessening of competition.

598. In the context of applying the net public benefit test in subsection 90(8)[142] of the Act, the Tribunal commented that:

> … something more than a negligible benefit is required before the power to grant authorisation can be exercised.[143]

599. The ACCC considers that the Alliance would, or would be likely to, result in:

[142] The test at subsection 90(8) of the Act is in essence that conduct is likely to result in such a benefit to the public that it should be allowed to take place.

[143] *Re Application by Michael Jools, President of the NSW Taxi Drivers Association* [2006] ACompT 5 at paragraph 22.

- material public benefits in the form of enhanced products and services. These products and services are comprised of loyalty program benefits, lounge access, and new frequencies (each of which the ACCC considers will be material benefits going forward) and increased online connections and better schedule spread (which the ACCC considers will result in small public benefits going forward). Increased access to existing frequencies may also form a public benefit, however based on the evidence available, the ACCC cannot conclude the magnitude of this benefit;

- material public benefits in the form of the promotion of competition on trans-Tasman routes, particularly in relation to the business traveller segment. The ACCC considers that this benefit is likely to manifest in a competitive response from the Qantas Group to the improvement in products and services of the Applicants on these routes. To a lesser extent the ACCC considers that the Alliance is likely to result in similar benefits in the domestic Australian market, but is unable to determine the extent to which the Alliance contributes to the increased competitiveness of Virgin Australia;

- small public benefits in the form of cost savings and efficiencies. These small benefits are likely to be derived from joint procurement, co-location of certain functions, utilisation of common resources and the removal of double marginalisation. The ACCC also considers that operational optimisation and high load factors may deliver efficiencies for the Alliance. However, based on the evidence available, the ACCC cannot conclude that high load factors are a likely benefit of the Alliance; and is unable to reach a conclusion on the magnitude of the benefit resulting from operational optimisation; and

- small public benefits in the form of stimulating tourism spend in Australia.

600. The ACCC is of the view that the Alliance is unlikely to have an increased ability or incentive to unilaterally reduce or limit capacity (in order to raise airfares) on the majority of trans-Tasman routes, including a number of the largest routes (Auckland-Sydney, Auckland-Melbourne, Auckland-Brisbane, Christchurch-Sydney, Wellington-Sydney and Wellington-Melbourne).

601. However, the ACCC considers that the Alliance is likely to result in public detriments by giving the airlines an increased ability and incentive to unilaterally reduce or limit capacity (in order to raise airfares) on the routes between:

- Christchurch-Melbourne
- Christchurch-Brisbane
- Wellington-Brisbane
- Queenstown-Brisbane
- Auckland-Gold Coast
- Dunedin-Brisbane

602. (which together account for around 16% of capacity on the trans-Tasman). The ACCC is imposing a condition in respect of these routes. Additionally, the ACCC notes that with the Alliance in place, there are only two major independently determined price/service offerings on the trans-Tasman (that is, Virgin Australia/Air New Zealand and Qantas-Group/Emirates). The ACCC is concerned that, compared to a likely future without the Alliance, there may be increased risk of coordinated conduct on the trans-Tasman, resulting in public detriment.

603. After weighing the public benefits and detriments discussed above, the ACCC has reached the view that the Alliance, subject to the conditions discussed in more detail below, is likely to result in material public benefits and that these benefits would outweigh the detriment to the public constituted by any lessening of competition that would result or would be likely to result from the proposed conduct.

604. The ACCC notes that, as was the case in the 2010 determination, the public benefits and public detriments likely to result from the Alliance are finely balanced.

Conditions of authorisation

605. As discussed under **Public detriments**, the ACCC is concerned that the Alliance will increase the ability and incentive of Virgin Australia and Air New Zealand to unilaterally reduce or limit growth in capacity on certain overlapping trans-Tasman routes in order to raise airfares compared to the likely future absent the Alliance, in which the Alliance partners would likely compete strongly. The ACCC is of the view that there are not sufficient competitive constraints on the Alliance to prevent such an outcome.

606. The 2010 authorisation was conditional on the Applicants maintaining a base level of capacity, subject to a growth factor, on the (then) routes of concern for the term of the authorisation. The growth factor required the Applicants to grow capacity seasonally on each of the routes of concern in line with most recent economic growth (GDP) or growth in trans-Tasman passenger demand (i.e. total passenger numbers measured by BITRE) (whichever is greater) for the term of the authorisation.

607. The routes of concern identified in 2010 were:

- Wellington – Sydney
- Wellington – Melbourne
- Wellington – Brisbane
- Dunedin – Brisbane
- Auckland – Brisbane
- Queenstown – Sydney

608. The 2010 authorisation was also conditional on the Applicants' maintaining a base level of capacity, subject to a growth factor, overall on the trans-Tasman.

609. To date, the Applicants have complied with the conditions of authorisation which have now been in place for four scheduling seasons (two years).

Submissions before the draft determination

Applicants' submissions

610. The Applicants submit that the experience to date supports their submission that there is unlikely to be any adverse competitive effects on any trans-Tasman route. In support of this the Applicants note that on each of the condition routes, there has been a reduction in the combined Alliance average fare (with the exception of the Sydney-Wellington route). The Applicants also cite a number of changes on the trans-Tasman which they view as having made the market more competitive:

- China Airlines have commenced services on Auckland-Brisbane and there is potential for further FFC entry on this and other trans-Tasman routes;

- total and competitor capacity on Auckland-Brisbane has increased substantially between the Pre-Alliance Year and Year 1;

- Auckland-Coolangatta is a substitutable route should the Applicants increase prices or decrease capacity on Auckland-Brisbane;

- Jetstar has demonstrated its ability to move quickly to deploy capacity in response to market opportunities. In the one year period from the Pre-Alliance Year to Year 0, Jetstar increased capacity by 16.7%. As a result, any anti-competitive behaviour by the Alliance would only encourage Jetstar's entry and expansion;

- Jetstar has commenced services on Queenstown-Sydney since the Final Determination; and

- Jetstar also boosted flights from Australia to Queenstown including Queenstown-Sydney when it increased its New Zealand based fleet from 8 to 9 Airbus 320 aircraft from 15 November 2012.

611. The Applicants also submit that the conditions are costly to both the Applicants and consumers. In this regard the Applicants note:

- the external audit services to monitor compliance with the conditions are costly;

- the conditions effectively set an output floor for the Alliance on the trans-Tasman as a whole and on an escalating basis for particular routes. As such, the Applicants are concerned that the conditions have the potential to create significant distortions and inefficiencies in the provision of trans-Tasman air passenger services which may not only result in compliance costs for the Applicants but in fact be to the detriment of consumers;

- the conditions reduce the ability of the Applicants to respond flexibly to adjust supply (i.e. capacity) to demand because the conditions artificially allocate capacity on the basis of a rigid formula that was determined in December 2010. This rigidity and artificial distortion to the dynamic air passenger services market comes at a cost;

- that during the short operation of the Alliance, the Applicants have had to apply to the ACCC and the New Zealand Ministry of Transport three times for variation to the conditions in response to exceptional circumstances and that considerable management time and external legal fees were also required to prepare and submit these requests for variation, and no doubt significant cost and resources were also invested by the ACCC and the New Zealand Ministry of Transport to consider and promptly respond to these requests;

- there have been several other examples of market distortions caused by the application of the conditions. For instance, during the NS11 season the Applicants experienced a higher level of operational (e.g. weather, engineering) cancellations than expected on the Brisbane-Wellington and Sydney-Wellington routes. As a consequence, the Applicants were obliged to add last minute capacity on these sectors to meet the conditions. While the Applicants did everything possible to ensure the additional capacity was added at attractive timings for the public, the last minute nature of this capacity meant that the flights were added at times when additional capacity was not needed. The short lead time meant the flights took off with low seat factors. When combined with lower than average fare levels the revenue for these flights was insufficient to cover costs;

- the conditions also constrain the Applicants' ability to make efficient fleet and network planning decisions;

- furthermore, the conditions could also have the unintended consequence of making entry or expansion more difficult. The trans-Tasman air passenger services market is characterised by a history of substantial capacity relative to passenger numbers. Under the conditions, the Alliance cannot reduce its capacity (and must grow capacity over time) regardless of whether there is excess capacity on condition routes. This regulated capacity is likely to discourage new entrants and make new entry more difficult. The ACCC acknowledged this in the Qantas/ Emirates determination. The Applicants submit that this distortion is exacerbated by the conditions in the Qantas-Emirates alliance which combined with the Virgin/Air New Zealand Alliance has the potential to result in capacity conditions on 95% of trans-Tasman routes; and

- further distortive effects are likely to be caused by competitor and supplier knowledge of the Applicants' obligation to operate according to a rigid, formula-driven, capacity floor per scheduling season. Specifically, the conditions will influence the capacity deployment and pricing decisions of competitors as well as negotiations surrounding supplier charges (e.g., airport aeronautical charges). The conditions create an environment where suppliers including airports can raise prices, knowing that the relevant airlines are unable to adjust capacity.

612. The Applicants submit that the conditions are not needed to satisfy the net public benefits test. The Applicants submit in support of this:

- short term or initial capacity conditions may be justifiable in cases which are finely balanced. However, the Alliance has clearly demonstrated that it has resulted in net public benefits and as discussed above, reauthorisation will result in further and deeper benefits from the Alliance without any material public detriment, including on any individual route. It cannot be considered that the public benefits and detriments from the Alliance are finely balanced. It is submitted that the Alliance experience of the past two years should address any concerns which existed at the time of the initial authorisation; and

- the core rationale of the Alliance is to stimulate passengers on Alliance services. It has been structured in a way to incentivise capacity growth, not capacity reduction, and the Alliance has triggered significant increases in passenger numbers on Alliance services through its enhanced product offering. The combined Alliance average fares have decreased and there has been no anti-competitive reduction in capacity on any trans-Tasman route. In particular, the competitive dynamics on the condition routes are such as to remove any need for the conditions.

Interested party submissions

613. A number of interested parties have made submissions regarding the conditions of authorisation. These are outlined below.

614. Emirates shares some of the concerns voiced by Virgin Australia on the potential distortions and costs associated with capacity conditions and does not oppose authorisation if it was subject to the same regulatory conditions imposed on Emirates and Qantas.

615. Emirates submits that for the following reasons, it is appropriate that authorisation be subject to conditions :

- similar competition dynamics - the Alliance has the leading market position on the trans-Tasman and in terms of market dynamics, if the ACCC when considering the Emirates and Qantas alliance was not comfortable that Virgin Australia and Air New Zealand could competitively constrain the Qantas and Emirates partnership, it is not clear, in the absence of similar capacity conditions, that Qantas or Emirates (as a FFC), would constrain the larger Alliance;

- similar conditions avoid the creation of market distortions - the ACCC has imposed regulatory conditions on Emirates and Qantas in relation to capacity and growth in the ACCC's determination in relation to the Qantas-Group/Emirates alliance to seek to safeguard the ACCC's perceptions in relation to the impact of the partnership on capacity and capacity growth and therefore competition dynamics. Emirates submits it would create regulatory distortions if the Alliance was not subject to the same regulatory conditions; and

- similar concepts of flexibility to promote innovation - Emirates submits that the Alliance should be subject to the same flexibility that the ACCC has sought to provide Qantas and Emirates in terms of new routes or other dynamic factors, but also the conditions should have the same audit and compliance processes to safeguard the competitive process as part of any conditions imposed by the ACCC.

616. Qantas submits that conditions requiring the maintenance of minimum capacity levels can produce unintended consumer detriments through operational inefficiencies and costs. However, Qantas submits that the Applicants' assertion that the benefits of their alliance are 'not finely balanced' and that therefore they ought not be subject to an ongoing condition requiring the maintenance of minimum levels of capacity is fanciful and unsupported in circumstances where the degree of overlap between carriers is much greater than that involved in the Qantas-Emirates partnership and the alliance involves the carriers having monopoly operations on several routes including Brisbane-Dunedin, Brisbane-Wellington, Adelaide-Auckland and until recently Perth-Auckland. In contrast, the Qantas-Emirates partnership does not result in Qantas, Jetstar or Emirates being the sole operator on any route.

617. DIAL submits that the conditions imposed on a renewed alliance agreement should be those which are imposed under the current authorisation. However, it may be appropriate to remove or add conditions where the current market and

operating environment has materially varied from that on which the original conditions were based. DIAL submits that:

- on the Brisbane – Dunedin route, market and operating conditions remain largely unchanged to those which existed at the time when the current authorisation was approved. DIAL submits that to ensure that the market continues to be serviced with capacity, frequency and competitive fares the specified capacity conditions for this route must continue;

- the Sydney and Melbourne routes to and from Dunedin are not subject to specified capacity conditions but subject to the general and overall conditions. DIAL submits that since the commencement of the alliance these routes have been operated by the airlines on a seasonal basis. DIAL submits that this reduction of services has impacted negatively on the market with Dunedin passengers having no alternative but to use other New Zealand airports for their travel and thereby incurring additional time and cost; and

- to ensure that the market is not disadvantaged, that the Sydney and Melbourne to Dunedin routes be made subject to a specific capacity condition that ensures that the level of capacity and frequency is no less (but subject to the growth factor) than that at the commencement of the current alliance agreement.

618. CIAL originally submitted that given the material competition issues raised by the alliance, and the fine balance of benefits and detriments resulting from the alliance on the Christchurch routes, the Applicants should be required to grow seasonally on the Christchurch routes. CIAL also submitted that a trans-Tasman capacity condition is also necessary. CIAL submitted that:

- the current capacity operated by the Applicants is a floor in operational capacity, and that new and added capacity should continue on each of the sectors;

- that there is a very weak prospect of new entry on the Christchurch routes and that this means there is a strong risk of anti-competitive detriment occurring, and that the airlines will have sufficient market power to unilaterally increase airfares and/or reduce or withhold capacity;

- that Air New Zealand's share of traffic on the Christchurch routes has been concentrating over time and that Air New Zealand has a position of dominance on the Christchurch routes;

- that the inflexibility and costs associated with capacity conditions is a necessary consequence of the fact that the airlines are being allowed to collude. CIAL submits that the variation regime has worked very effectively over the course of the alliance and that the time and cost involved in making applications should not be overstated; and

- that almost none of the public benefits have been realised on the Christchurch routes and that the conditions are necessary to satisfy the public benefit test.

619. CIAL made a supplementary submission indicating that in light of further confidential information provide to it by Air New Zealand its concerns had been lessened.

620. KWSG submits that any reauthorisation must be subject to conditions. KWSG submits that:

- the Applicants' arguments about lack of competitive detriments do not apply to the Wellington routes. In this regard KWSG submits that there are no (and it cannot reasonably be expected in future that there will be any) FFC operating at Wellington airport;

- there has been no particular change in market conditions on the Wellington trans-Tasman routes that leads to any different conclusion when considering the competitive state of those markets today. Competition remains limited on all three Wellington trans-Tasman routes and the prospect of new entry remains as limited as it was three years ago; and

- the conditions are essential to satisfy the net public benefits test. KWSG submits that its common concern is to maintain and increase the growing number of passengers coming into Wellington from Australia. In the decade before the Alliance between Virgin Australia and Air New Zealand was authorised, growth on the Wellington trans-Tasman routes was 44%, and it stemmed almost exclusively from the presence of a third operator, Pacific Blue, to challenge the Air New Zealand-Qantas duopoly. That competition brought increased capacity on Wellington trans-Tasman routes and lower average fares on these routes for consumers. Authorisation of the Alliance effectively removed the third operator from the Wellington trans-Tasman routes. In the absence of the competitive dynamics and forces that would otherwise be at play, some mechanism was essential to ensure that the competitive outcomes that would otherwise obtain on these routes were obtained. That mechanism was the imposition and enforcement of the conditions to the alliance authorisation. By requiring the Applicants to maintain and grow capacity in a situation of substantially reduced competition, the ACCC (rightly) has created a proxy mechanism for producing the competitive outcomes that would otherwise obtain if the trans-Tasman market were left to competition.

621. KWSG submits that the conditions should:

- preserve the base level capacity condition on the Wellington routes;

- keep the requirement to grow capacity in line with an appropriate measure of market growth;

- last for no more than three years; and

- the nature of the conditions should be the same as those currently in place.

622. The NZ Airports submit that:

- there is no reason to move away from appropriate conditions, and that the capacity conditions are not a particularly difficult target to reach in terms of capacity growth;
- prior to the authorisation of the alliance, the competitive market produced rates of growth far greater than those required by the capacity condition;
- the conditions protect the market from the commercial incentives facing the alliance partners by ensuring that a minimum level of capacity growth is maintained;
- given the clear link between capacity and price, this activity would have the effect of increasing air fares and suppressing demand from the price sensitive majority of trans-Tasman travellers;
- whilst some flexibility may be appropriate in such conditions, NZ Airports remains firmly opposed to the removal of the conditions protecting vulnerable routes; and
- where an argument could potentially be made that average air fares have reduced on some routes over the course of the Alliance, when considered alongside a substantial increase in ancillary revenue collected for services such as seat selection, on board entertainment and the ability to check-in baggage, the reality may be that the price faced by consumers to travel has not in fact reduced.

Submissions after the draft determination

623. Following the draft determination the Applicants made the following submissions in relation to the proposed capacity condition:[144]

- they agree with the removal of conditions on Wellington-Melbourne and Wellington-Sydney routes as compared to the 2010 authorisation.
- market dynamics do not support the application of conditions on the following routes:

    i. Dunedin – Melbourne/Sydney: are thin seasonal routes which have always been served by one carrier. It is extremely unlikely that both Virgin Australia and Air New Zealand would compete on these routes.

    ii. Auckland – Gold Coast: a highly competitive route and largely a leisure/VFR route. The route is particularly suited to the budget travel product of Jetstar, which acts as a major competitive constraint with 37% market share.

    iii. Christchurch – Melbourne: is also a highly competitive route and Jetstar again acts as a major competitive constraint with 37%

[144] Virgin Australia & Air New Zealand, Submission in response to draft determination, 24 July 2013.

market share. FFC entry/re-entry is likely once Christchurch recovers from the 2011 earthquake.

- if the ACCC is minded to impose capacity conditions on the routes above, these routes should also be included in a grouping such that there are no route specific conditions, and instead:

  i. the Brisbane – Queenstown/Dunedin/Christchurch routes should be grouped together in terms of applying conditions, as they are often used interchangeably by customers and are complimentary, operating on a seasonal basis. Further, all three routes compete for the same aircraft time, therefore grouping will allow the Applicants to interchange services as necessary and spread additional frequencies between the markets depending on seasonal demand.

  ii. the Brisbane – Wellington route should be grouped together with the South Island grouping above, with a zero growth factor. This would mitigate the route specific effects recognised by the ACCC.

- the new capacity conditions should commence from the start of Northern Summer 2014 (April). Commencing the capacity conditions earlier would have a material negative impact on the Applicants and consumers. Capacity for NW13 has already been planned and slots confirmed.

- The Applicants contend that any initial growth factor should be set at 0%:

  i. the ongoing reporting obligations permit the ACCC to monitor capacity and properly consider the actual capacity decisions in light of relevant market circumstances prevailing over the period of the authorisation, particularly where there is already substantial capacity in the market

  ii. applying capacity conditions with a capacity floor, as opposed to a growth factor, will enable the ACCC to assess the true Alliance impact as opposed to the impact created by the growth factor

  iii. adding extra capacity on a number of the proposed capacity condition routes would effectively add capacity that is out of line with passenger demand, and result in the Alliance being forced to redirect capacity away from other, better performing routes where the addition of capacity is required to meet demand.

- The capacity growth factor calculation, excluding “negative quarterly changes in Australia’s Trend Chain Volume GDP” would result in the Applicants being required to grow capacity ahead of GDP.

624. Four interested parties also commented on the capacity condition following the draft determination:

- RIA submits that the capacity conditions are not required as incentives and market dynamics already exist to ensure that fares are kept reasonable and capacity is added where required.[145]

- DIAL submits that the capacity conditions proposed in the draft determination are appropriate. It objects to the proposed bundling option put forward by the Applicants in response to the draft determination, that is, the bundling of the Dunedin-Brisbane route with the other Brisbane port routes. In its view this is likely to lead to increased detriment for passengers travelling between Dunedin and Australia as the Applicants will be able to move capacity away from Dunedin to another New Zealand port that was part of the proposed bundle.[146]

- QAC submits that it may be more appropriate to impose total capacity conditions in and out of Brisbane to the South Island, namely the Christchurch, Dunedin, Queenstown – Brisbane routes.[147] QAC also submits that a growth factor should apply from the first year and agrees with the Applicant's proposed bundling of the Brisbane – South island routes.

- KWSG supports the capacity conditions to be imposed on the Wellington – Brisbane route, although remains of the view that the proposed authorisation without capacity conditions on the Wellington – Sydney and Wellington – Melbourne routes may substantially lessen competition over the trans-Tasman.[148]

ACCC view

<u>Changes to routes of concern as compared to the 2010 determination</u>

625. In the 2010 determination, the ACCC concluded that the Alliance was likely to result in competitive detriments on the Wellington – Sydney/Melbourne/Brisbane routes and the Dunedin – Brisbane route. The ACCC also concluded that the competitive effect on the Queenstown – Sydney and Auckland – Brisbane route was uncertain. To limit any potential competitive harm from the Alliance the ACCC imposed a capacity condition on all six routes. The ACCC also imposed capacity condition to cover total Alliance capacity across the entire trans-Tasman.

626. As discussed in the **public detriments** section above, since the 2010 authorisation there have been a number of changes to the trans-Tasman market which have impacted the routes on which the ACCC considers detriments are likely to arise going forward. These include:

- the Qantas Group-Emirates alliance which was authorised, subject to conditions, by the ACCC on 27 March 2013 and came into effect on 18 April 2013;

[145] Rotorua International Airport, Submission in response to draft determination, 19 July 2013.
[146] Dunedin International Airport Ltd, Submission in response to draft determination, 23 July 2013.
[147] Queenstown Airport, Submission in response to draft determination, 24 July 2013.
[148] Key Wellington Stakeholders Group, Submission in response to draft determination, 24 July 2013.

- Virgin Australia implementing its game-change strategy which has resulted in it shifting away from being a low cost carrier, and focusing on attracting a broader range of customers including higher yielding business passengers;

- China Airlines commencing services on the Sydney – Auckland and Brisbane – Auckland routes;

- Jetstar commencing services between Sydney and Queenstown, between Auckland and Cairns and between Melbourne and Queenstown; and

- Jetstar ceasing services between Brisbane and Christchurch.

627. The ACCC remains of the view that the Alliance would face little or no competitive constraint and is therefore likely to result in competitive detriments on the Wellington – Brisbane and Dunedin – Brisbane routes, having regard to the likelihood that the Applicants would compete or potentially compete on these routes absent the Alliance, and for that reason is retaining a capacity condition on these routes.

628. In contrast to the view it reached in 2010, the ACCC considers that the Alliance is unlikely to result in significant unilateral competitive detriments on the Wellington-Sydney route when compared to the likely future without the Alliance. In reaching this view, the ACCC has had regard to Virgin Australia's incentives in relation to likely re-entry and specifically the likelihood of it being able to strongly compete for corporate and government accounts on this route absent the Alliance.

629. In relation to Wellington-Melbourne, the ACCC considers that, absent the Alliance, Virgin Australia is unlikely to enter. This view contrasts with the ACCC's 2010 view and is based on the likely future without the Alliance that would see Virgin Australia review its schedule and capacity on the trans-Tasman. The Wellington-Melbourne route has similar characteristics to the Wellington-Sydney route to the extent that both have strong demand by government and corporate passengers. The ACCC considers that Virgin Australia is likely to have a weaker service offering for corporate and business passengers on this route compared to Qantas and Air New Zealand and therefore considers that it will have a reduced incentive to enter absent the Alliance.

630. On the two routes which in 2010 the ACCC considered the competitive effects of the Alliance were uncertain (Auckland – Brisbane and Queenstown – Sydney), both have seen entry by additional carriers over the past two years. Having regard to the competitive dynamic moving forward, the ACCC now considers that it is unlikely significant detriments will arise on the Sydney – Queenstown route. Therefore the ACCC is removing the capacity condition from this route moving forward.

631. In relation to the Auckland – Brisbane route, the ACCC's view is that while there remains some uncertainty as to the competitive effect of the Alliance on this route, the additional confidential information provided by the Applicants after the draft determination has indicated that absent the Alliance Virgin Australia is unlikely to be as strong a competitive constraint against the other major airlines. The ACCC has also had regard to the Qantas-Group/Emirates alliance's recent capacity increase on this route and the presence of China Airlines. For these reasons, the

ACCC is not imposing a condition on the Auckland – Brisbane route going forward.

632. While changes in the market have reduced the ACCC's concerns in relation to some of the routes, the withdrawal of Jetstar on the Christchurch – Brisbane route has made it more likely that competitive detriments will arise on this route, and the ACCC is therefore adding a condition to this route.

633. In relation to the Christchurch – Melbourne route, the ACCC stated in 2010 that:

> Looking forward, the ACCC considers that Jetstar is likely to operate more like an independent LCC on this route and act as a competitive constraint on the Alliance.[149]

634. Given Virgin Australia's shift away from operating as a low cost carrier, the ACCC considers that Jetstar is likely to act as less of a constraint on the Alliance in the future (relative to the ACCC's assessment in 2010). The ACCC also notes the public statements from the Qantas-Group that it is unlikely to add capacity in the short term on the trans-Tasman. For these reasons the ACCC considers that competitive detriments are more likely to arise on this route, and it is therefore adding a capacity condition to this route.

635. When the ACCC considered the Alliance in 2010, the Queenstown – Brisbane route was only operated as a seasonal route with services offered by Qantas, Air New Zealand and Virgin Australia. Since this time, Air New Zealand and Virgin capacity share on the route has increased to 92.3%. As the ACCC is concerned that the route is too small to be commercially attractive for other airlines (including Jetstar) to enter, it considers that the Alliance is likely to increase the ability and incentives of the Applicants to unilaterally raise airfares on this route. For this reason, the ACCC is adding a condition to this route.

636. In relation to the Auckland-Gold Coast route, in 2010 the ACCC considered that:

> …Jetstar is likely to operate more like an independent LCC on this route and act as a competitive constraint on the Alliance.[150]

637. Similar to its assessment of the Christchurch-Melbourne route, the ACCC has had regard to the changing nature of Virgin Australia's product offering and considers that Jetstar is likely to operate as less of a constraint on the Alliance (relative to the ACCC's assessment in 2010). The ACCC also notes the public statements from the Qantas-Group that it is unlikely to add capacity in the short term on the trans-Tasman. The ACCC considers that competitive detriments are likely to arise on the Auckland-Gold Coast route and therefore it is adding a condition to the route.

638. In contrast to the capacity condition imposed on the 2010 alliance, the ACCC does not consider a trans-Tasman wide condition is necessary to address the identified public detriment. As discussed further below, the ACCC considers that the trans-Tasman wide condition will do little to limit the competitive detriments likely to result from the Alliance.

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[149] 2010 authorisation, p.74 at [5.309].

[150] 2010 authorisation, p.88 at [5.416].

639. In summary, the ACCC considers that it is likely that the Alliance will result in detriments on the following routes, and therefore has made them subject to a capacity condition:

i. Christchurch – Brisbane;

ii. Christchurch – Melbourne;

iii. Wellington – Brisbane;

iv. Queenstown – Brisbane;

v. Auckland – Gold Coast; and

vi. Dunedin – Brisbane.

640. In relation to the Dunedin – Sydney and Dunedin – Melbourne routes given the extremely thin nature of these routes and given that these routes are likely to remain monopoly routes, with or without the Alliance, the ACCC considers that the Alliance is unlikely to result in detriment on these routes. As a result, the ACCC is not imposing a capacity condition on these two routes.

Structure of capacity condition

641. The ACCC considers that a capacity commitment can, if appropriately set, limit the identified competitive harm on the trans-Tasman by removing the ability of the Alliance to unilaterally reduce or limit growth in capacity. On the other hand, the ACCC is conscious that a capacity commitment may have the effect of deterring entry onto the relevant routes or result in the inefficient allocation of capacity.

642. In the draft determination the ACCC contemplated three options for the structure of a capacity commitment in this matter:

(a) to cover the total capacity on all trans-Tasman routes;

(b) to cover the total capacity on the routes of concern; or

(c) to cover the individual capacity on each of the routes of concern.

643. The first of these options, covering total capacity on all trans-Tasman routes, has the benefit of providing the Applicants with the most amount of flexibility to respond to changing market circumstances. However, this option is also the weakest with respect to solving the likely competitive harm from the Alliance. In covering the total trans-Tasman, the capacity condition would apply to routes outside of the routes of concern, and cover the 84% of capacity on the trans-Tasman market that does not operate on the routes of concern. Including all trans-Tasman routes in the capacity undertaking is likely to provide Virgin Australia and Air New Zealand with greater scope to exercise market power on the routes of concern.

644. The second of these options provides the Applicants with flexibility to adjust capacity across the routes of concern to respond to changes in market conditions. This option would also directly target the routes of concern. However, the routes of concern vary in size from over 300,000 seats flown per year (Auckland – Gold Coast) to less than 80,000 seats flown per year (Brisbane – Dunedin). The routes

vary greatly in terms of growth rate - for example Brisbane – Queenstown has grown 18% in capacity over the past two years, while the Christchurch routes have decreased capacity significantly over the same period. The routes also vary by traveller type with the Queenstown route being predominately leisure orientated, and the Wellington route having more of a government and business focus.

645. The third option directly targets the routes of concern, and provides the most effective limit on the identified competitive harm. However it provides the Applicants with the least flexibility to move capacity in response to changes in market conditions.

646. In the draft determination, the ACCC proposed to combine the second and third options; that was to bundle the two Christchurch routes, and separately the three Dunedin routes together to provide a greater degree of flexibility to the Applicants.

647. For the remaining routes of concern, the ACCC proposed an individual capacity condition.

648. Having regard to the Applicants' submissions after the draft determination regarding the Dunedin – Melbourne/Sydney routes the ACCC now considers that bundling these routes with the Dunedin –Brisbane route will provide little additional flexibility for the Applicants. As the ACCC identified in the draft determination, due to the extremely thin nature of these routes, and that these routes are likely to remain monopoly routes, such that it is extremely unlikely that both Virgin Australia and Air New Zealand would compete on these routes, the public detriments arising from the Alliance are likely to be minimal. For these reasons, the Dunedin – Melbourne/Sydney routes are unlikely to warrant a standalone condition and the ACCC has removed these two routes from the capacity condition proposed in the draft determination.

649. As discussed above in the **Public Detriments** section, the ACCC remains of the view that, in addition to the Brisbane routes, competitive detriment is likely to arise from the Alliance on the Christchurch – Melbourne and Auckland – Gold Coast routes and has therefore maintained these as routes of concern for the purpose of the capacity condition.

650. The ACCC views the objective of the conditions as being to restrict the discretion of the Alliance to limit its capacity or limit the growth of its capacity on each of the trans-Tasman routes of concern. However, having regard to confidential information provided by the Applicants after the draft determination, the ACCC considers that the concerns identified by it in the draft determination that a capacity commitment may have the effect of deterring entry onto the relevant routes or result in the inefficient allocation of capacity have been confirmed.

651. Accordingly, the ACCC imposes conditions of authorisation which require the Applicants to maintain an aggregate base level of capacity across all six routes of concern in order to provide the Applicants with additional flexibility and mitigate some of the risk of the inefficient allocation of capacity. The ACCC's conditions of authorisation are set out at Attachment B.

652. The ACCC notes that the authorisation commences on 1 January 2014 which is two months after the commencement of the NW 2013 scheduling season and three months prior to the commencement of the NS 2014 scheduling season. Accordingly the ACCC has imposed on the Applicants a requirement to maintain

an aggregate base level of capacity for the transitional period of 1 January 2014 to 31 March 2014, as set out at Attachment B, which is equivalent to the level of capacity flown by the Applicant on the six routes of concern for the period of 1 January 2013 to 31 March 2013. The ACCC notes that as no growth factor will be imposed until after the review to be conducted from 1 September 2015, there should be no adverse impact for the Applicants or consumers of commencing the conditions prior to the Northern Summer scheduling season. Following the transitional period, the base level of capacity across the six routes of concern will be based on, and apply to, the NW and NS scheduling seasons.

653. As the commencement date of the authorisation, 1 January 2014, falls two months into the NW 2013 scheduling season, the Applicants' reporting obligations, as set out at Attachment B, will include the calendar months of November and December 2013, irrespective of these two calendar months pre-dating the period of authorisation, so that the Applicants report on the entirety of the NW 2013 scheduling season.

Growth Factor

654. The ACCC has also considered the appropriateness of including a requirement to increase capacity in accordance with a specified growth factor.

655. As underlying passenger demand grows over time, a capacity commitment that requires the Applicants to maintain current levels for the duration of the authorisation (five years is sought by the Applicants) would be likely to give the parties considerable latitude to limit growth in capacity and raise airfares by restricting capacity growth. This issue would be addressed by incorporating in the commitment an appropriate growth rate, preferably one that is exogenous to the parties.

656. On the other hand, the ACCC notes the Applicants' claims of excess capacity on the trans-Tasman. The ACCC previously considered in the Qantas-Group/Emirates determination that excess capacity may exist on the Auckland – Sydney/Melbourne/Brisbane routes and the Christchurch – Sydney route, and for that reason initially set the growth factor at 0% on these routes for a period of two years in granting conditional authorisation to Qantas and Emirates.

657. In the draft determination, the ACCC considered, based on the evidence available, that there was not excess capacity on the routes of concern. The ACCC therefore proposed that the growth factor be the greater of the sum of quarterly changes in Australia's real GDP, or zero.

658. The ACCC invited further submissions from the Applicants and interested parties as to whether there was excess capacity on the relevant routes between Australia and New Zealand.

659. As noted above, the Applicants contend that any initial growth factor should be set at 0% having regard to what they consider to be excess capacity on the routes of concern. The Applicants submit that adding extra capacity on the condition routes would effectively add capacity that is out of line with passenger demand, and result in the Alliance being forced to redirect capacity away from other, better performing routes where the addition of capacity is required to meet demand.

660. The ACCC does not accept that, absent the Alliance, there would not be growth in demand on the bundle of routes. The ACCC considers that on at least four of the

six routes subject to a condition that there is not excess capacity. As underlying demand grows, the ACCC expects to observe capacity additions by the Applicants on the routes of concern. However, the ACCC acknowledges that capacity additions are 'lumpy' in the sense that airlines add capacity by adding or upgrading aircraft which makes it difficult to add capacity in small increments. Rather than prescribe a minimum growth factor for the bundle, the ACCC considers it appropriate to review the Applicants' capacity additions in light of actual demand growth over the next two years. The ACCC will conduct a review at that time. The review will enable the ACCC to consider whether increases in the minimum required capacity are warranted. For this reason, the ACCC has chosen not to impose an initial growth factor on the routes of concern.

Information condition

661. The ACCC is also requiring the Applicants to provide information on key aspects of performance of the Alliance at the end of each scheduling season to assist the ACCC in assessing coordinated and unilateral effects going forward. The information requirement is set out at Clause 3 of the condition at Attachment B. Broadly it requires the Applicants to provide capacity, passenger, revenue, cost, fare schedule, and tactical fare data at the conclusion of each scheduling season.

662. The conditions also require the Applicants to provide additional information, documents and material to the ACCC in the time and form requested by the ACCC pursuant to or in relation to the conditions (clause 8).

Length of conditional authorisation

663. The Act allows the ACCC to grant authorisation for a limited period of time.[151] This allows the ACCC to be in a position to be satisfied that the likely public benefits will outweigh the detriment for the period of authorisation. It also enables the ACCC to review the authorisation, and the public benefits and detriments that have resulted, after an appropriate period.

664. In this instance, Applicants seek unconditional authorisation for five years. In the draft determination the ACCC proposed to grant authorisation, subject to conditions, for three years on the basis that it considered it appropriate to review developments on the trans-Tasman earlier than the requested five years due to the nature of the competition concerns identified.

665. The Applicants made further submissions regarding the length of authorisation following the draft determination, reiterating their request for authorisation for five years. In their submission, they seek commencement of the authorisation on 1 January 2014. The 2010 authorisation is due to expire on 31 December 2013 and the Applicants are required to continue reporting on the 2010 conditions of authorisation until the 2010 authorisation expires.

[151] Subsection 91(1).

666. The Applicants submit that a five year authorisation period will provide an increased level of certainty and confidence for the Applicants to continue to invest in key projects that will drive benefits from the Alliance.[152]

667. They further submit that there will be significant risks and costs associated with having a shorter authorisation term, including:

- removal of a viable competitive alternative to the Qantas-Group/Emirates alliance which was authorised by the ACCC for 5 years, potentially distorting market behaviour (for example, allowing the Qantas-Group/Emirates alliance to increase prices, or lower prices and exercise dominant anti-competitive behaviour).

- undermining the ability to achieve the benefits that could be derived from deeper integration between the Applicants over a longer period.

- undermining the ability and the incentive of the Applicants to further develop the Alliance, thereby further undermining the Applicants' competitive position against the Qantas/Emirates/Jetstar Alliance.

- higher costs to the Applicants if they have to unwind joint arrangements after only three years.

- there being limited data available to fully evaluate the benefits of the Alliance when the ACCC is required to consider a reauthorisation in 2-3 years.

668. Lastly, the Applicants submit that the conditions will provide a direct safeguard against competition concerns on those routes identified as potentially giving rise to a specific competition issue, and that if the ACCC has concerns with any trends showing in the data the Applicants are reporting to the ACCC, it has the ability to review the authorisation.[153]

669. A number of interested parties submitted that any authorisation should be limited to three years and be subject to capacity conditions. These interested parties indicate that the three year timeframe is necessary in order for the anticompetitive detriment of the Alliance to be mitigated.

670. As discussed above in the **conditions of authorisation** section, the ACCC considers it appropriate to review the Applicants' capacity additions in light of actual demand growth over the next two years. The review will enable the ACCC to consider whether increases in the minimum required capacity are warranted.

671. Taking into account the Applicant's additional submissions regarding the need for a five year term to allow for investment certainty and deeper integration of the Alliance partners, and in light of the review mechanism, the ACCC considers it appropriate to grant conditional authorisation until 31 October 2018. The ACCC considers that aligning the end date of authorisation with a scheduling season (31 October 2018) will assist in avoiding any future transitional timing issues if the Applicants seek re-authorisation of the Alliance when this authorisation expires.

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152 Virgin Australia & Air New Zealand, Submission in response to the draft determination, 24 July 2013.
153 Ibid.

Commencement date and transitional provisions for the capacity conditions

672. The ACCC considers that the authorisation should commence from 1 January 2014 as this date aligns with the expiry of the 2010 authorisation on 31 December 2013.

673. The ACCC notes that the capacity conditions both for the 2010 authorisation and the current authorisation apply over a scheduling season. The commencement of the current authorisation, that is 1 January 2014, does not align with the term of a scheduling season as the NW 2013 Scheduling Season covers the period from 1 November 2013 to 31 March 2014.

674. As discussed above, accordingly, the ACCC has imposed on the Applicants a base level of capacity for the transitional period of 1 January 2014 to 31 March 2014, as set out at Attachment B, which is equivalent to the level of capacity flown by the Applicant on the six routes of concern for the period of 1 January 2013 to 31 March 2013. Following the transitional period, the base level of capacity across the six routes of concern will be based on, and apply to, the NW and NS scheduling seasons.

End date of authorisation

675. The ACCC considers that the end date for the current authorisation should align with the end date for a scheduling season, on 31 October 2018. The ACCC considers that this will assist in avoiding any future transitional timing issues if the Applicants seek to re-authorise the Alliance when this authorisation expires.

Determination

The application

676. On 8 March 2013 Virgin Australia Airlines Pty Ltd, Virgin Australia Airlines (NZ) Ltd, Virgin Australia Airlines (SE Asia) Pty Ltd and Virgin Australia International Airlines Pty Ltd (together **Virgin Australia**) and Air New Zealand Limited (**Air New Zealand**) (together the **Applicants**) lodged applications for authorisation A91362 & A91363 with the ACCC.

677. The applications were lodged pursuant to subsections 88(1A) and 88(1) of the Act.

The net public benefit test

678. For the reasons outlined in this determination, and subject to the conditions below the ACCC considers that in all the circumstances the proposed conduct for which authorisation is sought is likely to result in material public benefit that would outweigh the detriment to the public constituted by any lessening of competition that would result or would be likely to result from the proposed conduct.

679. The ACCC therefore **grants** authorisation to applications A91362 and A91363 **on the conditions set out in Attachment B, including that the Applicants**:

- make available at least an aggregated base level of capacity across the following routes:

    i. Christchurch – Brisbane;

    ii. Christchurch – Melbourne;

    iii. Dunedin – Brisbane;

    iv. Wellington – Brisbane;

    v. Queenstown – Brisbane;

    vi. Auckland – Gold Coast;

- provide the data required under clause 3 of the condition to the ACCC at the end of each scheduling season.

680. The ACCC will commence a review on 1 September 2015 to determine whether to impose a growth factor on the routes of concern.

Conduct for which the ACCC grants conditional authorisation

681. Authorisation extends to Virgin Australia and Air New Zealand until 31 October 2018 to continue to:

- give effect to an Australasian Airline Alliance Agreement, an associated Code Share Agreement and related agreements contemplated by the Australasian Airline Alliance Agreement (collectively, the Alliance);

- make any related agreements which are contemplated by the Australasian Airline Alliance Agreement; and

- make agreements to the extent that those agreements give effect to the Australasian Airline Alliance Agreement.[154]

682. Authorisation is subject to conditions set out in Attachment B which require the airlines to:

- Make available at least an aggregated base level of capacity across the following routes:

    i. Christchurch – Brisbane;

    ii. Christchurch – Melbourne;

    iii. Dunedin – Brisbane;

    iv. Wellington – Brisbane;

[154] The ACCC does not grant authorisation to make any further associated codeshare agreement.

v. Queenstown – Brisbane;

vi. Auckland – Gold Coast;

- Provide the data required under clause 3 of the condition to the ACCC at the end of each scheduling season

683. The ACCC will commence a review on 1 September 2015 to determine whether to impose a growth factor on the routes of concern.

684. This determination is made on 3 September 2013.

Conduct not authorised

685. The authorisation does not extend to the making of any further associated code share agreement. In an email to the ACCC on 1 July 2013, the Applicants sought to clarify the scope of authorisation applications A91362 & A91363, and stated that authorisation is sought to make any further associated code share agreement. The ACCC does not have sufficient information at the time of making this determination to be satisfied with regards to the potential scope of any further associated codeshare agreement. The authorisation does not extend to the Applicants' provision of freight services, including freighter operations and cargo belly space on scheduled flights.

686. The authorisation does not extend to the Applicants' domestic networks to the extent that a particular service is not part of a connecting service across the trans-Tasman.

Date conditional authorisation comes into effect

687. This determination is made on 3 September 2013. If no application for review of the determination is made to the Australian Competition Tribunal (the Tribunal), it will come into force on 1 January 2014.

Attachment A - Summary of relevant statutory tests

Subsections 90(5A) and 90(5B) provide that the ACCC shall not authorise a provision of a proposed contract, arrangement or understanding that is or may be a cartel provision, unless it is satisfied in all the circumstances that:

- the provision, in the case of subsection 90(5A) would result, or be likely to result, or in the case of subsection 90(5B) has resulted or is likely to result, in a benefit to the public; and

- that benefit, in the case of subsection 90(5A) would outweigh the detriment to the public constituted by any lessening of competition that would result, or be likely to result, if the proposed contract or arrangement were made or given effect to, or in the case of subsection 90(5B) outweighs or would outweigh the detriment to the public constituted by any lessening of competition that has resulted or is likely to result from giving effect to the provision.

Subsections 90(6) and 90(7) state that the ACCC shall not authorise a provision of a proposed contract, arrangement or understanding, other than an exclusionary provision, unless it is satisfied in all the circumstances that:

- the provision of the proposed contract, arrangement or understanding in the case of subsection 90(6) would result, or be likely to result, or in the case of subsection 90(7) has resulted or is likely to result, in a benefit to the public; and

- that benefit, in the case of subsection 90(6) would outweigh the detriment to the public constituted by any lessening of competition that would result, or be likely to result, if the proposed contract or arrangement was made and the provision was given effect to, or in the case of subsection 90(7) has resulted or is likely to result from giving effect to the provision.

Subsection 90(8) states that the ACCC shall not:

- make a determination granting:

  i. an authorization under subsection 88(1) in respect of a provision of a proposed contract, arrangement or understanding that is or may be an exclusionary provision; or

  ii. an authorization under subsection 88(7) or (7A) in respect of proposed conduct; or

  iii. an authorization under subsection 88(8) in respect of proposed conduct to which subsection 47(6) or (7) applies; or

  iv. an authorisation under subsection 88(8A) for proposed conduct to which section 48 applies;

unless it is satisfied in all the circumstances that the proposed provision or the proposed conduct would result, or be likely to result, in such a benefit to the public that the proposed contract or arrangement should be allowed to be made, the proposed understanding should be allowed to be arrived at, or the proposed conduct should be allowed to take place, as the case may be; or

- make a determination granting an authorization under subsection 88(1) in respect of a provision of a contract, arrangement or understanding that is or may be an exclusionary provision unless it is satisfied in all the circumstances that the provision has resulted, or is likely to result, in such a benefit to the public that the contract, arrangement or understanding should be allowed to be given effect to.

Attachment B – Conditions of Authorisation

APPLICATIONS FOR AUTHORISATION A91362-A91363 – CONDITIONS

OBJECTIVE

The objective of these Conditions is to require the Applicants to maintain a base level of aggregated capacity on six routes (**Relevant Routes**), subject to a review to consider whether an increase in the minimum required capacity is warranted. Any obligation to grow aggregated capacity on the Relevant Routes is capped not to exceed trend (real) GDP growth in Australia. The Conditions also require the Applicants to provide information to the ACCC on an ongoing basis in relation to the Alliance.

The Conditions may also be varied in exceptional circumstances, or where there is a material change in market conditions or financial performance.

1. MINIMUM SEAT CAPACITY CONDITIONS

For each Scheduling Season which commences during the Term, the Applicants must make available not less than 100 per cent of the applicable Scheduling Season Seat Capacity for the Relevant Routes. To avoid doubt, this obligation requires the Applicants to make the specified capacity available in aggregate across all Relevant Routes. There is no minimum capacity required in relation to a particular Relevant Route.

2. TRANSITIONAL PROVISIONS

(a) For the period from 1 January 2014 to 31 March 2014, the Applicants must make available not less than 100 per cent of the applicable Transitional Scheduling Season Seat Capacity for the Relevant Routes. To avoid doubt, this obligation requires the Applicants to make the specified capacity available in aggregate across all Relevant Routes. There is no minimum capacity required in relation to a particular Relevant Route.

(b) The Auditor, in accordance with clause 7, must report on the Applicants' compliance with clause 2(a) of these Conditions for the period from 1 January 2014 to 31 March 2014. The Auditor is not required to report on the Applicant's compliance with the Previous Conditions of Authorisation for the period 1 November 2013 to 31 December 2013.

(c) Within three months of the end of the NW Season ending 31 March 2014, the Applicants must provide the information listed in clause 3 for each month of that Scheduling Season, being from 1 November 2013 to 31 March 2014.

3. REPORTING OBLIGATIONS

(a) Within three months of the end of each Scheduling Season during the Term, the Applicants must provide, for each month[155] of the previous Scheduling Season, the following information to the ACCC for all Trans-Tasman Routes flown by either or both of the Applicants:

(i) the total number of seats flown by the Applicants by cabin class on each route;

(ii) the total number of passengers (identifying separately Point to Point Passengers and Connecting Passengers where that information is available to the Applicant[156]) flown by the Applicants by cabin class on each route;

(iii) for each Applicant separately, and for the Alliance, average revenue per available seat kilometre (RASK) on each route by cabin class in accordance with the information that is retained in their financial accounting system;

(iv) if the RASK figures provided in accordance with clause 3(a)(iii) do not include all ancillary charges (including but not limited to in-flight food and entertainment purchases and excess or additional baggage purchases), the total amount of ancillary charges per available seat kilometre:

- A for each Trans-Tasman Route, where that information is available to the Applicant; and
- B as a total for all Trans-Tasman Routes,

in accordance with the relevant Applicant's financial accounting systems;

(v) for each Applicant separately, average cost per available seat kilometre (CASK) on each route, both in total and disaggregated by fixed and variable costs as is reported in the relevant Applicant's financial accounting systems, including but not limited to:

A. all direct costs;

B. fixed operating costs; and

155 As at the date of the Authorisation, Air New Zealand adopted a financial month reporting protocol that was a 4, 4, 5 week month format, and did not use calendar months. Also at the date of the Authorisation, for the purpose of reporting under the Alliance, the Applicants adopted a financial month reporting protocol that was a 4, 4, 5 week month format, and did not use calendar months

156 As at the date of the Authorisation, Virgin did not hold information identifying separately Point to Point Passengers and Connecting Passengers, but Virgin advised the ACCC that this information will be available to Virgin from 1 January 2014.

C. an allocation of overheads;

(vi) all applicable fare schedules (the route by route, class by class, pricing information); and

(vii) all tactical fare offerings, including the route to which they apply, the offer start date, the offer end date, the Filed Travel Period for which the fare is offered, and the price or discount offered, reported separately for Australian originated sales and New Zealand originated sales.

(b) The Applicants must provide a written description of the methodology used to calculate the RASK and CASK figures provided in accordance with clauses 3(a)(iii) and (v), and the ancillary charge figures provided in accordance with clause 3(a)(iv). The written description must include the details of all inclusions (e.g., any taxes or surcharges) and exclusions. The written description must also include the details of any changes to the Applicants' methodology compared to the methodology used for reporting under this clause 3 for the previous Scheduling Season.

(c) The information in this clause 3 must be provided to the ACCC in an accessible spreadsheet format.

4. ADJUSTMENT TO SCHEDULING SEASON BASE YEAR CAPACITY

4.1 Northern Summer Season

(a) On or before 31 January 2014, the Applicants must provide the ACCC with:

(i) **confirmed** Scheduling Season Base Year Seat Capacity figures from BITRE for the NS Season ending 31 October 2013, for those figures in Schedule A to these Conditions which are identified as being **provisional**; and

(ii) for each Applicant, the Route Profitability Information for each Relevant Route for each month of the NS Season ending 31 October 2013.

(b) In relation to clause 4.1(a)(i), the ACCC may undertake any consultation it considers necessary in relation to the confirmed figures provided by the Applicants.

(c) After considering the information provided by the Applicants in accordance with clause 4.1(a)(i), the outcome of any consultation undertaken in accordance with clause 4.1(b), and any other information the ACCC considers relevant, the ACCC may decide to adjust the provisional figures in Schedule A to these Conditions.

(d) The ACCC will give notice in writing to the Applicants of its decision on whether to adjust the provisional figures in Schedule A to these Conditions in accordance with clause 4.1(c) above.

(e) Any such adjustment will come into effect from the next NS Season after the date of the ACCC decision or such other date as determined by the ACCC, and the figures in Schedule A so adjusted will apply for the remainder of the Term, unless subject to further adjustment pursuant to clause 4.2.

(f) If the ACCC decides not to adjust the provisional figures in Schedule A in accordance with clause 4.1(c), the provisional figures in Schedule A will be taken as confirmed and will apply for the remainder of the Term, unless subject to further adjustment pursuant to clause 4.2.

4.2 Changes to BITRE's methodology for reporting the number of seats flown

(a) If BITRE changes its methodology for reporting the number of seats flown on the Relevant Routes from that which was used to calculate the Scheduling Season Base Year Seat Capacity Figures in Schedule A, then the ACCC may adjust the Scheduling Season Base Year Seat Capacity Figures in Schedule A to reflect BITRE's new methodology.

(b) In relation to clause 4.2(a), the ACCC will consult with the Applicants prior to making any adjustment.

(c) The ACCC will give notice in writing to the Applicants of its decision on whether to adjust the figures in Schedule A in accordance with clause 4.2(a).

(d) Any adjustment made under clause 4.2(a) will come into effect on a date that is determined by the ACCC.

5. ACCC REVIEW REGARDING WHETHER TO IMPOSE A CAPACITY GROWTH RATE

(a) The ACCC will conduct a review of these Conditions, commencing on 1 September 2015, to determine whether to impose a Capacity Growth Rate and may, in its absolute discretion, vary the Conditions to impose a Capacity Growth Rate applicable to future Scheduling Seasons subject to clause 5(e).

(b) When conducting a review, the ACCC must consult with the Applicants and allow the Applicants an opportunity to make submissions within a specified period. The ACCC may publish or otherwise make publicly available the Applicants' submissions in relation to a review under this clause 5.

(c) When conducting a review, the ACCC may undertake further consultation as it considers necessary, including inviting submissions within a specified period from the Applicants and interested parties.

(d) Without limiting the matters the ACCC may take into account for the purpose of determining whether to vary these Conditions pursuant to clause 5(a), the ACCC may have regard to the following matters:

(i) current market conditions on Trans-Tasman Routes;

(ii) airlines' current and planned future capacity growth on the Relevant Routes;

(iii) available forecasts of passenger demand on Trans-Tasman Routes;

(iv) the size and type of aircraft operated by the Applicants;

(v) regulatory constraints on either of the Applicants' ability to operate on each Relevant Route; and

(vi) the impact of the variation on Route Profitability on each Relevant Route.

(e) The ACCC must not make a determination to adjust the Conditions to impose a Capacity Growth Rate pursuant to clause 5(a) that is more than the sum of quarterly changes in Australia's Trend Chain Volume GDP, as published by the Australian Bureau of Statistics in Catalogue No 5206.0, data series A2298668K, commencing from the September-December 2013 quarterly change.

(f) The ACCC, having had regard to submissions received from the Applicants and any other interested parties and any other information the ACCC considers relevant, will advise the Applicants in writing of its decision, following its review, of whether to adjust the Conditions to impose a Capacity Growth Rate in accordance with clause 5(a).

(g) Any such adjustment will come into effect, and the Applicants will give effect to any such adjustment, from the later of:

(i) the next Scheduling Season after the date of the ACCC decision;

(ii) four months following the date of the decision;

unless the ACCC determines that another commencement date is more appropriate (which may be a date before four months following the date of the decision).

(h) The reporting requirement in clause 3 continues irrespective of whether the ACCC is conducting a review under this clause 5.

6. APPLICATIONS TO VARY THE CONDITIONS

(a) The Applicants may apply in writing to the ACCC for a variation to the Conditions, in the following circumstances:

(i) Exceptional Circumstances;

(ii) Material Change in Market Conditions; or

(iii) Material Adverse Financial Performance.

(b) Any application by the Applicants to the ACCC for a variation to the Conditions must state the nature of the variation sought and the circumstances claimed by the Applicants and must be accompanied by evidence supporting the application.

(c) The ACCC will consult with the Applicants in relation to the application for variation to the Conditions and allow the Applicants an opportunity to make submissions within a specified period.

(d) The ACCC may request from the Applicants any additional information required by the ACCC to assess the application for a variation of the Conditions.

(e) The ACCC may undertake any further consultation as it considers necessary to consider any such request for a variation to the Conditions, including inviting submissions from interested parties.

(f) In undertaking an assessment of an application to vary the Conditions, the ACCC may publish or otherwise make publicly available the Applicants' submissions in support of their request for variation and to any submissions made by the interested parties.

(g) Without limiting the matters to which the ACCC may have regard for the purpose of determining whether to vary the Conditions (including whether a Material Change in Market Conditions has occurred), the ACCC must have regard to any entry or expansion by airlines other than the Applicants on any Relevant Route and any commencement of services by the Applicants on any Trans-Tasman Route that neither of the Applicants serviced at the commencement of the Term.

(h) After considering an application to vary the Conditions and any submissions received in respect of such an application, the ACCC may, in its absolute discretion, determine to vary the Conditions or dismiss the application for variation.

(i) The ACCC may vary the requirement to comply with the Conditions either permanently or on a temporary basis and any variation may be expressed as subject to any conditions as the ACCC sees fit.

(j) The ACCC will advise the Applicants in writing of its decision in respect of an application for variation made under clause 6(a).

(k) If the ACCC determines to vary the Conditions, the variation will be effective from the date determined by the ACCC.

7. AUDIT OF COMPLIANCE

7.1 Obligation to appoint an independent auditor

(a) The Applicants must appoint and maintain an independent auditor to report to the ACCC with respect to the compliance by the Applicants with clause 1 (and clause 2(a)) of these Conditions.

7.2 Proposed Auditor

(a) By 31 January 2014, the Applicants must identify a prospective independent auditor **(Proposed Auditor)** and provide the ACCC written notice of the identity and contact details of the Proposed Auditor.

(b) The written notice referred to in clause 7.2(a) is to include such information or documents as the ACCC requires to assess whether to object to the appointment of the Proposed Auditor, including a copy of the proposed terms of engagement.

(c) The Proposed Auditor must be a person who has the relevant skills necessary to carry out the functions of the Auditor and is independent of the Applicants and their Related Bodies Corporate.

(d) Without limitation, an Auditor is not independent if he or she:

  (i) is a current employee or officer of either or both of the Applicants;

  (ii) is a person who has been an employee or officer of either or both of the Applicants in the past three years;

  (iii) is a person who, in the opinion of the ACCC, holds a material interest in either or both of the Applicants;

(iv) is a professional adviser of either or both of the Applicants, whether current or in the past three years;

(v) is a person who has a contractual relationship, or is an employee or contractor of a firm or company that has a contractual relationship with either or both of the Applicants, but for the terms of any Auditor agreement with the Applicants or any corresponding agreement in relation to the Previous Conditions of Authorisation;

(vi) is a supplier, or a person who is an employee or contractor of a firm or company that is a supplier of either or both of the Applicants;

(vii) is a material customer of, or a person who is an employee or contractor of a firm or company that is a material customer of, either or both of the Applicants; or

(viii) has, or has had, any other relationship with either or both of the Applicants which, in the opinion of the ACCC, is likely to affect the ability of that person to act independently.

7.3 Appointment of Auditor

(a) If, within five Business Days of receipt by the ACCC of the written notice referred to in clause 7.2(a), or such further period as is required by the ACCC and notified to the Applicants:

(i) the ACCC does not object to the Proposed Auditor, the Applicants must appoint the Proposed Auditor as the Auditor as soon as practicable (but in any event within five Business Days) on terms approved in writing by the ACCC and consistent with the performance by the Auditor of his or her functions under these Conditions and forward to the ACCC a copy of the executed terms of appointment of the Auditor within one Business Day of its execution; or

(ii) the ACCC does object to a Proposed Auditor, the Applicants will appoint a person identified by the ACCC at its absolute discretion as the Auditor on terms approved by the ACCC and consistent with the performance by the Auditor of his or her functions under these Conditions and forward to the ACCC a copy of the executed terms of appointment of the Auditor within one Business Day of its execution.

7.4 Obligations relating to the Auditor

(a) The Applicants must procure that the terms of appointment of the Auditor include obligations on the Auditor to:

(i) continue to satisfy the independence criteria in clause 7.2(d) for the period of his or her appointment;

(ii) provide any information or documents requested by the ACCC about the Applicant's compliance with these Conditions directly to the ACCC;

(iii) report or otherwise inform the ACCC directly of any issues that arise in the performance of his or her functions as Auditor or in relation to any matter that arises in connection with these Conditions; and

(iv) follow any direction given to him or her by the ACCC in relation to the performance of his or her functions as Auditor under these Conditions.

7.5 Compliance audit

(a) The Applicants must within 25 Business Days of the end of a Scheduling Season, provide to the ACCC a written audit report as set out in clause 7.5(b) from the Auditor in relation to the Applicant's compliance with its obligations under clause 1 (or clause 2(a) when applicable).

(b) The Auditor is to prepare a detailed report (**Auditor's Report**) on:

(i) the Applicant's compliance with clause 1 (or clause 2(a) when applicable) of these Conditions;

(ii) the reasons for the conclusions reached in the Auditor's Report;

(iii) any qualifications made by the Auditor in forming his or her views; and

(iv) any recommendations by the Auditor to improve the integrity of the auditing process and any reasonable recommendations to improve the Applicants' processes or reporting systems in relation to compliance with clause 1 of these Conditions.

(c) The Auditor must provide the Applicants with a draft Auditor's Report prior to it being provided to the ACCC, for the sole purpose of the Applicants having the opportunity to identify any factual errors. The Auditor retains complete discretion as to whether to accept or reject any corrections of factual errors proposed by the Applicants. Where corrections are accepted by the Auditor, the Auditor will provide the ACCC with details of the corrections proposed by the Applicants and accepted by the Auditor.

(d) The Applicants must implement any recommendations of the Auditor made pursuant to clause 7.5(b)(iv), and notify the ACCC of the implementation of the recommendations, within 10 Business Days of receiving the Auditor's Report or within a period agreed with the ACCC.

(e) The Applicants must:

(i) comply with any direction of the ACCC in relation to the matters arising from any Auditor's Report of the Auditor, within 10 Business

Days of being so directed to do so (or such longer period as is agreed with the ACCC);

(ii) direct its personnel, including directors, managers, officers, employees and agents to act in accordance with the obligations set out in these Conditions and ensure that such personnel are aware of the Auditor and its role; and

(iii) ensure that the Auditor will provide information and documents requested by the ACCC directly to the ACCC.

(f) The Applicants must maintain and fund the Auditor and must indemnify the Auditor for reasonable expenses and any loss, claim or damage arising from the proper performance by the Auditor of functions required to be performed by the Auditor under these Conditions.

7.6 Resignation or termination of appointment of the Auditor

(a) The Applicants must immediately notify the ACCC in writing in the event that an Auditor resigns or otherwise stops acting as an Auditor before the termination of this Authorisation.

(b) The ACCC may approve any proposal by, or alternatively may direct, the Applicants to terminate the appointment of an Auditor if in the ACCC's view the Auditor acts inconsistently with the provisions of these Conditions or the terms of his or her appointment.

(c) If either clause 7.6(a) or 7.6(b) applies, the ACCC may nominate an alternative auditor to be the Auditor.

(d) The Applicants must, within five Business Days of the ACCC nominating an alternative Auditor:

(i) appoint the alternative Auditor nominated by the ACCC on terms approved by the ACCC and consistent with the performance by the Auditor of his or her functions under these Conditions; and

(ii) forward to the ACCC a copy of the executed terms of appointment within one Business Day.

8. INFORMATION

(a) The Applicants must respond as soon as practicable to any queries or requests for information or documents made by the ACCC pursuant to or in relation to these Conditions.

(b) The ACCC may require the Applicants to:

(i) furnish information, documents and materials to the ACCC in the time and in the form requested by the ACCC;

(ii) produce information, documents and materials to the ACCC within the Applicants' custody, power or control in the time and in the form requested by the ACCC; and/or

(iii) direct its personnel, including its directors, contractors, managers, officers, employees and agents, to attend the ACCC at a reasonable time and place appointed by the ACCC to answer any questions the ACCC (including its Commissioners, its staff or its agents) may have.

(c) Information furnished, documents and material produced or information given in response to any request or direction from the ACCC under these Conditions may be used by the ACCC for any purpose consistent with the exercise of its statutory duties and functions.

(d) Nothing in these Conditions requires the provision of information or documents in respect of which either of the Applicants claim legal professional or other privilege.

9. DEFINITIONS AND INTERPRETATION

ACCC: means the Australian Competition and Consumer Commission.

Alliance: means the alliance between the Applicants pursuant to the Australasian Airline Alliance Agreement (AAA) dated 3 May 2010 and amended 15 June 2012, an associated Code Share Agreement dated 3 May 2010 and amended 15 June 2012, and related agreements which are contemplated by the AAA.

Applicants: means Virgin Australia Airlines Pty Ltd, Virgin Australia Airlines (NZ) Ltd, Virgin Australia Airlines (SE Asia) Pty Ltd, Virgin Australia International Airlines Pty Ltd (together **Virgin**) and Air New Zealand Limited (**Air New Zealand**).

Auditor: means the independent auditor appointed in accordance with clause 7.

Authorisation: means the determination by the ACCC regarding applications for authorisation A91362 and A91363.

Base Year: means the 12 month period from 1 November 2012 to 31 October 2013.

BITRE: means the Bureau of Infrastructure, Transport, and Regional Economics.

Business Day: means a day that is not a Saturday, Sunday, or public holiday in the Australian Capital Territory, New South Wales, Queensland or Auckland.

Capacity Growth Rate: means a growth rate as determined by the ACCC in accordance with clause 5.

Conditions: mean these conditions (including Schedule A) subject to which the Authorisation is granted.

Connecting Passenger: means any passenger carried by an Applicant on a single Trans-Tasman Route starting in New Zealand and ending in Australia, or vice versa, who before or after that Trans-Tasman Route, as part of the same journey, travels from or to another destination (domestic or international) operated by Air New Zealand, Virgin Australia or a third carrier.

Exceptional Circumstances: include:

(a) force majeure events, including natural disasters, national emergency, insurrection, riot, war, pandemic; or

(b) events or factors outside of the control of the Applicants:

  (i) such that the Applicants cannot, or on reasonable grounds anticipate that they cannot, practically comply with the Conditions; or

  (ii) which have or are reasonably anticipated to have a material adverse impact on the demand for travel on the Applicants' services or the Applicants' service operating costs, or affecting operations on the Relevant Routes.

Filed Travel Period: means the travel period for which the relevant fare is valid, as communicated in the Applicants' fare rules in the Applicants' internal booking engine(s) or via the Global Distribution System.

Material Adverse Financial Performance: means an actual decline in Route Profitability (whether the result is a profit or a loss) for the one or both of the Applicants which the ACCC agrees in writing is material on:

(a) a Relevant Route;

(b) more than one Relevant Route; or

(c) all Trans-Tasman Routes;

when compared to the relevant Route Profitability of each of or both of (as applicable) the Applicants in the Base Year.

Material Change in Market Conditions: means a change to the market conditions which the ACCC agrees in writing to be material on:

(a) a Relevant Route;

(b) more than one Relevant Route; or

(c) all Trans-Tasman Routes.

NS Season means the northern summer season from 1 April to 31 October.

NW Season means the northern winter season from 1 November to 31 March.

Point to Point Passenger means any passenger carried by an Applicant on a single Trans-Tasman Route starting in New Zealand and ending in Australia, or vice versa.

Previous Conditions of Authorisation means the conditions applicable to the ACCC's previous authorisation of the Alliance (authorisation numbers A91227 and A91228).

Relevant Routes means each of the following city pairs:

(a) Wellington-Brisbane

(b) Queenstown-Brisbane

(c) Auckland-Gold Coast

(d) Christchurch-Brisbane

(e) Christchurch-Melbourne

(f) Dunedin-Brisbane

Route Profitability: means the profit (or loss) on a route (which may be represented in terms of a net margin, that is, net route profit expressed as a percentage of total route revenue) determined in accordance with the relevant Applicant's usual management accounting methodology (that is, the same methodology that Applicant uses to determine route profitability on all other routes).

Route Profitability Information: means information regarding the profit (or loss) on a route accompanied by reports including categorised details of revenues and costs and an explanation of the relevant revenue and cost categories, determined in accordance with the relevant Applicant's usual management accounting methodology (that is, the same methodology that Applicant uses to determine route profitability on all other routes).

Scheduling Season: means either the NS Season or the NW Season.

Scheduling Season Base Year Seat Capacity: means the Applicants' combined total number of seats flown on the Relevant Routes in, as applicable, the NS Season or the NW Season in the Base Year as set out in Schedule A of these Conditions, and as adjusted in accordance with clause 4 of these Conditions.

Scheduling Season Seat Capacity means the Scheduling Season Base Year Seat Capacity in, as applicable, the NS Season or the NW Season, and as:

(a) adjusted for any Capacity Growth Rate determined by the ACCC pursuant to clause 5(a) of these Conditions; or

(b) varied in accordance with clause 6 of these Conditions.

Transitional Scheduling Season Seat Capacity means the seat capacity figures set out in Schedule B to the Conditions.

Term: means the term of the Authorisation.

Trans-Tasman Route: means any route between a particular Australian location and a particular New Zealand location.

Interpretation

In the interpretation of these Conditions, the following apply unless the context otherwise requires:

(a) headings are inserted for convenience only and do not affect the interpretation of these Conditions;

(b) a reference in these Conditions to any company includes its related bodies corporate within the meaning of section 4A of the *Competition and Consumer Act 2010*;

(c) a reference to a clause is a reference to a clause of these Conditions;

(d) if the day on which any act, matter or thing is to be done under these Conditions is not a Business Day, the act, matter or thing must be done on the next Business Day;

(e) a word which denotes the singular also denotes the plural and vice versa,

(f) a reference to the words ‘include’ and ‘including’, and similar expressions is to be construed without limitation; and

(g) a party includes its successors and permitted assigns.

SCHEDULE A – SCHEDULING SEASON BASE YEAR SEAT CAPACITY[157]

The **Scheduling Season Base Year Seat Capacity** means the Applicants' combined total number of seats flown on the Relevant Routes in, as applicable, the NS Season or the NW Season in the Base Year as set out in this Schedule A. In the below tables, references to seat capacity figures for a particular route are for information purposes only.

Scheduling Season Base Year Seat Capacity for NS Season:

Wellington-Brisbane	**Seat Capacity for NS Season**
Air New Zealand	0 (provisional)
Virgin	157,648 (provisional)
Total	*Total 157,648*
Queenstown-Brisbane	**Seat Capacity for NS Season**
Air New Zealand	15,135 (provisional)
Virgin	32,940 (provisional)
Total	*Total 48,075*
Auckland-Gold Coast	**Seat Capacity for NS Season**
Air New Zealand	47,125 (provisional)
Virgin	77,360 (provisional)
Total	*Total 124,485*
Christchurch-Brisbane	**Seat Capacity for NS Season**
Air New Zealand	69,707 (provisional)
Virgin	74,880 (provisional)
Total	*Total 144,587*
Dunedin-Brisbane	**Seat Capacity for NS Season**
Air New Zealand	0 (provisional)
Virgin	53,100 (provisional)
Total	*Total 53,100*
Christchurch Melbourne	**Seat Capacity for NS Season**
Air New Zealand	73,368 (provisional)
Virgin	30,060 (provisional)
Total	*Total 103,428*
TOTAL SCHEDULING SEASON BASE YEAR SEAT CAPACITY FOR NS SEASON	**631,323**

157 Note: For the avoidance of doubt, the above figures include both inbound and outbound seat capacity for each Relevant Route. This data includes all seats flown on the Relevant Routes. It therefore includes seats occupied by uplift/discharge passengers, seats occupied by transit passengers and unoccupied seats.

Scheduling Season Base Year Seat Capacity for NW Season:

Wellington-Brisbane	**Seat Capacity for NW Season**
Air New Zealand	0
Virgin	108,900
Total	*Total 108,900*
Queenstown-Brisbane	**Seat Capacity for NW Season**
Air New Zealand	0
Virgin	10,800
Total	*Total 10,800*
Auckland-Gold Coast	**Seat Capacity for NW Season**
Air New Zealand	32,897
Virgin	52,920
Total	*Total 85,817*
Christchurch-Brisbane	**Seat Capacity for NW Season**
Air New Zealand	38,969
Virgin	72,000
Total	*Total 110,969*
Dunedin-Brisbane	**Seat Capacity for NW Season**
Air New Zealand	0
Virgin	26,280
Total	*Total 26,280*
Christchurch Melbourne	**Seat Capacity for NW Season**
Air New Zealand	54,656
Virgin	44,640
Total	*Total 99,296*
TOTAL SCHEDULING SEASON BASE YEAR SEAT CAPACITY FOR NW SEASON	**442,062**

Note: For the avoidance of doubt, the above figures include both inbound and outbound seat capacity for each Relevant Route. This data includes all seats flown on the Relevant Routes. It therefore includes seats occupied by uplift/discharge passengers, seats occupied by transit passengers and unoccupied seats.

SCHEDULE B – TRANSITIONAL SCHEDULING SEASON SEAT CAPACITY

The **Transitional Scheduling Season Seat Capacity** means the Applicants' combined total number of seats flown on the Relevant Routes as set out in this Schedule B. In the below table, references to seat capacity figures for a particular route are for information purposes only.

Transitional Scheduling Season Seat Capacity:

Wellington-Brisbane	**Seat Capacity for transitional period**
Air New Zealand	0
Virgin	64,620
Total	*Total 64,620*
Queenstown-Brisbane	**Seat Capacity for transitional period**
Air New Zealand	0
Virgin	6,840
Total	*Total 6,840*
Auckland-Gold Coast	**Seat Capacity for transitional period**
Air New Zealand	19,433
Virgin	30,960
Total	*Total 50,393*
Christchurch-Brisbane	**Seat Capacity for transitional period**
Air New Zealand	22,812
Virgin	42,480
Total	*Total 65,292*
Dunedin-Brisbane	**Seat Capacity for transitional period**
Air New Zealand	0
Virgin	15,840
Total	*Total 15,840*
Christchurch Melbourne	**Seat Capacity for transitional period**
Air New Zealand	32,095
Virgin	25,920
Total	*Total 58,015*
TOTAL SCHEDULING SEASON SEAT CAPACITY FOR TRANSITIONAL PERIOD	**261,000**

Note: For the avoidance of doubt, the above figures include both inbound and outbound seat capacity for each Relevant Route. This data includes all seats flown on the Relevant Routes. It therefore includes seats occupied by uplift/discharge passengers, seats occupied by transit passengers and unoccupied seats.