Australian Government

Productivity Commission

PRODUCTIVITY COMMISSION

MR P LINDWALL, Commissioner
MR K BAXTER, Commissioner
MR S KING, Commissioner

TRANSCRIPT OF PROCEEDINGS

AT THE GRACE HOTEL, 77 YORK STREET, SYDNEY
ON WEDNESDAY, 28 NOVEMBER 2018 AT 10.00 AM

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COMMISSIONER LINDWALL: Good morning, everyone, and I'm glad you've been able to brave the rain to get here because it's an interesting one when you're talking about an airports inquiry and you find that Sydney Airport's operating on one runway today and obviously they're using less jet fuel today perhaps than they normally would.

I'm Paul Lindwall, the Presiding Commissioner on the inquiry and I've got Ken Baxter here and Stephen King here on my right who are my fellow Commissioners. We've got Nick here who's the only person who's able to come up because Katie was coming but the plane was cancelled, the flight was cancelled.

Anyway, we normally introduce a bit about the inquiry. Hello, Warren. The inquiry started with the terms of reference from the government in June 2018 as a 12-month inquiry, and its purpose is to investigate whether the economic regulation of airport services promotes the efficient operation of airports and related industries.

The Commission has been asked specifically to review the competition in the market for jet fuel, and that's why we decided to hold hearings on that topic. Today and in Melbourne on Friday.

We've talked to representatives from the Australian State and Territory governments, airports, airlines, representative bodies, academics, researchers and individuals with an interest in the inquiry. We released our issues paper on 9 July, have received 77 submissions since then, quite detailed submissions in most cases. Of course, as always, we're grateful to all the organisations and individuals that have participated with our inquiry and who put in submissions, appeared at hearings, as they will in the future, and this is our first public hearing for the inquiry. We will have one in Melbourne on Friday about jet fuel.

We aim to produce and release our draft report in February next year, and then we'll have public hearings on the broader issues of the inquiries, probably in March/April next year, and then our final report will go to the government in June 2019.

Participants and those who registered their interest in the inquiry will be advised of the final reports released by the government and that's up to 25 sitting days from the - it has to be tabled 25 sitting days after completion.

The purpose of hearings is to provide participants the opportunity to elaborate on their submissions, discuss issues with the Commissioners, and any organisation or person can participate in the hearings, but those who

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have an interest in jet fuel are obviously encouraged to appear. There will be an opportunity to speak afterwards for the registered participants that we've got today such as Barry.

We like to, as you can see, conduct our hearings in a reasonably informal manner, but there is a transcript being taken, as always in hearings, and that's why we don't take questions from the floor, but if you want to say something on the record you're welcome to come up and testify like anyone else.

You're not required to take an oath but of course under our Productivity Commission Act you're required to be truthful in your remarks.

You're welcome to raise comments on other submissions as you see fit, and if there are any media representatives please let yourself be known to Nick here, and of course if there is an emergency such as an evacuation being needed the building will be advised through the normal process and you'll have to use the stairs, I guess. You don't want to use the lifts.

So we'll start right now with Barry, and perhaps Barry, if you could just introduce yourself and if you want to say an opening statement that would be most welcome.

MR ABRAMS: Thank you very much. Barry Abrams, Executive Director. I've got some opening statements.

So the Board of Airline Representatives of Australia, or BARA, really appreciates the opportunity to provide further comment to the review of jet fuel supply at Australian airports.

Jet fuel represents about a third of global airline operating costs, and many of Australia's international air services have very long distances between airports leading to high fuel burns per passenger. Indeed, international flights now uplift about 5 billion litres of jet fuel annually in Australia costing about $4 billion. So minimising jet fuel costs is critical to maintaining and increasing the number of commercially viable routes to and from Australia.

It's taken BARA a long time to draw attention to, and then hopefully concentrate some attention, on the opportunities and benefits we see of a more competitive supply of jet fuel. BARA wants to promote a set of arrangements that support ongoing competition on its merits between jet fuel suppliers, and we also believe that competition is consistent with supporting more reliability in jet fuel.

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The problems we see today can be traced to issues with the jet fuel infrastructure supply chains. These supply chains transport the jet fuel from the refineries and ports to the aircraft at the airport. We think that modest reforms to providing and pricing for this infrastructure can support a more competitive and reliable supply of jet fuel.

What problem is BARA seeking to address? Our efforts, our long-standing efforts in this area stem from the sustained concerns raised by member airlines over a lack of effective competition when they tender for jet fuel at Australia's major international airports. Members want to see the same degree of competition and tension oversupply in Australia as occurs at many overseas airports.

Jet fuel rationing at Sydney and Melbourne airports has also been unwelcome and led to high profile events that disrupted industry operations, passengers and freight forwarders. Jet fuel rationing events have also attracted investigation and involvement by both the Australian government and State governments.

So governments today are already being drawn into problems with jet fuel supply, but largely on an ad hoc basis in response to severe jet fuel rationing events. BARA would like to see arrangements that actually minimise the need for this ad hoc involvement by government.

So what are we seeking, and what do we think will improve matters? In developing our policy document, a competitive supply of jet fuel at Australia's major international airports, BARA consulted a range of stakeholders that included the airport operators, infrastructure providers, jet fuel suppliers, and obviously airlines, and we canvassed a wide range of potential options that could improve the quality and the efficiency of the jet fuel infrastructure supply chains.

Given the previous experience we've had and the ongoing developments we've seen, we believe there's really three initiatives that would deliver on the desired outcomes or after. The first is investment in jet fuel supply infrastructure at the airports consistent with facilitating competition between suppliers and supporting the ongoing development of the airport; secondly, workable access arrangements to the on airport jet fuel storage and distribution facilities; and thirdly, periodic studies sponsored by the Australian government and relevant State government into the overall jet fuel supply and demand situation at each of the four major international airports.

BARA would like to emphasise how it's well within the industry's capability to implement these arrangements with a modest level of government support and encouragement. They also offer governments a

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more structured and effective involvement, rather than the ad hoc responses to jet fuel rationing events.

So just touching on where we are today, I think it is important to note that BARA has identified reforms that do appear to be largely endorsed by most industry participants reading through the submissions, and some implementation has already occurred, especially at Melbourne Airport, and therefore I think it's worth just commenting on the current situation at the two largest jet fuel markets in Australia, namely, Melbourne and Sydney Airports.

So starting with Melbourne Airport. So in response to widespread jet fuel rationing at Melbourne Airport in 2016, the Victorian Government established an aviation industry round table to help deal with the jet fuel problems, and BARA's been very supportive of the actions taken by both the Victorian and Australian Governments on these issues as the market participants themselves were unlikely to establish the necessary arrangements to improve matters.

So just touching on BARA's three reform initiatives, so when we look at jet fuel investment as stated by Melbourne Airport in a press release in a deal brokered with the assistance of the Victorian State Government fuel suppliers in Melbourne Airport agreed to terms that would ensure both on-site storage and input supply capacity will cope with the forecast growth in passenger numbers.

As airlines we would like to see and be consulted on more around the actual development as well out of this infrastructure, but it does show how, with assistance from the Victorian Government, some sensible progress could be made.

On access arrangements, BARA notes in Mobil Oil Australia's submission to the Commission, it stated that the joint venture supports a competitive market, namely, the JUHI arrangements include an open access regime that allows non-equity participants to access the facilities and services. A number of third parties have commenced the application process for JUHI access by making enquiries with the JUHI.

So whilst, as we've detailed in our submissions, we do have concerns about the detail and the lack of transparency around those arrangements, these are obviously positive statements and developments. They do show that just moving from what are effectively internally set arrangements to more open arrangements, it immediately encourages interest from potential fuel suppliers.

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The outcome at Melbourne Airport is also consistent with the case studies that we included in our submission where we showed that once an airport or a set of facilities moved to a more open set of access arrangements, there was normally an immediate sort of increase in interest from potential suppliers.

So then we look at the demand and supply studies. So through the aviation industry round table the Australian and Victorian Governments also jointly sponsored a jet fuel supply and demand statement for the airport. The study has identified emerging issues in the supply chain and it is understood we need to repeat that study about once every five years.

And finally, BARA does appreciate that Melbourne Airport has not used the leased negotiations with Melbourne JUHI as an opportunity to extract economic rent through a fuel throughput levy. Now, by focussing on the issues at hand, it's encouraged the negotiation of outcomes that are far more likely to be aligned with industry needs.

So then we turn to Sydney Airport. Unfortunately, it's a rather different, and I might say, sad state of affairs for the jet fuel supply arrangements at Sydney Airport as BARA understands them. BARA remains particularly concerned at Sydney Airport and Sydney JUHI will not agree upon outcomes in the best interests of supporting Australia's international aviation industry. Adding to the uncertainty BARA understands that Sydney Airport can terminate the current lease with Sydney JUHI with three years' notice, and that was put on the public record as part of the access declaration by Sydney JUHI.

So again, just touching on the sought after initiatives, on jet fuel investment BARA is unaware of any arrangements that would underpin the orderly investment in jet fuel supply infrastructure at the airport. BARA has highlighted the lack of investment in the bridger facilities for road tankers to support a more reliable and competitive supply of jet fuel, just as one area of concern. It's an investment that's been identified that's of low cost, can generate a lot of benefit and yet we haven't seen it in seven, eight years now.

On access arrangements, access to Sydney JUHI remains as per the internally generated equity participation arrangements, and uncertainty over the lease tenure and other terms and conditions could also well contribute to a barrier to entry to new suppliers, and you come into Melbourne JUHI and equity, well, you might be wound up in three years and who knows what you might get at the end of that.

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Finally, on the demand and supply studies, the supply and demand of jet fuel was last investigated in about 2010, and it's unclear at least to BARA how close the industry may or may not be heading towards problems in jet fuel supplied at Melbourne Airport, given the growth in demand and a conversion of the two refineries.

COMMISSIONER LINDWALL: Sorry, Melbourne or Sydney?

MR ABRAMS: Sydney.

COMMISSIONER LINDWALL: I think you said Melbourne a couple of times in there which should have been Sydney.

MR ABRAMS: Sydney, yes. Sorry. Little information is available to the industry participants. Yes, sorry, all of the previous of those statements are regarding Sydney.

COMMISSIONER LINDWALL: Yes, yes.

MR ABRAMS: And finally, BARA has a long-standing problem with Sydney Airport extracting unjustified economic rent through its fuel throughput levy which we consider to be a fee for no service, and overall BARA sees a clear need for some government oversight and involvement to encourage outcomes at Sydney Airport to fit with improving the provision and pricing of jet fuel services at the airport.

So just in summary, BARA does consider that there is a relatively straightforward path to supporting market-driven improvements in the reliability and competitive supply of jet fuel. It does require some government involvement and BARA has outlined how they can support the establishment of improved arrangements, and we've already seen this occur in part at Melbourne Airport. Airlines would like to see this improved upon and progressively implemented at the other major airports, and that's my opening remarks.

COMMISSIONER LINDWALL: Thank you, Barry. Could you, since you've mentioned Sydney and Melbourne, briefly comment about Brisbane and Perth then perhaps?

MR ABRAMS: Okay. So as we understand it today at Brisbane Airport, the level of capacity and we believe there are, sort of, three effective suppliers. So as we see it today, the level of issue at Brisbane Airport seems to be considerably less. That said, it obviously then becomes interesting how is the world going to look in, say, five, ten, 15, 20, years with the growth in supply, and are the arrangements suitable for the future.

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Perth Airport, as we understand it, there is really just one effective supplier, and one pipeline to the airport, so it clearly has some issues in terms of competition and the potential issues with reliability to supply. So that is an airport of a level of concern to BARA that in turn we would like to see improved upon.

COMMISSIONER LINDWALL: Okay, and the Victorian Government actually was to set up a round table.

MR ABRAMS: Yes.

COMMISSIONER LINDWALL: Anything else that the Victorian Government did in particular?

MR ABRAMS: Well, I think the important parts of the round table was to get all the parties in one room to be talking about the issues that needed to be addressed, so that included around, "Okay, what are we doing on the level of tankage at the airport? What's going on with the rest of the supply chain?", you know, "Why can't we see some sensible access arrangements put on".

So what other things the Victorian Government may or may not have done behind the scenes, because Melbourne Airport talk about brokering a deal, so presumably there were some meetings and some discussions to help the parties to come together as well as the round table which was sort of more the formal following and investigating of what was happening.

COMMISSIONER LINDWALL: Okay. No, that's good. I your Table 1 of your submissions, you've got the number of effective suppliers.

MR ABRAMS: Yes.

COMMISSIONER LINDWALL: So, say, Sydney is two. Well, they're all two, apart from Brisbane which is three, and Perth, as you mentioned just then, one.

MR ABRAMS: Yes.

COMMISSIONER LINDWALL: How do you reach the numbers?

MR ABRAMS: Yes, yes, so for Sydney and as part of our access declaration, we went to a number of members to provide information on how the quality of the outcomes when they tendered for jet fuel at the airport. So as we put in more detail in our submission to the competition

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policy review, so what we found was that for ten contracts there were 46 opportunities put out for fuel suppliers to provide a bid. Of those 46 opportunities, no bid was received 26 times. So the majority of the contracts there was only one potential provider, and in a few cases there was two potential providers to provide 100 per cent of the fuel of an airline's needs.

So what we sort of linked it to for Sydney is basically the maximum number of 100 per cent that airlines were achieving. For the other airports, and that also sits with our understanding that there are effectively two suppliers at the airport with a significant presence.

So then in the roll-out for the other airports we've simply used the commonly understood and known, you know, suppliers at the airport who are providing a significant amount of fuel for international airlines.

So I don't pretend there's any hard science behind those numbers, because, you know, concepts of competition and the level of competition are always a bit subjective but that would be our best view at the moment.

COMMISSIONER KING: Just to follow upon that Barry, so if 20 of the tenders, I think you said, got no bids, what does the airline do in that situation?

MR ABRAMS: So what's happened, so when I say there was no bids, so an airline's put out a contract and it's put it out to, say, four fuel companies, for argument's sake. Maybe one or two come back and say, "I'm prepared to put in a bid". So that's what we've based it on. So it doesn't mean there was 26 times there was no fuel offered. So what it means was, there were, of those ten contracts there was effectively 46 offers put to fuel companies, and of that, I think about in two cases an airline got more than one bid that could meet its fuel needs.

COMMISSIONER BAXTER: Could I just explore this a little more and tie it up with the Victorian arrangements that are made by the Victorian Government, is there any evidence or do you or some of your members have a suspicion that there is a quid pro quo in the Victorian Government and enabling the facilities that would provide Melbourne Airport? In other words, does the Victorian Government get some benefit out of reaching that arrangement which is not necessarily transparent?

MR ABRAMS: There's certainly no information that BARA would have that would raise those concerns. I think from a perspective of participating in the round table arrangements, we were very supportive and encouraged by the efforts of the Victorian Government to try to broker some sensible arrangements on both the investment in the tankage at the airport, and also to encourage the bringing in of some initial steps at access arrangements.

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So in BARA's perspective, no, they weren't concerns that came to mind. At the same time, you know, we're obviously not party to the detail of any of those discussions and negotiations that went on. We're just looking at it in terms of the final outcomes that we saw.

COMMISSIONER LINDWALL: Now, obviously, there are two sides to this because we're talking about fuel.

MR ABRAMS: Yes.

COMMISSIONER LINDWALL: And one is about the supply and this forum is a way of approaching that, I guess, to ensure that you have sufficient for the foreseeable future for the foreseeable amount of activity, but the other is the price, right?

MR ABRAMS: Yes.

COMMISSIONER LINDWALL: Do you have any thought about how much price is above what it would be in a more open market, and how much would that - what's the ball park figure there would you say?

MR ABRAMS: It's a very good question. Unfortunately from BARA's perspective, we specifically don't get any commercially sensitive information from any of our members or suppliers on the level of jet fuel pricing.

Obviously as IATA and others have put in, jet fuel costs in Australia are very high globally, and then of course that brings into question how many cents per litre could be achieved through a combination of efficiency benefits. We would like to think through a combination of improvements in competition, improvements in the efficiency of shipping and improvements in the efficiency of the supply chain that we are talking in the order of cents per litre, not, you know, point of a cent per litre or something like that.

COMMISSIONER LINDWALL: Yes.

MR ABRAMS: So we would see those benefits, potential benefits should be material and should flow into the millions of dollars for overall jet fuel costs for individual airlines, but as I said, to actually have that information you'd need that directly either from an airline or a supplier because as I said, BARA strictly doesn't get any commercially sensitive information.

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COMMISSIONER KING: Just to follow up on that, of course, BARA did the application to the NCC for declaration Sydney 2012, I think, around about that time. You gave similar information to the NCC that we've received based on the IATA data and the NCC said, well, it's less than convincing that there's a problem, and in fact obviously some other parties got some consultants to do some work breaking that down in the consultant report, and most of it is public; basically came to a conclusion that any price differentials could be explained by differences in taxes, transport costs and so on.

So we haven't received anything different and that puts us in a very difficult situation in that, we're sitting with the same data, but the NCC's already said it didn't show a problem, or wasn't sufficient to show a problem, I think is a better way of putting it. How do we find a problem?

MR ABRAMS: Yes, I think there's, from BARA's perspective, I suppose there's a couple of aspects to this. One is, obviously that represents a build-up of the costs as per the existing suppliers of jet fuel, so an alternative supplier may, for argument's sake, be able to achieve economies in, say, shipping, and it may be able to achieve economies in the areas of the supply chain itself. So it depends whether or not you think that evidence put forward actually represents the most efficient supply of fuel versus what a new competitor may be able to provide.

From BARA's perspective, so in terms of the problem, it's obviously been raised by members on many occasions around the lack of competition and the lack of competitive tension on their bids when they tender for fuel, and I would note the NCC did make the finding, regardless of how we got there, that they did not consider the supply of the market for jet fuel at Sydney Airport to be vigorous or competitive, so that's the important finding too.

In turn, I think, and I appreciate the difficulties here because a lot of data in this type, this part of the industry is just locked up, but BARA has also met with many potential fuel suppliers over a number of years who have come to BARA and said, "We really believe we can bring a more efficient product and service to the airlines if we had the opportunity to come into Australia and compete in these markets".

So when at the same time I've got members saying there are problems, and I have potential importers saying, "Well, we really think we can come in and bring some real efficiencies here", that's something we continue to sort of push forward on, but I certainly note your point that the lack of - and we mentioned this in our submission - the lack of information and data within the jet fuel supply chains, there's not much about.

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COMMISSIONER LINDWALL: Now, under Part 48 or section 48 of the Productivity Commission Act there's a provision which allows us to use powers to obtain information. Would you think that we should do that, and if so who should we ask and what should we ask?

MR ABRAMS: Okay. Obviously being from the Commission, and your background, you'll obviously have a view about what sort of information would give you, if you want to know what is the problem, so then the question then is, what information would you like.

So two forms of information that I would think would be useful would be to understand that each of the four major airports, what is the volume of supply being supplied by the participants at the airport, so that would at least give you a feel for the level of market concentration, and I think especially for, say, Sydney JUHI, an understanding of if and how many times a potential fuel supplier has come to the JUHI and sought access to those facilities for the purposes of competing and what the outcomes are - were.

So perhaps there's some quite simple information that could be asked for that would be readily available within, you know, the JUHI's around the country at the four major airports.

Now, we've obviously heard from in the submission with regards to Melbourne JUHI that as soon as they moved to an open-access arrangement in their view, they've had interest and they're processing applications. So hopefully by the time of the draft report or soon after we'd actually know the outcomes of that. So in terms of trying to look at both parts of the spectrum, so I understand in terms of what would be the benefits.

Now, if at the end of the day new providers can get access on some reasonable workable terms, then the market will just determine that, you know? If there's still only two providers in the future, that then just suggests, well, that's what the market will bear and that's the go. If we saw an increase in the number of suppliers, then that's not a bad proxy for saying we've had a general increase in the level of competition.

COMMISSIONER LINDWALL: On your declaration that Stephen mentioned, and I think you applied for it in 2011 and of course it was determined in 2012, things that have happened since then, would you ever consider reapplying to the NCC for a declaration?

MR ABRAMS: Unlikely. The reasons, I think, are as follows. One is, in discussions with potential fuel suppliers through a long period of time, one is, we would need to go through the process again. One thing that we learnt

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was that airlines and providers can be reluctant to come forward with information on the public record as you're probably also experiencing here at the moment.

COMMISSIONER LINDWALL: Yes.

MR ABRAMS: Just that's the way this industry tends to work.

Secondly, in some discussions we've had, we've then put it forward to say, "Well, even if we get access, we get it declared, it's still then up to a potential fuel supplier if they can't reach the terms, acceptable terms and conditions, to then go through an arbitration process which could be then through the ACCC and then potentially the Australian Competition Tribunal, and I think a very firm view that we keep getting put forward to us is to say, hang on, we want to cover this country and compete and supply fuel and bring efficiencies. We don't want to have to fight our way through regulatory or legal systems, or through arbitrations to achieve it. Why can't we see the same situations that we see as we've put in our submission at, you know, Hong Kong and at Warsaw and at LAX and, you know, where workable arrangements are in place.

So even if BARA was to push forward again, which obviously has no certainty to it, it's not clear if they're actually going to fully deliver the outcome for the pool who want to potentially use it.

COMMISSIONER LINDWALL: So when you look at reform in this space, obviously we'll start with Western Sydney Airport, the government's deciding to build that. Obviously your position would be that it should be open access from the start.

MR ABRAMS: Yes.

COMMISSIONER LINDWALL: And continue to be open access.

MR ABRAMS: Yes, I think the most sensible arrangements there would be the on-airport storage and distribution facilities could be owned by the airport itself, the company if it wanted, and it could then just tender out the running of those operations to a specialist fuel provider, or there could be some hybrid where a fuel supplier - sorry, a provider of those infrastructure services, more correctly, also has invested in those facilities as well, but either way, we would see that as a very clean and straightforward opportunity to bring in an open set of access arrangements for Western Sydney Airport.

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COMMISSIONER LINDWALL: And now the government's also announced that ultimately its intention would be to privatise Western Sydney Airport. What would you want to ensure that when it happens, a long time in the future, presumably, that it remains open access.

MR ABRAMS: Okay. I think we would - you would therefore specify that as part of any lease conditions for the purchaser of the airport, so the part of the lease conditions as I understand now for the major international airports is around, you know, facilitating aviation and investing in infrastructure and the like. So you could imagine or envisage a situation where they've built in a set of lease requirements that, "Here are the standard terms of access for the facilities, and it is part of the lease requirements to be maintained through time".

COMMISSIONER LINDWALL: Yes.

COMMISSIONER KING: Can I just follow up on that on different forms of access, so when you're talking about access I understand you're talking about as in your submission, non-discriminatory access without requiring an equity buy-in.

MR ABRAMS: Yes.

COMMISSIONER KING: Now, if we talk to people from Sydney JUHI I suspect they would say, "Well, we have access. It's an equity-based access". What's wrong with an equity-based access thing where anybody can get access to the JUHI and related facilities as long as it buys into the relevant company.

MR ABRAMS: Certainly. BARA's not opposed to equity access type participation as one option. There's probably a couple of things that come to mind. One is, if a fuel supplier is just seeking to see in the early days whether or not it can actually establish a market, grow its market with airlines, then having a non-equity form of participation can be a lower risk, lower cost type operation where they just pay a fee. They might operate some, you know, trucking services to the airport and basically see how they go. The issue that seems to be at Sydney, and obviously Sydney JUHI and Sydney Airport will know far more about this than BARA, but according to what we've seen with regards to the access declaration is that Sydney Airport can terminate the lease within three years' notice.

So if you were to buy into these facilities, depending on what the outcomes were when the lease was terminated, it might be you've got a substantial risk and you buy into the facilities. Then there's a notice that says, "Sorry,

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you're out in three years' time", and you may or may not know what you're going to get out of that.

So it's not that equity participation is streamlined, entered into and applied in a good faith nature with a sufficient tenure could not work, but that's not what we see at the moment, and having the two forms options available to people would seem to be a much preferable situation.

COMMISSIONER LINDWALL: You've spoken of what the Victorian Government has done to promote a forum and a bit of consultation. What would you like the Federal Government to do at the minimum.?

MR ABRAMS: Yes, so at a minimum, what we've asked for is what we would like to see, is the Government invite each of the JUHI operators to submit some standard terms for workable access to their facilities for some review and comment by industry members. So this very much still says it's the JUHI's or whoever is the owner/operator of those facilities. They are responsible for the provision of pricing of those services, but we think by simply requiring some transparency and some consultation with industry that we can actually get some sensible arrangements in place. So that's one part.

The other part is, in effect I think what we're asking for is the Australian Government to effectively implement a form of master planning for jet fuel supply at the four major airports, whereas, as we've done in Victoria, we have an external party come in and help, and that there's a proper end-to-end review done of the supply and demand of jet fuel at the airport, and then that, as you would expect in an airport master plan, then starts to raise all the issues of where the augmentation may have to happen. Are we in a pretty comfortable place? Do we have obvious problems coming?

As we would see it, given the various parties on the table, so we've got an airport, we've got various fuel suppliers, infrastructure providers, some form of oversight is necessary to bring us all together to actually conduct those types of studies, and that was done in, I think, in quite a collaborative and good way for Melbourne Airport.

COMMISSIONER LINDWALL: And it doesn't require legislative change or new regulations or anything like that?

MR ABRAMS: No. No. Nothing BARA has put forward in its submission points to a fundamental need of, say, a legislation change. Our view is, as I suppose I pointed to early, we think the changes necessary are actually pretty modest and well within the capabilities of industry today if they're just given an appropriate prod, so to speak, to get there. We don't

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envisage especially in the first instance there would be any need for any type of new legislation.

COMMISSIONER LINDWALL: So if it's all so modest, I would ask why hasn't it happened already?

MR ABRAMS: Because it's not in the interests of the parties in question to implement.

COMMISSIONER LINDWALL: There's a mutual gain here between airports and airlines perhaps.

MR ABRAMS: Yes.

COMMISSIONER LINDWALL: Of course there are lots of things that they're not in the same interest.

MR ABRAMS: Yes.

COMMISSIONER LINDWALL: But your interests are pretty well aligned I would have - apart from the fuel, the levy that's at Sydney Airport, but in other things you both have a mutual gain, I would have thought, in reaching this, and if they're so modest it's still quite interesting that it hasn't happened.

MR ABRAMS: Yes, it's certainly perplexing. As I said, we look at Sydney Airport seven, eight years ago, you know, modest, sensible investments to help the level of competition and reliability and supply through the bridger facilities have all been identified and known, yet we haven't seen anything. We've spoken obviously to Sydney JUHI and Sydney Airport and many others, and we've written to the parties saying, "Please produce a sensible infrastructure plan.

COMMISSIONER LINDWALL: Yes.

MR ABRAMS: and produce some workable access arrangements". This isn't that hard, but yet we don't see it. You know, obviously these are decisions and negotiations going on between the parties. We at the moment just sit back kind of in frustration and somewhat shaking our head at the lack of progress when, as you said, these aren't particularly difficult initiatives to employ.

COMMISSIONER BAXTER: What's the response that you get when you make that approach that you've just described.

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MR ABRAMS: I think, in terms of when we've written to Sydney JUHI in the letter we gave to Sydney Airport we didn't receive any official response. I think as I've seen in a submission from Sydney Airport they say they're supportive of trying to improve the level of competition. It may well be that Sydney JUHI is neither adverse to opening and creating some workable access arrangements, but we don't actually just see any progress in practice. So what is actually going on between the parties is something that we don't know because we're not a party to it, but we do hear statements that everyone is not in disagreement with what BARA has put forward and needs to be achieved. It just is, we just don't see it being achieved.

COMMISSIONER LINDWALL: Do you think that Qantas being a member of the Sydney JUHI makes a difference with respect to the reforms that have happened in Melbourne?

MR ABRAMS: It's difficult for me to comment because that's not something that BARA has information on.

COMMISSIONER LINDWALL: Okay. Ken, do you - I've got more questions but I thought I'd give my colleagues a bit of a chance to ask some questions.

COMMISSIONER KING: I'm a bit like you, Paul, I scratch my head and say, "Well, why aren't Sydney Airport, their incentive to having airlines paying too much for their fuel", but - - -

COMMISSIONER LINDWALL: Barry, you have answered that and you said you don't know either, so.

MR ABRAMS: Yes, you'd need to go the parties in question.

COMMISSIONER BAXTER: The only query I've got is, are there any more complex and not necessary transparent relationships between some of the oil companies and JUHI owners, and the controllers of the various pipelines that go around Sydney. Having had a little bit to do with them, you know, the roles I've played, they were always very difficult to do, and the relationship that NSW Government didn't have with Shell and Caltex in particular in the run-up to the Olympics, and the requests that certain of the tankerage be removed because of concerns that some of the Olympic participants, including the Israelis and the Americans, and about the proximity of those tanks to some of the grounds. I'm always trying with that to peel out and find out what's the part of the onion that you're really looking at, what is the thing that determines what should be, prima facie, a

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straight relationship between a fuel supplier, storer and then on seller and the airlines who use.

MR ABRAMS: Yes, I think that's exactly right. From BARA's perspective, given how we operate in quite an open and transparent manner, and how we work with our ACCC authorisation, we're obviously not getting down to that level of detail to know exactly what's going on. So we're sort of sitting one level back and saying, "Look, you know, members are raising concerns. Potential providers are telling us that there's opportunities here". We see between Sydney JUHI and Sydney Airport there seems to be no progress on these matters and maybe there has, but for us there's been - we can't see any new lease arrangements. Perhaps it then is open to the Commission to try to find out more, to write to Sydney JUHI and Sydney Airport to better understand the basis of what is going on.

COMMISSIONER LINDWALL: Could I ask, Barry, about, have you considered another avenue which is that under the Competition Consumer Act the Minister can instruct the NCC to conduct the - - -

COMMISSIONER KING: Yes, so the Minister can seek declaration, it doesn't have to be an outside part of - - -

MR ABRAMS: We could, but as I said, in the first instance what we've sought to do through this inquiry and first through the competition policy review is, look for almost the smallest and the lightest touch necessary.

COMMISSIONER KING: Yes.

MR ABRAMS: But certainly there should be no reason why if, within a reasonable timeframe, we don't see some of these quite sensible and straightforward arrangements in place, then that could well be something then that the Commonwealth says, "Well, look, if you're not prepared to get on and do the things that you need to do, then these are the acts that we'll actually get on with", which is a very nice threat that clearly doesn't require any new regulation or legislation.

COMMISSIONER LINDWALL: Now, what can you tell us about your members in terms of the types of contracts they have with the JUHI and how long they last and what type of circumstances they might want to change from one provider to another and so forth?

MR ABRAMS: Okay. As I would understand it, what members have are contracts with fuel suppliers, not the JUHI.

COMMISSIONER LINDWALL: Correct.

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MR ABRAMS: So the JUHI is an input service.

COMMISSIONER LINDWALL: Yes.

MR ABRAMS: Who in theory at least are separate from the suppliers of the fuel, so the supplier of the fuel will have a contract with, or an agreement with JUHI. Airlines are then just tendering and purchasing the final product, and I understand that most international airlines look to structure tenders for supply for about one to two years. as a general rule, and then that kind of allows one opportunity for them to perhaps find a different supplier, and two, you know, have there been any sort of changes in the market, but generally, as I would understand from most of my internationals, they're running on, you know, one to two to maybe three years.

COMMISSIONER LINDWALL: Okay.

COMMISSIONER KING: Can I just check, so the contracts are essentially for the supply, so that includes the into-plane servicing or services?

MR ABRAMS: That's a good question. I would understand that the supplier of the fuel will also have the contract with the inter-plane service provider and that the airline itself is behind the final product, at least for a sort of standard international operation.

COMMISSIONER KING: Okay, and the contracts are for one to two years. If you know, do they tend to be exclusive or can the airline say, "Ah, well, I can get a better deal on this day at the Sydney Airport so I'll go with that".

MR ABRAMS: Yes, as I would understand it, they tend to be exclusive for the time period, so if you were three suppliers and I was an airline and, say, "Right, you've won the tender and you'll be providing the fuel for the next couple of years until it comes around again to put out". You do have some instances of what we call part supply so that's where an airline might get some of its fuel from one supplier and some from another. At times that can be advantageous to an airline, but for most international airlines in operations into Australia the preference sits with 100 per cent supply from one supplier so you're not trying to dual manage two suppliers over the course of the operations.

COMMISSIONER LINDWALL: I wanted to ask, and I alluded to this at a coffee break earlier, about the IEA's effectively policy that there should

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be 90 days of supply and I think that the average is about 20 days in Australia. What do you think of the 90 days, is that too high or is that a reasonable objective?

MR ABRAMS: I think there's a few parts to that analysis. So the first is what level of storage should you have appropriately on the airport which is, in effect, your ability to manage supply disruptions up the supply chain.

A number of three days' supply is often bandied about. Now, at the end of the day that level of stockholding should be done with regards to an analysis of both how resilient your supply into the airport is, and secondly the ability of airlines to actually manage supply disruptions in terms of tankering and the like.

Then when you come to the, sort of, the off-airport storage, I don't have exact figures but my understanding is it's normally perhaps a couple of weeks, so we're not talking three months.

COMMISSIONER LINDWALL: No.

MR ABRAMS: That's an awful lot of storage tanks to have with fuel in them.

COMMISSIONER LINDWALL: Yes.

MR ABRAMS: It would be far better to be using that sort of resourcing and funding to ensure that you've got a very resilient supply chain and a good, diverse set of supply routes to the airport because that's likely where you're to get the most benefits in terms of reliability and supply, rather than just more tanks at the airport or off airport.

COMMISSIONER LINDWALL: Well, you did see the disruption that's been caused, say, in Auckland.

MR ABRAMS: Yes.

COMMISSIONER LINDWALL: Or as you alluded to earlier in Melbourne. It can cause significant obviously problems, Auckland being a classic case.

MR ABRAMS: Yes. So you could have significant storage facilities off airport, but if the pipeline breaks down between those facilities and the airport, well, it doesn't matter how many tanks you've got out there for jet fuel.

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COMMISSIONER LINDWALL: We've got a testimony from Bioenergy Australia about biofuel.

MR ABRAMS: M'hmm.

COMMISSIONER LINDWALL: Do you have a comment about that, any aspect of that?

MR ABRAMS: So biofuels is currently a small part of supply, and I think just reading from some IATA documents, you know, we're potentially looking at, you know, 5 per cent plus in terms of biofuel. We would like to see the opportunities for biofuel simply to be put on the same level playing field as per, you know, standard jet fuel. Obviously with things such as capping the carbon emissions from international flights from 2020 through their CORSIA scheme, through IATA, that may create some opportunities for, you know, carbon offsets and the like through biofuels.

So for each airport as I suppose we would see it with the JUHI you would expect the service standards that you set also have a view as to how they can handle and distribute biofuel out to the aircraft and what facilities are in place. So again it should be part of the mix and part of the potential options put on the table.

At the moment, you know, BARA simply wouldn't know the ability of each JUHI to be able to do that. There's not enough interaction between the parties for BARA to have - to be able to form a view as to whether or not it's capable today, or if there could be capability in the future.

COMMISSIONER LINDWALL: Ken?

COMMISSIONER BAXTER: No, I've got no more.

COMMISSIONER LINDWALL: I think we've - I can't think of many other questions. I mean, basically you're arguing for obviously a more open arrangement, whether it be through equity or pure open non-equity participation; greater transparency; a bit of a consultation forum or some sort like that where each of the different airports to look at future investment and needs and so forth. That's about it, really, isn't it? I think so.

MR ABRAMS: I think so. Yes, we've - I mean, BARA's view is, we want to keep this as commercially and as market driven as possible, so we've just tried to focus on those key aspects of the market that have been brought to us by, generally by potential fuel suppliers to say, "If we can create some improvement in these areas, then we think that will unlock our opportunity to start investigating our ability to move into these markets".

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So BARA is certainly not saying that, you know, we need to see a guarantee in the level of competition or the number of suppliers. We're simply saying we'd like to see some, what are relatively straightforward adjustments and improvements that will just simply let the market determine the outcome.

COMMISSIONER LINDWALL: Okay.

COMMISSIONER BAXTER: Perhaps the only query I've got, and it's probably a bit outside this is, how much then is the influence of the oil companies tankering, that is, shipping tankering from Singapore predominantly and part of the Middle East to Australia, dictate the way in which it behaves in terms of access or providing jet fuel?

MR ABRAMS: I don't pretend to be any expert on shipping, but it is true that there are economies of scale in larger ships, and therefore there may also be economies of benefit if there are - there could be on a particular ship fuel from multiple suppliers.

COMMISSIONER BAXTER: Yes.

MR ABRAMS: So effectively that Certainly the economics of the shipping is really important to the market dynamics, and that's why we think having both Sydney and Melbourne open as the two biggest markets is quite critical because that's what's going to give you the biggest volumes with regards to shipping efficiencies, and then if you sort of, if we've got improvements in Sydney or Melbourne, that has more opportunity then to cascade to, say, Brisbane and Perth where the fuel volumes are obviously much lower.

COMMISSIONER BAXTER: Okay.

COMMISSIONER LINDWALL: Well, thank you very much for appearing today, Barry.

MR ABRAMS: Thank you.

COMMISSIONER LINDWALL: Now, we've got out there something to eat if you want, so do you want to grab something really quickly and a coffee, and then we can work out whether the AAA or Bioenergy testifies first because it could be either. Can we just grab a quick cup of coffee if you want. You don't have to, but I think it's been paid for so you may as well use it.

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SHORT ADJOURNMENT

DR MUNDY: Thanks, Paul, my name's Dr Warren Mundy. I'm the Chief Economist of the Australian Airports Association. As the Commission will be aware, Australian Airports Association is the Australian industry association representing all airports in Australia from our largest member, Sydney Airport, down to regional and remote aerodromes in indigenous communities throughout the country.

Commissioners, I'll briefly make some opening statements, of course, and they'll probably be a little bit broader in their scope than Mr Abram's observations because, of course, jet fuel is also required in the domestic aviation market as well as international markets.

I think it is fair to say though as we expressed in our submission to the commission that Australian Airports Association broadly endorses BARA's stated objectives with respect to fuel supply. I think we'd make the passing observation that concentration and questions about market efficiency in relation to petroleum products more broadly in this country are nothing new, and obviously issues of concentration and increasing concentration and reduction in refinery capacity are significant questions.

I think it's important for us to start thinking about why we're actually concerned about fuel issues. Fuel constitutes a substantial part of airline operating costs. In our submission, the primary submission to the Commission in Figure 2.1 we show IATA data for, I think, 2017 that showed fuel and oil was about 26 and a half per cent of operating costs. Airport charges were 6.2.

So we would have thought the policy concern with fuel should be about four times the policy concern with airport charges, but that appears at least not to be the case with respect to domestic airline advocates.

In Figure 2.8 in our submission we provide some data which is publicly available data which is a chart that we sourced from Moody's Investors Services that shows when fuel costs fell in Australia - sorry, when fuel costs fell by about 60 per cent in financial year 2015, there was no change in domestic air fares as a result, and indeed, when they fell by 50 per cent, although obviously from a lower base, in financial year '16, there was again no change on domestic air fares. If anything, domestic air fares just continued a gradual drifting trend upwards.

Interestingly, late in 2017 there was an increase in domestic air fares associated with an increase in fuel prices, and it will be interesting to see as

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the BITRE data becomes available for the back end of this year whether the recent reductions in fuel prices led to a reduction in domestic air fares.

We say this largely to suggest that the primary concern with fuel prices is not about air fares, at least in the short run, maybe in the long run, but that requires a much more detailed econometric analysis which is virtually impossible to undertake for the reasons which Barry outlined before - because it does actually require information about not only internal cost structures of individual carriers which will differ in the market they are working, obviously fuel becomes a relatively larger proportion of airlines costs when airlines are operating on longer routes.

But as we've indicated in our primary submission, we think the evidence of a relationship between any component of airline cost structures with air fares is passing, and I think the difficulties in understanding these relationships are well evidenced by the Parliamentary report that came out of the Legislative Assembly in Western Australia, and also the, I think the challenges that the Senate Rural, Regional and Transport Committee is having in its inquiry to regional air fares getting to the bottom of some of these issues.

It is probably the case also that trying to associate movements in fuel prices with at least short-term trends in air fares is difficult because of the presence of very complex and sophisticated hedging strategies within airlines which may indicate that there should be, that may indicate that there will be significant lags between fill price events and hedging.

But that said, we do think fuel prices are important. They're clearly important to airline profitability, and Australia having profitable airlines is important for the Australian community. I had the experience of many years ago being an airport executive at a point in time when we had a very unprofitable airline in Australia. It was called Ansett. That caused substantial disruption to the Australian economy and probably led to the suicide of 16 people.

So profitable airlines are important, and the market thinks they're important. We've seen a report in the Canberra Times only this week that Qantas' share price increased by around about 10 per cent in the last month, largely off the back of improvements in the price of fuel. The report suggests that Qantas is working off a long-term fuel price of around about $US130 a barrel and on Monday the price was around $83 a barrel.

Secondly, and probably in my mind of equal importance is that it is not only the price of fuel, but also the security of supply, and this is, I think, what's motivating the government including these matters in the terms of

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reference, and really there is a short-run issue and a long-run issue. The short-run issue is, as we witnessed in Melbourne recently and in other places from time to time, when fuel goes short for some reason, perhaps because the supply chain lacks resilience, planes get cancelled, people are inconvenienced, airlines have got to undertake tech stops and it's all no good for anyone.

However, in the long-run there are also concerns. The first is, of course, if you have a lot of those sorts of events, individual airports, and potentially over time, our nation becomes seen as an unreliable place for international aircraft to operate, airlines to operate too. That will affect competition, particularly in the international market where we know competition is much more intense than what it is in the domestic market.

Entry is vigorous, it is vibrant, and fuel is an important part of that, and I think the evidence that Mr Abrams has given about the way that airlines contract is, is that without fuel, without certainty of fuel supply from a supplier, entry is going to be challenging, and that's the second point. We need to have a fuel system which is able to expand in accordance with demand from the market.

We do not want circumstances whereby an airline wishes to operate to a major Australian airport, but because of capacity constraints within the fuel supply cannot get certainty around fuel, either be it to offer a seasonal service which may occur, for example, around Chinese New Year, or alternatively to establish services on an RPT sort of basis.

So we are particularly concerned about that because there is, in our mind, and you no doubt have picked this up, a very different competitive environment between domestic airlines and international carriers and their ability to get access to fuel and those sorts of things. So that's what we think are the important community and economic outcomes that we see at the end of the day.

Briefly, the role of Australia's major airports in the supply chain was largely determined in the run up to the privatisation process when the JUHI arrangements were, if not put in place, certainly reinforced. Diligence was undertaken by the Commonwealth to clean some of these contracts up and it basically, the idea was that the JUHI's, which were the major fuel companies, would rent the site from the airport, and the airports and those rents would be ratcheted up from time to time in accordance with the market rates like most FAC leases were, and that there was also provision in those JUHI arrangements with the FAC to impose a fuel throughput levy.

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There is no doubt, and the Commission understood this in inquiries in 2001 and 2006/7, that the Commonwealth held out to bidders that fuel throughput levies were an additional source of revenue which they may levy after privatisation.

Now, the Commonwealth said no more or no less than that. It was a simple statement of contractual right, and indeed, a number of airports imposed those fuel throughput levies, and the imposition of fuel throughput levies was a matter of some contention in the first airports inquiry.

As Mr Abrams mentioned, Melbourne Airport has had a long tradition of not imposing fuel throughput levies, even though it possessed those rights. Other airports, notably Brisbane and Perth, did, although it has to be said that in relation to Brisbane Airport an independent arbitration conducted by - well, a determination I think it was, to be fair - conducted by senior counsel found that the level of the levy to Brisbane imposed was not unreasonable in the circumstances. I think at the end of the day, the question about throughput levies is about how big they are and what is the mechanism in which they're set.

Since then, and obviously not all airports where jet fuel is uplifted in Australia will be operated by the FAC. Cairns and Mackay are two obviously in mind, but obviously also increasingly now in airports in the Pilbara where the case is that the fuel's actually shipped into Port Hedland and distributed by road train around the airports in the Pilbara that require uplift.

What has happened over time, though, is that the models under which, particularly the fuel infrastructure on the airports, have changed, and they've tended to have changed when an airport has undertaken a major reconstruction of its apron infrastructure.

The reticulation network essentially sits below the apron, and what we've seen when airports have had to rebuild their aprons, as was the case with the terminal redevelopments in Adelaide and Canberra, that the airport has taken more responsibility over the hydrant infrastructure than was the case under the JUHI arrangement. I think simply, because it is an integral part of the apron infrastructure, and over time there is a need to relocate the hydrant points, it just is easier to take one participant in the discussion out.

The charging models are different. There are some models whereby the hydrant infrastructure really just becomes part of the apron and you never see a price attached to it. There are other examples where it might be funded transparently by some sort of fuel throughput levy. Again, none of that's right or wrong. It's all sort of pretty reasonable. Price signalling in that

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sort of environment is pretty weak, thinking about demand. It's just people come to different arrangements.

We, as you'll hear no doubt on Friday, from Ian Kew, Darwin is in the process of acquiring the entirety of the JUHI. BARA's provided examples of Hong Kong where the airport runs the JUHI infrastructure effectively on an open-access basis.

There are examples, though, in Europe where the airport itself becomes the primary provider of fuel at that airport, so they attend not only to the infrastructure in its delivery to the aircraft, but they also procure it, effectively retail it to the airlines and also attend to its transport from the refinery or the wharf to the airport site.

That's really what the role of airports is and can be. There are obviously other issues. I mentioned concentration in the refining and effectively retailing to airlines part. There are issues about carriage of the fuel to airports. Trucking is common in Australia. Trucking is common to major Australian airports, and there is a real and legitimate question about the safety and environmental issues associated with the trucking of large amounts of fuel through metropolitan areas.

Obviously there are issues with the storage safely of what are hazardous materials, and other issues, but they are not really matters that my members, other than as a participant, and perhaps a facilitator have particular control over. Although I think it is fair to say that those who invest in airport infrastructure more broadly have from time to time talked about setting up a wharf and building a pipe, owning the infrastructure from go to whoa, and there are specialists; and I think Mr Abrams alluded to this, there are specialist investors who seek to own and invest in this sort of infrastructure and then typically the business partner provide the operations around that, but we haven't seen that sort of market development in Australia, I think just because of the predominance of the existing legacy arrangements. So that's really all I have to say.

COMMISSIONER LINDWALL: I appreciate that. Could I start by asking, in your comments you mentioned about the privatisation back from the FACs. Thinking of Western Sydney Airport, what different process should be taken if that gets privatised ultimately?

DR MUNDY: I just need to be careful because I have advised the Commonwealth on these matters, and I have certain confidentiality obligations to the - - -

COMMISSIONER LINDWALL: Yes.

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DR MUNDY: Commonwealth which I suspect are enduring. Obviously Sydney Airport, when opens, Western Sydney Airport, or Badgerys Creek as old people like me call it, when it opens will be a relatively small airport, and by that I mean a few million passengers a year, but it will grow over time.

So there are a few issues. One is, how do we get the fuel to the airport, and as I indicated, and I said this, I think it is difficult to see a sustainable circumstance whereby large amounts of fuel is going to be trucked to Badgerys Creek, so it will either have to be brought from, well, probably have to be piped from Kurnell maybe, maybe Clyde but probably Kurnell. So obviously an easement needs to be acquired and preserved for whenever that's required, and obviously then the pipeline infrastructure is going to have to be financed somehow.

I think it would be an error, and this is not the AAA's view, this is my view personally, but I know a bit about it. I think it would be an error to permit the current market structure that we see at many major airports duplicated at Badgerys Creek.

COMMISSIONER LINDWALL: Okay.

DR MUNDY: The Commonwealth has an opportunity to fix this. There were many things done in the run up to privatisation for Phase 1 and Phase 2 airports which sensible people acting reasonably at the time did, but 20-odd years on you wouldn't do it again, and those arrangements were there and they were convenient at the time, and you know, our airports 20 years ago were processing half the numbers of passengers they are.

COMMISSIONER LINDWALL: Yes, exactly. All right. Now - - -

COMMISSIONER KING: Let me just follow up on that because you mentioned trucking in your opening comments. Wouldn't any situation, you know, let's imagine that the JUHI is owned by the airport or some other common access arrangement or whatever's put in for Western Sydney Airport, as you said, the pipeline is most likely to be an extension of an existing pipeline, or that's my understanding. How do you get round the pipeline being a bottleneck, or do you see it being again a separate open-access pipeline? So it would actually be completely a new pipeline?

DR MUNDY: Yes, well, I'm not, Commissioner, I, with respect - - -

COMMISSIONER KING: No, no, but - - -

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DR MUNDY: I'm not sure that substantial new pipeline infrastructure will not be required.

COMMISSIONER KING: Okay. And you'd see that being - - -

DR MUNDY: I mean, there is an issue of supply security, would you build one pipeline or two?

COMMISSIONER KING: Yes.

DR MUNDY: The answer to that is, you'd probably build one. You'd rely on trucks in emergency and, then at some point when it gets sufficiently large you'd build a second pipeline.

COMMISSIONER KING: But in the easement that you would seek from the government, it would probably be for two pipelines but you might only build one?

DR MUNDY: You'd seek an easement that was sufficiently wide to - the question is would - and it would depend ultimately on how the storage facilities at the port were to develop over time, but you could see two pipes running down an easement to somewhere in Botany Bay. That would be the sort of thing.

The laying of these pipelines, as you would appreciate, given all that is going on with development, road infrastructure and also rail infrastructure in metropolitan Sydney is quite challenging, and obviously this is a hazardous material that we're transporting here, so it's got to get there somehow, and I suspect a pipe is less hazardous than truck. I just see the corporate affairs impacts of a truck turning over on a road on its way to Badgerys Creek is pretty, you know, pretty horrible.

COMMISSIONER LINDWALL: You heard from BARA about the type of government actions that have happened, say, in Victoria and what they think the Federal Government should do. What do you say to that and what type of actions would you recommend the government take as an AAA representative?

DR MUNDY: I'm not in a position to make any observations about what has occurred in Victoria and you would be better to put those questions to Melbourne Airport.

COMMISSIONER LINDWALL: Yes, we will.

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DR MUNDY: It seems to me that if airlines are particularly exercised about the issue as a provision and planning fuel supply to Australia's major airports which are subject to regulation under the Airports Act 1996, they need only to actively participate in the master planning process which airports by dint of law require them to be consulted and raise these as substantial and serious issues because once they are raised as an issue in that process, the airport, under the Act, is required to respond to those concerns that are raised, and provide that response to the Minister in consideration of the approval of the master plan.

So the mechanisms already exist, so I don't think there is any need of legislative action. I think there is, of course, with these sorts of approval process as the Commission is well aware from its own working major project approvals that there is always an element of discretion available to decision-makers and in setting up these processes it would be - it would not be controversial for the Minister to indicate via his or her department that fuel provision is now one of the things we expect to be covered in the master plan.

If you pick up an airport master plan and compare it to the statutory provisions contained in the Act, you will find many, many more things in the master plan than are specified in the statute, and my observation would be, having probably only been involved in about a dozen airport master plans around the country, a lot of that material's incorporated at the behest of the department.

So it may well be appropriate for the permission in regard to this planning issue, which I think is a fair and legitimate proposition to make a recommendation that perhaps the Minister could indicate that in future fuel should be one of those matters which is relevant to the primary development of civil aviation at the airport, which is one of the objectives of the master plan that is set out in section 70-something there.

COMMISSIONER LINDWALL: What about the non-transparency of the contracts and the arrangements of the JUHI's in the airports, do you see any need or mechanism, or should the PC, for example, use its powers to try and obtain some information about some of these matters?

DR MUNDY: I'm just thinking carefully as I have actually read a few of these contracts. The Commission should always use its powers in pursuit of its statutory purposes and that's a matter for the Commissioners, and I know it is a difficult and weighty matter, and I know that the Commission only ever does so with a heavy heart, it prefers people to be open and transparent.

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I don't think you're going to learn very much that you don't already know. There's a lease, there's a bit of land that the tanks sit on. There's a licence to operate a hydrant network. There's a right to impose a fuel throughput levy. There's a truckload of boilerplate clauses that go to things like GST and stuff like that. That's what was broadly in the contracts which were in place when the airports were privatised.

The Commonwealth can give you those contracts, Commissioner, because it's a party to them. They're pretty much all the same.

COMMISSIONER LINDWALL: Yes.

DR MUNDY: Now, obviously as time's gone on there are new arrangements with Melbourne Airport which we, the AAA, are not privy to. I know that various of your members have taken the Commission on good faith and provided them with contractual material on a confidential basis, and I know that's the way the Commission always prefers to proceed.

COMMISSIONER LINDWALL: Yes.

DR MUNDY: I would hope that our members would be generally disposed to being of assistance to the Commission, but ultimately that's a matter for them, and the undertakings they've given to others.

COMMISSIONER LINDWALL: Okay. No, that's fair, so it's a very circuitous type of response, though, but that's good. Stephen.

COMMISSIONER KING: I want to come back to Sydney and the fuel throughput levy and Sydney's incentives, so you may end up responding to these by you have to ask Sydney. Two elements. Let's start off on the throughput levy, and yes, airports are allowed to put in place throughput levies, and I think Brisbane was the first one to do it, off the top of my head.

DR MUNDY: Brisbane imposed a levy, I think, of .4 cents a litre across the board and Perth imposed a levy of .5 cents for internationals only, and they did so somewhere around 1998, 1999.

COMMISSIONER KING: Yes, I think on day one of the privatisation of Brisbane Airport or - - -

DR MUNDY: I'm not sure of the dates, Commissioner. They certainly did - - -

COMMISSIONER KING: It was very rapid.

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DR MUNDY: They certainly did it in the period indeed where their return on assets at Brisbane Airport was negative.

COMMISSIONER KING: Yes.

DR MUNDY: And that was revealed in the ACCC monitoring reports.

COMMISSIONER KING: So understand that there may be some post justifications for throughput levies because things have changed over the last 20 years since they were initially imposed but if parties put to us that these throughput levies are really just a back door way of raising the fees, the charges to the airlines, but in a sense, you know, it's a way of raising those charges that is perhaps a bit hidden, a bit less transparent to the public, a bit less, you know, not in the headline rate that gets quoted and that it would be better if those throughput levies were eliminated and that may lead to an increase in the headline airport landing and departure charges. So what would be your response to that?

DR MUNDY: Well, my first response would be, I very much doubt that the travelling public has any idea what constitutes the airport taxes and charges box that is on the - that is - used to be on the ticket. It's now somewhere down the right-hand side on the screen. We know that they don't represent what is charged by an airport to an airline for any of (indistinct) and I get that. That's - so let's put this transparency to the public to one side because it's just another component of a blanc mange of this.

Fuel throughput, and I think I may have argued this in a submission to the Commission many, many years ago, that they can be seen as a payment in the form of rent. It is effectively a payment for access to run the hydrant network across the airport. I'm not necessarily - so the question then is, what's the efficient level rent extraction, and certainly in a determination, as I said earlier, at Brisbane Airport, senior counsel looking at the relevant agreements found that the levy at Brisbane Airport was not unreasonable.

There are cases where, and I think this may well be the case in Canberra Airport, that the hydrant, the setting of the levy was in the context of new infrastructure being built for the terminal involved. So the question then becomes - I think that's a different question. I think if it's associated with the development of infrastructure, I think that's the question and that then really becomes, well, is that the best way to charge for that infrastructure in the context of that development? That's a matter for - I think that's different. That's a how to price, not whether to price.

There are, you know, I think if it goes to the question of fuel throughput levies I think the question then becomes, well, why not provide the sites

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that the tanks sit on for free. It's a rent, it's just rent for access to land, and as I say, and I said in my introductory comments, I think the real issue is not whether those levies are there or not, it's how are they set and what are the mechanisms around their resetting, that is, I think the relevant question that goes to an exercise of market power, rather than the existence of, for exactly the same reasons, for example, that the ACCC, when Melbourne Airport made an application to it to impose taxi charges in 2001 found the imposition of taxi charges was fair and reasonable.

The only issue that Melbourne Airport had with the ACCC was how much. They're a payment for a - they are charges relating to access to the airport's land, or to run over it and or to run under it. That's what they are.

COMMISSIONER BAXTER: But do they take any responsibility for the maintenance of those pipelines the moment they hit the boundary of the airport?

DR MUNDY: In respect to those arrangements that were in place at the time of privatisation my recollection is no.

COMMISSIONER BAXTER: Who does carry the responsibility?

DR MUNDY: JUHI.

COMMISSIONER BAXTER: JUHI. So if there's a break in the pipeline the moment it comes in through, say, the Melbourne Airport boundary then it's up to the JUHI to fix it.

DR MUNDY: And my recollection is that the airport is indemnified for relevant environmental harm.

COMMISSIONER BAXTER: Okay.

DR MUNDY: That's my recollection, Commissioner. It's a long time since I've looked at those. That would be my expectation. You could put that question to our members. They would probably have a better idea, but that would be my expectation.

COMMISSIONER KING: Just a simple follow-up, if you give a levy as a rent, a land rent, any argument why it wouldn't be more efficient just to have a fixed land rent rather than a throughput levy which pushes up the marginal cost of fuel?

DR MUNDY: I think you can argue it both ways, Commissioner. I think at the end of the day we know that - well, as I indicated, the marginal cost

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of fuel doesn't seem to be having very many efficiency impacts around the place. I think it's the aggregate cost of lifting fuel to the aeroplane that's relevant, particularly for long-haul aircraft because they're probably going to fill up anyway.

And the other observation I would make about fuel throughput levies is that the FAC didn't dream this up all by itself. This was common international aviation practice which the fuel companies were happy to enter. There wasn't an exercise of market power here, even by the FAC. This was common practice which the fuel companies were happy to have, but as I say, the world, we weren't talking about competition in fuel supply in the mid-90's. It wasn't something, partly because, and I think this is an important issue, not necessarily for the Commission to solve, but to keep in mind is that part of the impetus for this debate, I think from government, is the closure and the reduction in refinery capacity - - -

COMMISSIONER KING: That's right.

DR MUNDY: In Australia rather than anything else.

COMMISSIONER LINDWALL: So other things being equal, and I know you have to leave soon - - -

DR MUNDY: No, I'm fine.

COMMISSIONER LINDWALL: on the open access and in your submission you said that solutions had to be tailored to individual airports, it that because of the nature of all of the different pipelines and the use of trucking and other things that vary quite markedly from the different airports?

DR MUNDY: No, I don't think so, not in principle, because the real issue here is, the storage of the fuel and its carriage to the plane. How it gets into the tank at the airport is a - you know, obviously if there is a pipeline network then we need to contemplate an access arrangement to the pipeline. I know that certainly the former chairman of the Commission was very keen on access arrangements for general urban road infrastructure and waxed lyrical on these matters in a public infrastructure report, Commissioner, but I think the real issue is, there's two. If you've got a pipeline coming to the airport, and let's face it, you're not going to have a lot of them- - -

COMMISSIONER LINDWALL: No.

DR MUNDY: You know, it's not one or two. The real issue is from the tank to the aircraft. You know, BARA has suggested that that is something

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airports could do. I think it's fair to say that the membership of the AAA is in some places interested in doing it, and other places not, and that's just about diversity of business and shareholder preferences, perhaps the issues that they have with fuel in their locale.

COMMISSIONER LINDWALL: Okay. Did you have any more questions?

COMMISSIONER KING: Just the one that I never got to ask. Sydney which you - - -

DR MUNDY: You can have a go.

COMMISSIONER KING: You were in the room when the issue of the three-year lease came up at Sydney.

DR MUNDY: Yes.

COMMISSIONER KING: And that is a disincentive for investment by the JUHI joint venture and by all - in fact by potential interest. A number of us up here have commented on, you would expect the airport to want an efficient fuel system operating as competitively as possible because it presumably has no desire to make the oil companies rich. It would prefer to be running an efficient airport, and if there were profits to be made to keep it for themselves.

Any thoughts about why - you know, is Sydney Airport's behaviour then with regards to the JUHI, not taking control of it, not moving down the Melbourne route and keeping on a three-year lease that seems to create uncertainty. What are we meant to read into that as a Commissioner?

DR MUNDY: Far be it from me to tell the Commission what it should read into things. I am not aware of the content of the commercial arrangements that Sydney Airport has with its JUHI tenant. I accept on face what Mr Abrams says about the term, but I am not aware of what else is in that agreement which may provide more colour or more detail around whatever that arrangement is, and for me to comment on it, Commissioner, quite frankly would put me in a position where I could be misleading the Commission and that is something I am not prepared to do.

COMMISSIONER BAXTER: Okay. Following that question, and you may not want to answer this, but do you have any knowledge as to whether there is discussion between the oil companies as to whether fuel is shipped out of the tanks that are at or close to the airport itself in Sydney, or shipped out of the tankerage that is at the end of the harbour here which then

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transfers currently, I think the pipeline is still there, from that storage tank to the Shell refinery or was the Shell refinery.

DR MUNDY: Commissioner, I have no such knowledge and nor have I ever had such knowledge since I started working in this industry in 1999.

COMMISSIONER BAXTER: Yes, okay.

COMMISSIONER KING: Well, I think we've probably kept you long enough, Warren, so thank you, Dr Mundy, for turning up today and testifying to us.

DR MUNDY: Thank you, Commissioners.

COMMISSIONER KING: Thank you

COMMISSIONER LINDWALL: We might now ask our next, is the Bioenergy Australia. If you'd just like to tell us your name and organisation, and maybe make a little of an introductory statement that would be great.

MS McKENZIE: Sure. So Shahana McKenzie. I'm the chief executive of Bioenergy Australia. I'm also Australia's representative on the International Energy Agency for bioenergy. We are - Bioenergy Australia is the industry association for the bioenergy sector, so ranging across the whole, sort of, area from liquid transport fuels through to potentially products and chemicals, gas, electricity, heat, et cetera.

Our members are made up of a very diverse mix, so all of Australia's biofuel producers. We also have some international producer as well. We have state governments; we have Qantas and Virgin; we have both airlines. We have trucking companies, really a whole range that I'm sure you could imagine that have an interest or an association with bioenergy now or into the future.

I suppose in terms of moving on to the topic sort of here today ,and giving a bit of scene-setting, I suppose, which was included in the submission, but bio-jet has in 2017, it achieved over 100,000 flights globally. There is currently six approved pathways for the production of bio jet, and with those being able to be blended up to a 50 per cent capacity, so as you can imagine that is a substantial amount of fuel potentially for the future that will be consumed through bio-jet.

I suppose then also just talking about that sort of global scene-setting, one of the key drivers in terms of the development of the industry internationally

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but also in Australia in the significant interest in terms of investment interest in Australia is due to the decarbonisation efforts of the aviation sector, and also the marine sector, so the IMO as well as the CORSIA agreement.

So effectively a 50 per cent reduction in emissions by 2050. The only real substantial way that the airlines are going to be able to achieve that is through a shift to biofuels, and really we're talking about the percentage of around 30 to 40 per cent of the fuel consumed in flights in order to achieve that target by 2050 will need to be, you know, renewable, low emission fuel.

I suppose then moving on from that point, one of the - a number of our members participated in a pilot project out of Brisbane Airport, so Virgin and the Queensland Government as well as some others that identify for us some key concerns around the ability for biofuels to be able to make their way to market.

And I suppose the really concerning part for us regarding that was when you have a pilot project such as this that has and was in planning for quite a number of years that has the full support of the Queensland Government, including the Premier, that has the full support, well, actually initiated by one of the major airlines, that that project was very difficult to succeed. It sort of presents in our mind, if you've got that much backing from such key partners, then how on earth is the industry going to make a pathway to be able to access the fuel being able to make its way to market.

So I suppose from that perspective, and I'm sure you'll probably ask some questions specifically around that project so I won't go into it in too much detail, at high sort of level from our perspective what was identified through that process was a lack of transparency around decision-making by the JUHI so there wasn't the ability to understand why decisions were made, when they were made, when they would be made.

There was no appeal process to be able to understand if decisions were made, where do we now go, what is the process for then appealing that process, and I think as was mentioned earlier on today, that there does seem - there's no transparency around the terms of access. So if we're - as a country if we're looking to potentially create a new industry in Australia which would potentially have a whole raft of different knock-on positive effects in the country around international investment through the development of local biofuels from way streams and a whole raft of other things, that will only be successful if there is an opportunity for that fuel to make its way to market. So from our perspective hat very much was, you know, identified as key issues.

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I think one of the other key things from our perspective was to make a recommendation that there is a process or a person who is appointed as an independent person that participates in those decision-making processes around fuel being able to make its way through the JUHI.

Now, this trial, I suppose, is unique in a sense because it wasn't biofuels being delivered on its own to an airport and pumped straight in. It was done through a contract of an existing member of the JUHI who had a contract to supply that fuel.

So in one respect it was an even easier process, I suppose, than you know, a truck pulling up with biofuels and requesting that access. So yes, so I think that that sort of in terms of the summary of where we're at and what our recommendations are, that's really

COMMISSIONER LINDWALL: Thank you. Could I ask a few more technical questions.

MS McKENZIE: Sure.

COMMISSIONER LINDWALL: I mean, to start with, to put the scene on this, when you said there were six methods, you're talking about using algae or fatty acid methyl esters and things like that. Now, do you have a view on which one is most propitious on that?

MS McKENZIE: I think, I mean, look, at the moment there are six approved pathways that come from a range of different feedstocks, but also a range of different technology types in terms of how that fuel is actually created, and my understanding is that there's another 17 pathways that are currently in the process of either going through the approval process or, you know, finalising the technology, and I think, I mean, what we certainly have seen at Bioenergy Australia is that there has been a substantial increase in the amount of energy, activity and the like which is going into the development of biofuels, particularly bio-jet, and I think that what ultimately will happen will be a - it will be a game of, you know, the market really deciding whichever is going to deliver the lowest cost fuel, and that will range on so many different factors.

I mean, you can imagine that a project which is currently in development at the moment over in the US which is taking municipal solid waste and converting that into jet fuel. That becomes very favourable depending on whatever the landfill levy is that's then diverting that waste.

So I can imagine that there's going to be a process where we currently have six, there's 17 in waiting and I think that we will end up at a place when

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we're sitting here, well, not here hopefully, in 30 years' time with a number of different pathways that have risen to the top as being the most economically viable, but also achieve the highest level of emissions reduction and the like.

COMMISSIONER LINDWALL: Are all the compounds, chemical compounds of the six pathways identical or are they identical to Jet A-1, for example, which is kerosene, so can you distinguish them?

MS McKENZIE: So they're either - so each of those pathways are approved, so the six pathways are approved by ASTN, and now with the upgrading of DEF STAN that basically that is now also, you know, approving those as well.

There is some work that's being done at the moment to develop a 100 per cent drop in bio-jet as well synthetic, so that isn't yet at, you know, at any sort of place where that is even close to being commercially viable, but the synthetic creation of aromatics potentially could then take bio-jet to a very different space in terms of not requiring that blending at all, and that's certainly where the path is in terms of renewable diesel, so it is 100 per cent drop in fuel rather than requiring that blending.

COMMISSIONER LINDWALL: Do you feel that some of the reluctance or the pushback, if you like, from the JUHI's is because they say that it's a different fuel and therefore should be treated separately or do they assert things about safety or security or anything like that?

MS McKENZIE: Well, I think that that's one of the key issues in terms of the process is that actually receiving any feedback from the JUHI on decision-making is vacant, so I think that that, you know, from our perspective we - you know, there's been certainly no official notice to us in terms of any concerns that they have regarding bio-jet in Australia and how that is running through the system, and I mean, the fuel that was utilised for this pilot was probably the most highly tested fuel that has ever existed in this country to the number of times that it was tested, and so it - I mean, you can draw your own conclusions in terms of that process, but yes, from our perspective we haven't been notified that there's any official concerns. The fuel absolutely met spec; in fact, you know, exceeded spec, and as I said, this is tried and tested for over 100,000 flights. If you've flown out of LAX you've flown on a plane that has bio-jet running through it, so you know, it is safe.

COMMISSIONER KING: Can I just follow up on that point.

MS McKENZIE: Of course.

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COMMISSIONER KING: In your submission you went a little bit further that you just went.

MS McKENZIE: Okay.

COMMISSIONER KING: And you mentioned unreasonable levels of testing. Are you able to expand a bit more on why you thought - so you said there was very thorough testing.

MS McKENZIE: Sure.

COMMISSIONER KING: Why unreasonable? Why do you think it went further than could possibly - well, do you think it went further than could possibly justified? Do you see or do you have any views on why that may have occurred?

MS McKENZIE: So I suppose in terms of hypothetically, if a fuel was to be tested by a JUHI and it was tested by one of the JUHI members and the results were provided to the remainder of the JUHI members, then I would wonder why that then required multiple other tests being required of that particular fuel.

COMMISSIONER KING: By other JUHI members or - - -

MS McKENZIE: Perhaps, yes.

Ms McKENZIE: Okay. So I'm probably not privy to or being able to share exactly what took place, but I think that there should be, and this sort of comes back to our recommendation, if there is a transparent approach to the process that you need to go to in order to supply particularly bio-jet because it is a different fuel in this market, then that process should be clearly articulated so that you understand exactly what is required along each of those steps of the way in order to then understand the decisions that are made.

So whereas that is certainly not currently the case, the fuel goes into a vacuum and it sits there with really no expectation on when you will understand if it will be approved, when it will be approved, if it won't be approved, what's actually happening to it so presumably if an open-access regime exists at an airport - - -

COMMISSIONER KING: do you think that sort of - I mean, obviously open access can involve things like physical how you deliver the fuel to the

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relevant facility, the pricing. These other matters that you've just been discussing, how important are they for an open access regime?

MS McKENZIE: I mean, incredibly important from our perspective and I think creating an opportunity that is a transparent process for the purchase of fuel from airlines, I mean, we - we have, both of our airlines, both Virgin and Qantas, both have their own agendas at the moment in terms of seeking to support the development of biofuels in Australia, and from our perspective anything that is going to be a barrier to them being able to purchase that fuel and for that fuel to be able to run through the system is negative from our perspective.

So creating an open access system that was transparent and fair and had a, you know, a good governance structure would was supporting it and had a process that was able to be appealed through, you know, some vehicle, we would support.

COMMISSIONER LINDWALL: The 100,000 flights you mentioned - - -

MS McKENZIE: Yes.

COMMISSIONER LINDWALL: what percentage of biofuel to total fuel was consumed during those flights?

MS McKENZIE: Oh, I think we're like 1 to 2 per cent by the time it is diluted through that - - -

COMMISSIONER LINDWALL: Yes, but is there any limit in terms of individual flight to which could be used where you wouldn't want to go beyond or could you use 100 per cent, for example, theoretically?

MS McKENZIE: So at this stage it is approved up to - of those six pathways, up to 50 per cent blend. In saying that, it has been tested particularly with the American forces in terms of their defence forces. They have flown flights on 100 per cent biofuels. It certainly is - my anticipation in our submission that that is where we will move to, and the rate at which the technology is improving because of drivers such as the CORSIA agreement, that we will see a significant, you know, change in that. I mean, there is billions of dollars of investment happening in the US at the moment just in this space. It is, you know, a new industry really.

COMMISSIONER LINDWALL: Obviously if you look at it logically from a perspective, here's some pipelines coming into an airport.

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MS McKENZIE: Yes.

COMMISSIONER LINDWALL: You wouldn't want to be trucking in your - - -

MS McKENZIE: No.

COMMISSIONER LINDWALL: Want there to be a pipeline coming in. It's got to come beginning of the pipeline, so where's the source of all the biofuel in Australia, for example, and the distribution network of it and how do you see that growing over time?

MS McKENZIE: Yes, well, I think that this is really the opportunity in terms of for a new industry in Australia that is, you know, generally a regional industry in terms of the production of fuels, but we have a number of international investors and domestic groups that are currently looking at, you know, scoping projects in this country in order to develop bio-jet as well as whether it's renewable diesel and the like.

So I think that being able to deliver, it is a blended fuel at that time, so it requires a relationship for that fuel to be able to access It doesn't need to go through a, you know, an oil company necessarily in order for that bled to happen, but it does require the support of the infrastructure system and the JUHI for the fuel to make its way into the market for it to be able to make its way in place.

COMMISSIONER LINDWALL: And it can be imported by ships, for example.

MS McKENZIE: Absolutely. Absolutely, and I think, I mean, if we look at the Brisbane example, that was imported bio jet that came from the US.

COMMISSIONER LINDWALL: Yes.

COMMISSIONER KING: So does that mean then for - when you're talking about access, it's really access to the entire supply chain potentially back to storage facilities - - -

MS McKENZIE: Yes.

COMMISSIONER KING: that would otherwise be used for imported fuel?

MS McKENZIE: Yes.

COMMISSIONER KING: So storage pipeline.

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MS McKENZIE: Absolutely.

COMMISSIONER KING: Storage at airport, JUHI interplaying as well?

MS McKENZIE: Well, I mean, access - well, potentially, yes.

COMMISSIONER KING: Yes.

MS McKENZIE: I guess the concern that we have is, if the requirement for biofuels to make their way to, you know, to airlines in order for the distribution, if the only path that they can go through is trucking, then it makes it basically financially unviable for that to happen. So it, you know, from our perspective it is about providing access to the JUHI.

COMMISSIONER LINDWALL: So the trial in Brisbane, was that principally promoted by the Queensland Government obviously?

MS McKENZIE: Yes.

COMMISSIONER LINDWALL: So what about in Victoria which, of course is, Melbourne Airport has changed its arrangements somewhat. Is that something that you might be considering the Victorian Government promoting?

MS McKENZIE: I'm - to be honest, we are engaged with the Victorian Government regarding what's taking place with the airports down there. Our first - and the development, I suppose, in terms of bio-jet in Australia has been a relatively new thing in terms of particularly around this public pilot demonstration that took place. So this is a sort of new venture for us in terms of making our way across the country and engaging with governments around how they could be looking at this in the potential of a whole of government approach around, you know, new industry development and attraction, and you know, and then that associated in terms of what's required in order for that fuel to actually make its way to market.

COMMISSIONER LINDWALL: So there was thought about applying through a Part 3A declaration to the NCC?

MS McKENZIE: Not at this stage. Not at this stage, I mean - - -

COMMISSIONER LINDWALL: Is that because it's too early and it's too complicated or - - -

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MS McKENZIE: Well, I mean, I suppose from our perspective, and it probably follows off what was said earlier on this morning, I think if there were some processes around having some transparency of decision-making that there was an ability for an appeal process, you know, that we have seen that fail already.

COMMISSIONER LINDWALL: Yes.

MS McKENZIE: And I'm not sure that there is, as was said earlier, that there is much new evidence to support that that would be a different approach of a different decision. So, you know, we would really just like to see that there is a different approach to, you know, to how, I suppose, government seeks to provide guidance to the governance structures of the JUHI and the transparency that is provided there around decision-making.

COMMISSIONER KING: Purely a mechanical question, in the Brisbane pilot, where was the biofuel, where did it enter the supply chain?

MS McKENZIE: To be perfectly honest, I can't answer that question.

COMMISSIONER KING: Okay. All right.

COMMISSIONER BAXTER: Can I just ask what is - - -

MS McKENZIE: I can check. So it came into the port of Brisbane and was then taken to Caltex's refinery.

COMMISSIONER KING: Okay.

COMMISSIONER BAXTER: Did you want to follow up?

COMMISSIONER KING: No, no, it was purely understanding that you needed the entire supply chain for that pilot.

MS McKENZIE: Yes.

COMMISSIONER BAXTER: What's the attitude of the oil companies to biofuels? I mean, is it neutral? Is it regarded as a serious competitor? Is it regarding it as - - -

COMMISSIONER KING: Opportunity.

COMMISSIONER BAXTER: Parts of it regarding it as - - -

COMMISSIONER KING: Opportunity or threat, yes.

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MS McKENZIE: Look, without doubt it's a threat, and I think - I think if you look at, I mean, what's interesting from our perspective is that you can look at it - there's probably two answers. One is the domestic market and one is the global market. If you look globally and you look at the 50 year sort of strategies for BP and the like, biofuels are a large component of their transition strategy and what they're seeking to do.

In the Australian market, from our perspective, the biofuels industry struggles at every hurdle really in terms of being able to access market. It is, from my perspective, I would say that biofuels are viewed as a threat and a challenge that they would prefer to see pushed down the path as long as possible.

COMMISSIONER BAXTER: I see, yes. I mean, this is in -sorry, but sort of critical reaction, this is in spite of the fact that quite a number of the media in both the US and Europe and UK have been positive towards the involvement of biofuels. Why this negativity in terms of the Australian suppliers? Just because it's too difficult for them and it's just something they don't want? Because most of their owners presumably are going to be either US or UK.

MS McKENZIE: Look, I mean, I can't answer on behalf of the fuel companies in terms of why they are resisting biofuels in Australia. I think that in every market across the globe there is a resistance against biofuels from the oil incumbents, and I think it's just, you know, similar to the coal fire, you know, generation of electricity and renewables. I think, you know, there has been a very long and secure market that they have operated and held, and that that is now under threat and in an increasing and significant way, and that you know, that this year's potentially going to be an area that they are going to lose substantial amounts of money.

So for - globally, I mean if you look at BP for example, BP are one of the investors in the Fulcrum Project which is the municipal waste to bio-jet project in California. They're also one of the funders of, you know, one of the biggest sort of ethanol production facilities in Brazil as well, so I think that it depends on the market climate and the preparedness for them to embrace this change, and even potentially to be able to capitalise on it, and I just don't think the Australian - that there's a level of interest there.

COMMISSIONER BAXTER: Except that they're an investor in a waste fill regeneration project in Perth at the moment.

MS McKENZIE: Well, yes, potentially.

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COMMISSIONER BAXTER: Yes. Well, no, they actually are. They've actually forked out quite a significant amount of money.

COMMISSIONER LINDWALL: Who's they?

COMMISSIONER BAXTER: BP, and they've got eh support of the Western Australian Government.

MS McKENZIE: Yes.

COMMISSIONER LINDWALL: I've got one final question about your adjudication role that you just spoke of. Is that something you thought the ACCC should be doing?

MS McKENZIE: Look, I suppose from - short answer, yes. Yes, I think to be able to have a clear appeals process that you can go through that was clearly understood, and that was able to, you know, for you to be able to provide evidence and then to be given a reason as to why yes, or no, that fuel is going to be permitted, and in what timeframe. You know, I think the ACCC is the natural organisation that would, you know, that would do that.

COMMISSIONER LINDWALL: And have you engaged with the ACCC, and if so, are you able to tell us the type of discussions that you've had?

MS McKENZIE: Yes, we haven't engaged with the - I sit on the ACCC fuel consultative committee. We have not engaged with the ACCC on this specific pilot that took place, and I think it's probably, we didn't understand the way that the JUHI operated until going through this process, and I think that that was one of the reasons why the pilot was initiated was to, you know, to say, "Okay, how are we actually going to go about getting this fuel into the system", and this isn't just a one-off pilot. So Virgin are planning on bringing this fuel round on multiple occasions. In order to, you know, almost sort of smooth the pathway a bit, and as each time hopefully it will become easier and those issues will be identified in order to make it easier for that to happen.

But, I mean, we can't afford for that to happen at every airport across the country in order for us to be able to, you know, to supply this fuel which has such significant benefits in terms of what it does around emissions reduction, particular matter efficiencies and the like.

COMMISSIONER LINDWALL: Does this require a legislative change or new regulations or merely government's action and requesting the ACCC to do something?

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MS McKENZIE: Yes, I think so. I think it - - -

COMMISSIONER LINDWALL: It doesn't require- - -

MS McKENZIE: No, I don't think so, and to be honest, I haven't really been able to spend the time to look into what that would look like.

COMMISSIONER LINDWALL: Yes.

MS McKENZIE: But I think to, you know, the key for us is really around providing that level of transparency. In an idea world, and I don't think if, you know, what would be required, but to have a level of independence in the decision-making around the JUHI from our perspective would be ideal. It's probably incredibly difficult for anything like that to happen but it doesn't, you know, as an outsider looking in, common sense sort of says to me that, does it make sense that decisions are made about new fuel access by those that have a vested interest in it staying as it is, and I think you know, would we - which it once did happen, but would we allow Virgin and Qantas to decide the slots at Sydney Airport.

COMMISSIONER LINDWALL: Yes.

MS McKENZIE: Or would we allow the taxi industry to decide who is provided Uber certificates. I mean, it's sort of from a common sense sort of approach it doesn't sort of rub well with me.

COMMISSIONER LINDWALL: Well, if you could perhaps reflect on that and maybe come back to us - - -

MS McKENZIE: Sure.

COMMISSIONER LINDWALL: - - - at some stage about the actual mechanism - - - -

MS McKENZIE: Specifics.

COMMISSIONER LINDWALL: Yes.

MS McKENZIE: Happy to.

COMMISSIONER LINDWALL: Stephen, did you have any more?

COMMISSIONER KING: No.

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COMMISSIONER LINDWALL: I think that's fine.

MS McKENZIE: Thank you.

COMMISSIONER LINDWALL: Thank you very much, Shahana. Well, that's officially all we have registered, but does anyone else want to either comment on or make any statement in relation to our previous hearing participants or anything else for that matter? You're most welcome to come forward. No one? Barry doesn't want to say something again to - okay, well, in that case thank you very much everyone for coming to our hearings today. I'll adjourn them and we'll resume on Friday in Melbourne, and thank you all for being here, and thanks to our transcript gentleman.

MATTER ADJOURNED AT 12.03 PM UNTIL FRIDAY, 30 NOVEMBER 2018

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Australian Government
Productivity Commission

PRODUCTIVITY COMMISSION

MR P LINDWALL, Commissioner
MR K BAXTER, Commissioner
MR S KING, Commissioner

TRANSCRIPT OF PROCEEDINGS

AT LEVEL 12, 530 COLLINS STREET, MELBOURNE
ON FRIDAY, 30 NOVEMBER 2018 AT 9.55 AM

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RESUMED **[9.55 am]**

COMMISSIONER LINDWALL: Good morning. I don't expect too much turbulence today, but like always you should have your seatbelts fastened just in case. I am Paul Lindwall. Welcome to the public hearings for the Productivity Commission's inquiry into the economic regulation of airports. I'm the presiding Commissioner here. I've got Ken Baxter on my left and Stephen King on my right here, who are my fellow commissioners. The inquiry started with a reference from the Australian Government in June 2018. The purpose of the inquiry is to investigate whether the economic regulation of airport services promotes the efficient operation of airports and related industries. The Commission has been asked specifically to review competition in the market for jet fuel in Australian as part of its inquiry.

We've talked to representatives from the Australian state, territory governments, airports, airlines, representative bodies, and academics, researchers, and individuals with an interest in the inquiry. Starting with our issues paper on 9 July we've received, I think, 77 submissions since its release and more are obviously welcome and will be available on our website. We're grateful to all the organisations and individuals who have taken the time to prepare submissions and to appear at the focused hearings here on competition in jet fuel markets. We had a hearing in Sydney a couple of days ago. We're now working towards completing a draft report, having considered all of the evidence presented at the hearings and in submissions and in other discussions, and we're expecting to be releasing that in February 2019.

Public hearings regarding the broader inquiry will then be held in March to April 2019 following the release of the draft report. The final report will be submitted to the Australian Government in June 2019. Participants and those who have registered their interest in this inquiry will be advised of the final reports released by government, which may be up to 25 parliamentary sitting days after completion. That can be a long time. The purpose of these hearings is to provide participants with an opportunity to elaborate on their submissions and to discuss issues with the commissioners here. Any organisation or person can participate, but those who have an interest in the market for jet fuel have been encouraged to appear.

We like to conduct all hearings in a reasonably informal matter, but I remind you that a full transcript is being taken, and that's why questions from the floor can't be taken, but at the end of today's proceedings, if you want to come up and either correct what someone else has said or make

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your own statement you'll be welcome to do so. You're not required to take an oath, but of course under our Act - the Productivity Commission Act 1998 - you're required to be truthful in your remarks. You're welcome to comment, as I said, on issues raised by other people or in submissions. The transcript will be made available to - well, on our website at some stage. What, about a week I think it is? Something like that. Submissions are also, of course, on our website. For any media representatives attending today some general rules apply. Please see any one of our staff for a handout which explains the rules.

To comply with our - we're in the Commonwealth territory building office here - with occupational health and safety legislation you are advised that in the unlikely event of an emergency requiring the evacuation of the building, please listen to - for instructions over the PA system. Follow the exit signs to the nearest stairwell - so it's back out that way and the stairwells are right there. Lifts are not to be used, and please follow instructions of the floor wardens. If you believe you're unable to walk down the stairs it's important that you advise the wardens, who will make alternative arrangements for you. You are invited - participants are invited to make brief opening remarks, and I'd like to welcome Melbourne Airport, and if you could introduce yourself for the transcript, and make any initial comments you wish to.

MR GANDY: Certainly, I will do. Thank you, Commissioners, for having us here today. We're both very pleased to be here. My name's Simon Gandy. I'm the Chief of Aviation for Melbourne Airport, and with me I have my colleague, Scott Elliott, who is the Executive for Strategy and Business Improvement. I thought it would be useful to start with a bit of a brief overview of the current arrangements for jet fuel at Melbourne Airport before we get into any questions. We've got a keen interest on how the jet fuel market operates at Melbourne Airport. From our perspective we want Melbourne Airport to be competitive with other airports, which forms part of our offering to existing customer airlines, as well as attracting additional services and new airlines too.

There are two key aspects to a competitive offering when it comes to jet fuel, from our perspective. The first is to ensure that there's a resilient supply of jet fuel, and this has been an issue in the past for us, but we've put agreements now in place to remedy this situation at the airport. The second is that Melbourne has competitive jet fuel pricing; so those are the two key aspects that we believe provides a competitive offering. These objectives are completely aligned with those of our airline customers as well, as what's best for them is best for us as an airport at the same time. However, the provision of jet fuel is ultimately a transaction between

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individual airline and fuel companies, and so our ability to influence can at times be somewhat limited in this.

Where we can make the biggest difference is through the terms of the lease between Melbourne Airport and the JUHI joint venture at the airport. In November 2017 we signed a new 20 year agreement with the JUHI joint venture, which will result in better outcomes in the future, and I'll quickly over off on a couple of important features of the new agreement before going into a bit more detail. So, the first is really around improving the resilience of the jet fuel supply. There are new provisions in the agreement that require the JUHI to meet benchmarks for onsite storage capacity, input capacity into the JUHI, and a supply of hydrant infrastructure which is distributed throughout the whole airport precinct. So that's how we get fuel direct to aircraft on stands.

By introducing these requirements the agreement will ensure that not only is the JUHI facility suitable for today's needs, but actually it keeps pace with the growth of Melbourne Airport over the next 20 years, where we're going to be approaching between 65 and 70 million passengers by 2038. The new agreement requires that onsite storage capacity at the JUHI must meet the IATA guidelines for three days of operating supply. Currently we're well below this, with storage at about 1.2 times the average daily usage. To meet this requirement new storage facilities at the JUHI are currently being constructed, so this is already underway, and we're expecting that these will be operating in late 2019.

This is expected to add an additional 25 megalitres of storage capacity, which will more than triple the existing storage capability, and that supports the recovery of any unforeseen outages for a longer period of time at the airport, should they occur. The new agreement also requires that the input capacity to the JUHI will be maintained at least 110 per cent of the average peak day daily operating requirement. So that's making sure that we're able to get fuel into the JUHI facility at a sufficient rate. that supports fuel resilience with greater storage, allowing Melbourne Airport to recover from potential supply shocks should they occur in the supply chain, and in the past 12 months a third bridger, which is the - effectively the - it's the facility that enables trucking to offload at the JUHI. A third bridger has been delivered, and that investment has increased the input capacity of the JUHI, and there is also provisions in the agreement to enable a new pipeline to be constructed as well.

The agreement also ensures that Melbourne will have sufficient hydrant infrastructure over the life of the agreement, and this really is committing the JUHI joint venture to investing in hydrant infrastructure in line with our passenger growth. So in the past we haven’t had that link, but it's

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importantly linked now, and it's linked with the investments that are included within our Air Services Agreement that we have with our airlines. So there's a flow through from the demand for passenger growth and airline growth, through to the JUHI providing onsite facilities in terms of hydrant infrastructure. So they're the steps we've taken to improve resilience of the fuel supply at Melbourne. They are important measures, and they will provide great certainty for the airlines operating out of Melbourne in the future.

As I mentioned, we're also keen on ensuring that the price of jet fuel at Melbourne is competitive. This is particularly important for aviation growth as we compete for traffic with other airports, and given that fuel is one of the largest costs to our customer airlines this is a key consideration for airlines in reviewing the overall commerciality of a route to Melbourne. So while we have no direct involvement, it's very important for us that Melbourne is competitive, which is why the new agreement requires the Melbourne JUHI joint venture to provide for open access to the JUHI facility. We hope that this will promote competition in the jet fuel market, reduce resilient - reliance on a small number of providers, and give airlines the opportunity to introduce their own supply should they require it.

We understand that there's been significant interest in this from companies to access the Melbourne JUHI, so there are entrants that are potentially ready to enter the market. As I said, the agreement allows for an additional pipeline to the JUHI. This will be important for not only meeting future demand but also allowing access seekers greater choice in how they transport their jet fuel to the JUHI facility at Melbourne. So that's really a summary of the measures that we've put in place, into our new 20 year agreement. We think it will serve Melbourne Airport and its airlines well. However, ultimately the supply of jet fuel is based on commercial relationships between airlines and fuel companies, and the extent to which Melbourne Airport can influence the jet fuel market is limited beyond our agreement with the joint venture. The joint venture also doesn't address, obviously, the supply chain that leads into the airport as well, which is a key factor.

COMMISSIONER LINDWALL: Thank you very much for that.

MR GANDY: That concludes my opening statement, thank you.

COMMISSIONER LINDWALL: Thank you. I'll ask a couple of questions and then get my colleagues to ask questions, but could I ask, firstly, the - when you met with - the other day, BARA, and they said the

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open access is not - Melbourne Airport and the new lease is not really open, what would you say to that comment?

MR GANDY: It's an interesting comment. The provisions in the agreement require that - the JUHI joint venture to provide for open access, and I think that has been tested. Our understanding from the JUHI is that they've had a number of companies apply for access. So we're very much leaving that for the JUHI to manage in that process. We're pretty clear from what's included within the agreement that open access should be being provided by the JUHI, and we'll keep, obviously, tabs on how well those access requests are going over time.

COMMISSIONER LINDWALL: But at this stage it's too early to tell, I guess, that?

MR GANDY: Very much so, yes.

COMMISSIONER LINDWALL: Yes, and when you were negotiating the new lease agreement, compared to the previous one, the - you have incorporated this open access. What did you - how did you manage to get that in, I guess? That's quite a good addition, one would have thought, naturally.

MR ELLIOTT: Yes, yes. Well, the negotiation with JUHI was quite a long and complex one, because we were looking to solve a problem that we had at the time in Melbourne Airport, and I think the problem came about, and it's - potentially taking one step back to be able to give you the context - it came about because the existing lease that we had with the JUHI lacked, probably, the necessary provisions to ensure an orderly transition at the end of that lease, which meant that both parties probably had quite different views on how to go forward, but equally that gave us quite a lot of scope to talk about, if we were to partner for the next 20 years, what would that agreement need to look like? And we had some quite clear views, and Simon's already articulated those, that we needed to make sure we had the necessary investment in infrastructure but also the open access.

The JUHI had, I guess, realised the - if they did want to be able to enter into a long-term agreement with us there would need to be some flexibility on all of those points, and I must say they didn't accept our - exactly our position on all of these items, so there was quite an intense negotiation, but ultimately we were able to, as part of the package, include open access, and like Simon said, though it is at an early stage.

COMMISSIONER LINDWALL: Yes.

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MR ELLIOTT: And the open access regime that is included within our agreement only covers on airport infrastructure.

COMMISSIONER LINDWALL: Yes.

MR ELLIOTT: It doesn't cover anything outside of that because we were negotiating with a set of owners.

COMMISSIONER LINDWALL: Yes.

MR ELLIOTT: And that set of owners isn't replicated throughout the supply chain.

COMMISSIONER LINDWALL: The terms and conditions for access under the open access, they're not public, I assume?

MR GANDY: No, they're not. They're part of the commercial agreement.

COMMISSIONER LINDWALL: Would that be better, to be transparent about that type of thing, so that a potential new entrant would know ex ante the types of terms and conditions that are needed to be agreed to reach the open access?

MR GANDY: Yes. Whilst the legal terms in the document are commercially, obviously, sensitive, there is a requirement on the JUHI to have, on their website, how you actually gain access, so what the conditions under the open access are and how you apply. We believe they're all in place, and certainly the feedback from some of the organisations that are currently applying for access, they've been able to navigate that and they've been able to apply, so - and there are companies going through that process right now. So we're not hearing, really, a lot of noise coming back saying we haven't got enough information to move forward.

COMMISSIONER LINDWALL: I will talk about some other issues, but maybe you want to start, Stephen.

COMMISSIONER KING: Yes. Just following up on what you said there, so can I take it from what you've said that there was an issue with a lack of investment because the end of lease terms and conditions weren't clear; is that what you were saying when you talk about an orderly transition?

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MR ELLIOTT: That was one of the items. There was no sunset provision in the agreement that dealt with investment in the last three to four years, for example.

COMMISSIONER KING: Okay. Well, we note that there's different arrangements at different airports.

MR ELLIOTT: Yes.

COMMISSIONER KING: So, in your opinion, how important is a longer term lease arrangement with the JUHI? How important is that for investment?

MR GANDY: I'll answer that. I think the key thing here is the airport is going to be around for some time, and it's the front - it's a front door to the state and the city of Melbourne for this particular traffic. So, having a long-term agreement actually enables organisations to invest for an appropriate period of time in the necessary infrastructure to mark time with growth. The previous agreements didn't have any of that tie-in in terms of what our airline customers would need in the future to match the growth of the airport, and therefore the necessary investment in the JUHI. The new agreement has that, and the 20 years was considered to be an appropriate length of time to enable all organisations to succeed in that process.

COMMISSIONER LINDWALL: So, I think some of the fuel companies have said that the lack of investment that was apparent previously is partly due to the non-lease - the lease terms not being long-term. Would you agree with that, or?

MR GANDY: I think that might have been an argument at a moment in time that has now passed. So, I don't see that as being a problem.

COMMISSIONER LINDWALL: So, could I ask, you've currently got 1.2 times average daily supply?

MR GANDY: Yes.

COMMISSIONER LINDWALL: I think you mentioned three times as being increased with this 25 - - -

MR GANDY: Megalitres, yes.

COMMISSIONER LINDWALL: Megalitre storage. Does that mean it's 3.6 days, I guess? Is that - - -

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MR GANDY: Yeah, I think it is. It's slightly over. Because of the size of the tanks it's not an exact science.

COMMISSIONER LINDWALL: Okay.

MR GANDY: So, it's a minimum - the IATA guideline is a minimum of three days.

COMMISSIONER LINDWALL: Yes.

MR GANDY: The fact that we might have slightly more than that is obviously a benefit, but - - -

MR ELLIOTT: Initially it will be (indistinct words).

MR GANDY: Yeah, they tend to build these in lumps of 10 megalitre tanks if they can, because it's more efficient to do, so.

COMMISSIONER LINDWALL: Of course. So, the issue you had in the past with black light traffic, what, a couple of years ago when it was - - -

MR GANDY: Yes.

COMMISSIONER LINDWALL: That is not likely, you don't think, to happen in the future?

MR GANDY: Well, I think the important thing here is that the length of time that we've got to recover from a potential incident - because what we're not doing is addressing any of the supply chain issues before the fuel actually gets to Melbourne.

COMMISSIONER LINDWALL: Of course, yes.

MR GANDY: So, I'd love to say I'm never going to have another - a change in traffic light. It's just my ability to respond to that, and therefore how quickly I might move through the traffic lights might vary. The one thing we have learnt is that communication is absolutely key. If there's something that's known upstream in the supply chain, to know that early and then to represent that in the form of a traffic light system really helps airlines and airports manage the whole process.

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COMMISSIONER LINDWALL: So if you consider what happened in Auckland Airport, where pipeline was disrupted, perhaps, by a tractor or something.

MR GANDY: Yes.

COMMISSIONER LINDWALL: And it made quite a major change to operations for a while.

MR GANDY: Yes.

COMMISSIONER LINDWALL: What type of contingencies would happen at Melbourne if that were to happen?

MR GANDY: Yes.

COMMISSIONER LINDWALL: Because you've got the one pipeline coming in.

MR GANDY: Yes.

COMMISSIONER LINDWALL: And how much can you substitute with trucks, for example, for a period?

MR GANDY: Yes, that's why we've tended to include the provision to maintain both bridges and pipeline, but if we had an outage on the pipeline - that's a significant supply source to the airport - it would - having the additional tanks gives us more time to then adjust the operations and actually look at the fuel rationing, rather than having to do that in a day.

COMMISSIONER LINDWALL: Of course, yes.

MR GANDY: So you've actually built in a bit of time to be able to respond, but at the end of the day, if you've lost a pipeline, which is more than 50 per cent of our supply, then it's problematic.

COMMISSIONER LINDWALL: Exactly.

COMMISSIONER KING: Can I just follow up, just on that trucking? So you mentioned that there either is a potential for another bridge or it will go ahead.

MR GANDY: No, a third bridge has already gone in.

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COMMISSIONER KING: Okay, excellent. It's been put to us quite stridently at some airports and by some participants that trucking fuel is simply uneconomic, that it can't compete against pipelines. Melbourne Airport appears to be an exception to that. Why? Is trucking in the fuel actually an economically viable substitute for the pipeline at Melbourne Airport, and why are we getting these different messages from other airports?

MR ELLIOTT: In terms of the economics, transporting jet fuel by pipeline is superior to trucking. The costs are higher. Despite that, we've still got suppliers that are more than happy to truck fuel and are able to make a profit. So, those that have access to a pipeline I'm sure enjoy using that pipeline, but it doesn't necessarily exclude people from the market if they have to truck. That's been the feedback that we have received.

COMMISSIONER KING: Is it partly, then, that the pipeline - or there's limited pipeline capacity coming into Melbourne Airport, so it's fairly constrained? Is that a difference, perhaps, compared to other airports where we find that the trucking isn't viable?

MR ELLIOTT: That would likely be the case.

MR GANDY: Yeah.

COMMISSIONER KING: Okay.

COMMISSIONER LINDWALL: Ken.

COMMISSIONER BAXTER: Yeah. Are you people aware of the shareholding ownership in the Melbourne JUHI, compared to the shareholdings in the Sydney JUHI?

MR ELLIOTT: We are aware that there are differences, but to be perfectly honest we don't - we focus on the arrangement we've got in Melbourne. So we don't really have a lot of information about the way in which those shareholders interact and what the difference is.

COMMISSIONER BAXTER: But presumably with Sydney Airport, as with Melbourne, there is one pipeline that goes from the terminals which the oil is delivered from, presumably, either the (indistinct) store from Singapore.

MR ELLIOTT: Singapore, yes.

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COMMISSIONER BAXTER: What is the assurance that you've got that there's actually a competitive market in terms of that fuel being delivered? I mean, is there any evidence that, the shareholders probably being very much the same, that there's a neat collusive agreement between them as to what the prices are that's offered?

MR ELLIOTT: To be perfectly honest, I don't think we're best placed to comment on that, simply because we're not involved in the day to day negotiations between the airlines and the fuel suppliers, and we don't have the - probably the information required to be able to give you an answer for that.

COMMISSIONER BAXTER: But is that not - I mean, not suggested to you by the amount of fuel that might be drawn down by, let's say, Qantas or Virgin, compared to what might be drawn down by others from the JUHI in Melbourne? Do you have any sense of the volumes that go through the JUHI, or you're just the lessors?

MR ELLIOTT: We understand the overall volumes, but aside from that we don't have access to the information.

COMMISSIONER BAXTER: Right.

MR GANDY: The fuel companies have been fairly clear around their ability to share any of that commercial information with us.

COMMISSIONER BAXTER: That they won't.

MR GANDY: Yes, they won't.

COMMISSIONER BAXTER: Sorry, Stephen.

COMMISSIONER KING: Perhaps coming at the issue for a different direction though. Obviously the new lease has a range of investments in there to get a - to deal with the supply disruption potential, but it has also got the open access in there. Why? What drove the desire from your perspective to have open access in there, rather than just simply additional investment? What's - what do you see is the benefit of open access?

MR GANDY: Yes. So part of this is responding, also, to our customers. So, BARA and other airlines were clear that, actually, open access was a key requirement from their lens. So, part of this is championing our customers' view into the agreement that we had control of, and the second is, as I said right at the start, there's a commercial benefit for us to be competitive as a city, and competitive in terms of new routes and

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additional routes, and existing routes. So, how well an airline performs in its existing state is absolutely key. Given that fuel is one of the biggest costs to them, then the more we can do to support that the better.

COMMISSIONER KING: So when you say competitive, do you mean the price of fuel?

MR GANDY: No - - -

COMMISSIONER KING: Do you mean that the airlines want open access because it's a pricing issue, or what - why do the airlines want open access?

MR GANDY: The airlines want open access for that ability to be able to get access to the cheapest fuel they possibly can, because it's a big proportion of their cost, and if we're - if Melbourne is seen to be more expensive than Sydney or Brisbane, if you're an international airline, they will look at those metrics when they're deciding where to place their new routes. So, internationally we are - as Australia, we will be competing with other major cities for additional services and existing services.

COMMISSIONER BAXTER: And presumably - sorry, can I just follow that - the airlines that stop at, say, Singapore, also balance as to how much fuel they put in a tank or an aircraft, say, leaving Melbourne or leaving Sydney, and how much they then top up when they get to Singapore or to, say, Hong Kong?

MR GANDY: Yeah. Yes.

COMMISSIONER KING: Did the airport - I mean, as part of the negotiations, obviously, the open access would have been something that would have taken time and effort to get in the agreement. So, did Melbourne Airport do, sort of, due diligence test to see if the prices of fuelling the plane were higher at Melbourne than, say, Sydney or Brisbane, or did you get information from the airlines to back up their concern that the prices were higher? I mean, what evidence did you have that the prices actually were higher at Melbourne, so that this fear that you had, of the internationals moving to other airports, was justified?

MR ELLIOTT: I am not sure how much - - -

MR GANDY: Yes.

MR ELLIOTT: Well, I'm not sure - we had feedback from different parties, but it's more anecdotal than anything else. People are not willing

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to share, and most often aren't able to share, the specific information. So, in terms of having a view on relative fuel prices between destinations, we don't have that exact information, but based on the feedback that we were getting from the airlines we thought it was more than worthwhile to ensure that we had open access. There's no downside to including the open access.

COMMISSIONER KING: Yes.

MR ELLIOTT: As long we've got a competitive market we can't be doing anything more than that for our customers.

COMMISSIONER LINDWALL: Would you see a benefit in greater transparency in pricing and other terms and conditions?

MR ELLIOTT: Yes.

COMMISSIONER LINDWALL: The PC has powers under s.48 of our Act to obtain information necessary, if we wish to, should be exercise that power.

MR GANDY: That's an interesting question. I think the piece for me is, in terms of the airport and the airport's lens, are we providing what we think we need to locally to enable the best possible outcome for our customers? And for that we've looked at it in terms of, are we able to match the growth that airlines are saying that they want into Melbourne with the provision of infrastructure?

COMMISSIONER LINDWALL: Yes.

MR GANDY: We think we've covered that off, and are we enabling other fuel suppliers to enter the marketplace? How you then determine whether you need to look at prices or not is really, I would suggest, whether there's a need to explore more into the supply chain outside of the airport, more than anything else, and how that works.

COMMISSIONER KING: I just want clarification. Presumably the price negotiated with the airlines by the oil companies is a CIF price into tanks at airport, not an FOB price. What is it?

MR GANDY: I don't know. I don't know.

COMMISSIONER LINDWALL: I think they'd be with the airlines, yes. The Victorian Government, as far as I understand, promoted a consultative forum of a sort to - between the airlines, fuel companies, and

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airport. Has that been successful, and would you like to see that continue? And I think the Department of - federal Department of Infrastructure thinks that a consultative forum would be quite helpful too.

MR GANDY: Yes. So - and you can say a bit more on this as well, Scott. I think the roundtable that was established actually demonstrated the importance from all players. So, federal government was at the roundtable, state government as at the roundtable, airport in terms of the infrastructure provision at the airport, and also airlines and fuel suppliers. So, you've got all of the important people on this subject in a room talking about what was effectively outside of the Melbourne Airport JUHI and starting to look at, "Right, so what do we see in the next 20 years as being enablers for great fuel supply at Melbourne Airport", and looking into that upstream supply piece. So, from our lens it was - we welcomed it and we supported it with our attendance, and it was great to see it supported by the industry in general.

COMMISSIONER LINDWALL: And is it likely to continue then?

MR GANDY: We hope so, yes.

COMMISSIONER LINDWALL: Yes. Does it require anything - I mean, do you think the PC should be recommending that type of - that forum be around the country, basically, along the same type of structure, with state, federal, airlines, airports, and fuel companies all participating?

MR GANDY: Yes. I think it's - it depends on the - what you're trying to solve at your particular airport. As I think we said at the start, all of the airport - - -

COMMISSIONER LINDWALL: Everything is different, yes.

MR GANDY: All of the airports are different. This was a great mechanism, and is a great mechanism, for dealing with the challenges we've got at Melbourne.

MR ELLIOTT: Just generally on the forum, while there was no specific authoritative decision making capability of that forum, simply having the transparency and having all stakers - stakeholders involved in the discussion was extremely helpful in flushing out some of the issues we were dealing with and then ensuring that everyone was aligned in terms of how we were going to go about solving them, so.

COMMISSIONER LINDWALL: Can I go back to the open access and ask another question, which is more of a theoretical question, that you've

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got a particular open access regime with fuel companies participating in the JUHI. How would you compare that to an alternative where there's a JUHI and fuel companies are not participants in the JUHI, and in fact some third party, or the airport itself for that matter, is the actual equity holder of fuel infrastructure, and then they have open access to fuel companies to bid for that?

MR GANDY: So, are you - can I just clarify my understanding? So are you saying that fuel companies would be enabled to - - -

COMMISSIONER LINDWALL: Would not be - not part of the JUHI.

MR GANDY: Would not be. Right. So they'd just be (indistinct words).

COMMISSIONER LINDWALL: It would be some third party operative independent agency, yes.

MR GANDY: Yes. Yes, we think that could work.

COMMISSIONER LINDWALL: I think Northern Territory, and we're going to hear from them, have that type of arrangement.

MR GANDY: Right, yep.

COMMISSIONER LINDWALL: Sorry, Stephen.

COMMISSIONER KING: When you were considering for renegotiation to lease did you consider alternative approaches? For example, did you consider Melbourne Airport taking back the JUIH infrastructure, and obviously that - you've decided not to do that. I'm interested in why, why have you decided not to go down that route.

MR GANDY: I think it comes back to core business that you're directly operating and that you have experience in, as opposed to enabling other core businesses to operate on your site in a way that still enables the ongoing growth and commerciality of our business, so - and we did look at a number of options, but came down to, probably from a risk-based approach, that actually the incumbents had a lot of knowledge around how to operate a good - at that time good relationships with the network of airlines that existed, and we were able to do an agreement with them. Ultimately, if we weren't able to do an agreement with them we might have chosen another way.

COMMISSIONER KING: Yes, yes. I guess that's a reasonable point.

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COMMISSIONER LINDWALL: Are you able to run through what sort of - you mentioned "We considered some other options", but you discarded them. What sort of options were you looking at?

MR GANDY: Oh, pretty much the ones that you spoke about, but these were high level reviews when we started the process, as to do we stay with current incumbents, do we look at doing it ourselves? We quickly got to a point of going "No, we're not a fuel supplier and we're not a fuel operator", and looking at third parties.

COMMISSIONER LINDWALL: Okay. So I note BP, in its submission, mentioned that you embarked on an open tender process for fuel infrastructure as part of the lease process. Is that one of the options that you considered and moved down the table a bit further? Just a bit more background on that would be useful.

MR GANDY: Do you want to talk about that piece, or?

MR ELLIOTT: That was actually before my time at the airport. But that was one of the considerations, and there was a tender process run. It only made a certain way through that process where, as Simon said, once that was - the pros and cons of that tender process and continuing that as opposed to continuing down the path that we had with the JUHI.

COMMISSIONER KING: Are you able to elaborate on - because that one seems to be, you know - it went past the sort of high level "Let's think about these. No, this is the way to go."

MR ELLIOTT: Yes.

COMMISSIONER KING: I mean, if you actually got into the tender process.

MR ELLIOTT: Yes.

COMMISSIONER KING: So, it would be useful to know what came out of that process that led the airport to say "Ah, this isn't the way to go. We'll renegotiate with the current owners."

MR ELLIOTT: I'd have to take that on notice and come back to you with more information.

COMMISSIONER LINDWALL: The other day we heard from Bioenergy Australia, I think, and it was about biofuels and the trial they

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had in Brisbane, which had some problems, principally - and we'll ask Brisbane Airport later on, but about having to be tested, I think, five times I think it was testimony on Wednesday, and compared to only once for the fuel.

MR GANDY: Right.

COMMISSIONER LINDWALL: What would be - well, (a), what do you think about biofuel - but from what I understand it's a more dense form or fuel and has fewer impurities - about entering the - your JUHI, and how would that work with your current open access, I guess?

MR GANDY: Yeah, it's interesting. I wouldn't know the details from a fuel specialist perspective. I don't think there's anything in our open access that precludes a biofuel being provided. There are standards that the fuel companies operate to, and they're specified as part of the open access regime, so whether it forms part of that or not I just don't know. It's just not an area of specialism that we have.

COMMISSIONER LINDWALL: Ken, have you - - -

COMMISSIONER BAXTER: No, I've got no - - -

COMMISSIONER LINDWALL: Did you have anything?

COMMISSIONER KING: Yes. Sorry, we're going to be jumping about a bit, a little bit.

COMMISSIONER LINDWALL: Yes.

COMMISSIONER KING: Just coming down to the open access regime, and understanding it's early days, and obviously you, the airlines, the suppliers, and ourselves will be very interested in how it goes. Is there a process in place to evaluate whether the open access regime is actually working? Is there a process by which the airport is involved, for example, if there's complaints about, you know - some of the parties come back and say "Oh well, yes, we tried to get open access but we found our fuel was being tested five times every time we tried to put it into the JUHI storage facility, so it - you know, it hasn't worked for us"? Is any of that mechanics built in to be able to check, "Yes, this is working", or "No, this needs further negotiation and a rethink? Is that part of the airport's strategy?

MR GANDY: Yes. No, it's a good question. What we've established with the agreement that we've got with the JUHI is regular sessions to

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review not just the progression of infrastructure and the operation, but also to do a once a year check and say "So, how are we going. We're going on the journey as intended in line with the agreements that we've got in place, and open access would be one of those that we'd revisit and look at and say "So, what's the reaction been", and the JUHI have in the past shared the names of organisations that have applied, and we've contacted them to say "So how's it going from your lens?" So, as we say, early days, but we'd see that continuing probably on an annual basis, just to keep tabs with the requirements in the agreements that we've got.

COMMISSIONER KING: Okay, and presumably not - you mentioned the parties that you contacted.

MR GANDY: Yes.

COMMISSIONER KING: Presumably access seekers, but also would you be talking to the airline about whether they see any difference, any improvement, or - - -

MR GANDY: Generally we would, but again, we're not going to get into the - we couldn't be able to determine whether or not they've got a commercial price and agreed.

COMMISSIONER KING: No.

MR GANDY: So to that extent it's really how well they can negotiate with fuel companies. At the end of the day we'd be talking about the provisions we've got in the agreement and saying "Yeah, we think they're working, and we are keeping pace with growth, and we're enabling people to access the JUHI should they wish to.

COMMISSIONER LINDWALL: But presumably - you mention anecdotes from the airlines were an important input to the decision.

MR GANDY: Yes.

COMMISSIONER LINDWALL: So presumably you'll be looking for the anecdotes to change, if I can put it that way.

MR GANDY: Yes, but we'd kind of sense check in balance with all of the other things that we're seeing as part of the agreement, so, it's - the idea is we build relationship rather than we just get a contract out every time somebody writes to us.

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COMMISSIONER LINDWALL: No, understood. So, when - of course you're about to embark on a parallel runway being constructed, which will change the tarmac area and the apron areas.

MR GANDY: Sure.

COMMISSIONER LINDWALL: Obviously I would - they would affect the fuel supply within the - that area. How will that be provisioned? Is it through this lease or separately?

MR GANDY: No, it's through this agreement.

COMMISSIONER LINDWALL: Okay.

MR GANDY: And what we do is, we do a check every five years, which starts to look at "So, where's the next agreement going? What's that infrastructure requirement and how does that then link in with what the infrastructure requirement is in the JUHI and in the hydrant infrastructure. So the two start to move in parallel with each other.

COMMISSIONER LINDWALL: Okay.

COMMISSIONER BAXTER: Can I just follow up on that? In the current arrangements is the JUHI pipeline operating at full capacity, or has it still got available capacity in it to - if one of the airlines decided to, say, shift taking on fuel from, say, Sydney to Melbourne? What's the capacity of the pipeline at the moment?

MR GANDY: Have we got the capacity?

MR ELLIOTT: We don't have the exact numbers, but it's very close to capacity.

MR GANDY: Yes.

COMMISSIONER BAXTER: Close to capacity. So if there was an increase in demand via Melbourne there would have to either be changes in the arrangements in terms of fuel delivery to Melbourne Airport.

MR GANDY: Yes, that's right. So, the - and the fuel providers would look at whether they're going through the pipeline or going through the bridger units.

COMMISSIONER BAXTER: As you were talking about a second pipeline earlier.

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MR GANDY: Yes.

COMMISSIONER BAXTER: Yes. Okay. Do you have any more questions?

COMMISSIONER KING: No (indistinct words).

COMMISSIONER LINDWALL: I have to take this slight leftfield one here. In the Australian today it says:

> *Luxury shopping strips within international airports are being blamed by BARA for distracting and confusing passengers to the point of causing flight delays.*

And it's - and it says Melbourne and Sydney and so on. Do you have anything to say to that?

MR GANDY: It's interesting, isn't it? Not in relation to fuel supply, no.

COMMISSIONER KING: We were wondering whether you should employ people with pitchforks to push the passengers down, but - - -

MR GANDY: Yes. No, that's not the way to load aircraft these days. It might have been at some point, but not today.

COMMISSIONER LINDWALL: Well I note, Simon, that you've been doing quite well with Movember.

MR GANDY: Thank you very much.

COMMISSIONER LINDWALL: I understand you're having to shave off this afternoon or this evening.

MR GANDY: Can't wait, yep.

COMMISSIONER LINDWALL: You can't wait. So, thank you both, Scott and Simon, for attending today.

MR GANDY: Thanks very much.

MR ELLIOTT: Thank you.

COMMISSIONER LINDWALL: Going to keep going, or you - - -

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UNIDENTIFIED SPEAKER: More than happy to keep it going. I'm just stretching, so.

COMMISSIONER LINDWALL: Now, I just wanted to check if Ian is on the line from Northern Territory Airports.

UNIDENTIFIED SPEAKER: (Indistinct words.)

COMMISSIONER LINDWALL: (Indistinct words.) Just a five minute break then?

UNIDENTIFIED SPEAKER: We just had someone join the meeting.

COMMISSIONER LINDWALL: Hello, is that Ian? We might just - - -

MR KEW: Yes it is.

COMMISSIONER LINDWALL: Brilliant. Are you happy to continue?

UNIDENTIFIED SPEAKER: Yes.

COMMISSIONER LINDWALL: Hello. Is that Ian? Could you introduce yourself for the record, and perhaps make an initial statement, if you're right to continue?

MR KEW: Yes, I'm happy to do that. My name is Ian Kew and I'm the CEO of Northern Territory Airport, and thank you for the opportunity to attend, by phone, this hearing. Northern Territory Airport put a submission in to the Economic Regulation of Airports. We did touch on the issue about testing the supply. We support and agree with BARA's submission that there should be open access of JUHI joint venture facilities at Australian international airports, and indeed in 2017 Darwin International Airport secured open access for its JUHI facility. Previous, since the airport had been constructed in 1991, only two oil companies, Shell and BP, who constructed the facility at that time, had marketed fuel to airline customers at our airport.

So, at the end of the lease we negotiated an arrangement whereby we bought into the existing fuel infrastructure. We purchased 40 per cent of it, with an additional 20 per cent to be bought every three years until, at the end of 12 years, we would own all of the existing infrastructure. All new fuel infrastructure we will invest in ourselves, and we will - as a consequence of that we have organised (indistinct words) it is now an open access regime, and at Alice Springs we are attempting to do the same

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thing. The leases with the oil companies there, Shell and BP, have lapsed. Those facilities at Alice Springs are 50 years old, almost, and we are very keen to upgrade them and modernise them and provide appropriate facilities for the next decade or two.

We found, during the process of buying into the existing infrastructure, that there was some support from the - strong support from BARA and some of the airlines, but at least one airline was not supportive of airport investment in fuel infrastructure, and indeed was quite happy to have the status quo remain for the future. I think that is about all I'd like to say in our - my opening statement.

COMMISSIONER LINDWALL: Thank you very much, Ian. This is Paul Lindwall. I'll get my colleagues to introduce themselves when they ask you questions. When you considered going through this process, I mean, firstly could I ask, because you've got the initial 40 per cent and then 20 per cent acquired over the years before taking 12 years to acquire all of the existing infrastructure, do the fuel companies continue to have a say on their current shares for that period, until you actually acquire all of the share?

MR KEW: Yes, of course they do.

COMMISSIONER LINDWALL: Yes, but they have to agree to that open access regime, as you say.

MR KEW: They have agreed to that open access regime. We've put in place, as best we could understand, appropriate arrangements for that. There has yet to be another oil marketer, market fuel through the facility yet, but we are hopeful that will happen. Those open access regime requirements were embedded into the new leases that we provided to Shell and BP.

COMMISSIONER LINDWALL: Okay, and since you've created this open access regime what have you observed, perhaps in prices and supply, by other companies apart from Shell or BP?

MR KEW: Okay. Well as I mentioned, there has not been another company, and it's only less than 18 months or so since that happened.

COMMISSIONER LINDWALL: Yes.

MR KEW: And we don't know what billing arrangements and contracts were in place, but we've had a lot of interest from other oil marketers who were very keen now that it is an open access regime, and we know that

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they're talking to the airlines. The other thing that we heard early on was that the - just the sort of increased competition reduced fuel prices, but we don't get to see what prices they charge. Fueltrac and other organisations like that do monitor jet fuel prices around airports in Australia, and that's the information that we had at that time.

COMMISSIONER LINDWALL: Okay, and as for the airline you mentioned that didn't like the change, and you may - I assume you're not going to tell us what the name of the airport - airline is. I suppose I could say that it might be Qantas, but who knows? What do you think is the reason for their reluctance to agree to that arrangement?

MR KEW: Well look, I can only speculate, but I would - if I did speculate I would have thought that if you'd have the most market power, and by that I mean purchasing power and supply chain power, especially if you're an importer yourself and you're one of the major fuel buyers in Australia, then why would you want a level playing field with your competitors?

UNIDENTIFIED SPEAKER: Correct, yes.

COMMISSIONER LINDWALL: Not knowing who the airline is.

UNIDENTIFIED SPEAKER: No, not at all, no.

COMMISSIONER KING: Ian, Stephen King here. You mention the prices of fuel and in your original submission you stated there were indications on a like for like basis Darwin jet fuel cost has reduced because the market is not contestable. I understand, of course, you're not privy to the exact contracts, but what's the basis for that? What is the basis for that remark and your comment here, that you think the potential for competition has pushed those prices down?

MR KEW: Well we were advised of that by some consultants that we were using at the time who regularly monitored jet fuel prices as published by Fueltrac around Australia. so, they - you know, Fueltrac monitors retail gasoline prices, diesel prices, and jet fuel prices, and the information they had at the time was that jet fuel prices at Darwin reduced after we made those new leasing arrangements.

COMMISSIONER LINDWALL: Okay. Any comments from the airlines themselves that you've heard, that they've seen the difference, or?

MR KEW: Oh, I think initially some said that their prices had gone up because the increased costs, but we believed, and we certainly still

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believe, that that initial increase was quickly wiped away by the source of increased competition. So, other fuel marketers knocking on the airlines doors, I think - you know, I'm not privy to what happened there, but I can only assume that they - you know, that now that it is an open access regime they've been much more competitive in their pricing.

COMMISSIONER LINDWALL: Okay, and the terms - what would you say about the transparency of, now that you've got an open access, should there be greater transparency about the types of arrangements so that a potential supplier can look up very quickly and easily the types of terms that are available at - to have access to your network?

MR KEW: Yes. That transparency and the details about what are the arrangements for the open access regime are all embedded in the lease, so there is a requirement by BP and Shell to provide all of that information to any competent fuel marketer, and we know that that has happened because we've talked to fuel marketers who have looked at the arrangements, because they are very interested in being a supplier of jet fuel to Darwin Airport in the future.

COMMISSIONER LINDWALL: Would you describe your open access arrangement similar to the one in Hong Kong, which of course is a different airport by a long shot, but that's been put to us as - or by BARA, for a start, as an example of the gold standard for open access?

MR KEW: I don't know the details for Hong Kong open access regime. We work through here with not only the existing oil companies, BP and Shell, but we also went to other oil companies that were keen to market fuel, so that we road tested the open access regime that we embedded into the lease with other companies like Caltex and Exxon and those, to make sure that they were somewhat comfortable that the open access regime that we were proposing would work.

COMMISSIONER LINDWALL: Yes, yes. Now - sorry, Stephen.

COMMISSIONER KING: Sorry, just a fairly mechanical question, because not - just on the - you've got the JUHI facilities, the storage facilities. Presumably there's a pipeline that comes to the airport from the port of Darwin.

MR KEW: No, there isn't, but that's a project that we have proposed publicly, and we are seeking to do that. Of course, when we were not a participant in the facility before we had no way that we could, you know, organise or make happen the connection between that pipeline and the facility. Now the pipeline, if and when it is built, and we're certainly

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proposing that, we will fund that ourselves. We will obviously want the oil companies to use that, but it will have to be priced competitively against road transport. We understand that, but there are some real economic, environmental, and safety advantages of delivering the fuel by pipeline compared to road transport.

COMMISSIONER LINDWALL: Yes, so just to be clear, at the moment is all the fuel at Darwin Airport trucked in to the airport?

MR KEW: That's right.

COMMISSIONER BAXTER: Okay, and sorry, on that trucked in, from the port of Darwin, or trucked in from Adelaide?

MR KEW: Yes. It's a long way from Adelaide.

COMMISSIONER BAXTER: I know, but there's still a lot of stuff (indistinct).

MR KEW: Three thousand kilometres to deliver 100,000 litres of fuel.

COMMISSIONER BAXTER: Yes.

MR KEW: No, it's trucked in in double road trains from the port of Darwin.

COMMISSIONER LINDWALL: Okay. Now, as a result of your purchase, I think you've introduced a fuel throughput levy. How has that levy been structured and set, and what consultation did you have with the participants, like the airlines, about the setting of that levy?

MR KEW: Okay. We've had that fuel throughput levy in place for probably ten to 15 years. So, we've continued the fuel throughput levy in the new lease, but it was payable under the old - we had the form of the old - one of the FAC (indistinct words) fuel throughput levy, and we did apply that.

COMMISSIONER LINDWALL: Okay.

MR KEW: So it's always been there, for a long, long time. Our rate is consistent because the way that it was determined at the time of introduction was that it had to be consistent with rates applicable elsewhere in Australia. So that's why they are all somewhat similar at the moment.

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COMMISSIONER LINDWALL: Yes.

MR KEW: And we would continue to charge the fuel throughput levy. We view the fuel throughput levy as part of the economic rent for all the site, and you know, that - charging of a levy like that or a reverse rebate was not inconsistent with what the oil companies did for getting access to blocks of dirt that delivers huge volumes of fuel, whether it be retail fuel, petrol to cars, or diesel to trucks. They quite often paid a site rent and then they paid a rate per litre as well.

COMMISSIONER LINDWALL: Okay.

MR KEW: We see the fuel throughput levy as very consistent with what the oil companies have done outside of airports for the last 50 or 60 years.

COMMISSIONER LINDWALL: Has the levy changed since you've moved to your new open access regime?

MR KEW: I think it just moves by CPI. So there was no change in the structure of it when we moved to the new lease and the new open access regime.

COMMISSIONER LINDWALL: Okay, and what was the catalyst for moving to the open access? Was it the leases for your - the existing JUHI with the fuel companies coming to the end, or was this something that you thought would - your customers, apart from one of them, were pushing for, or - it was something that you initiated yourself, obviously, but what was the process, if you could describe to us, of moving from the old arrangement to the new arrangement, and did you have to terminate any leases early?

MR KEW: Sorry, I must go back and correct the statement about the fuel throughput levy.

COMMISSIONER LINDWALL: Oh, okay.

MR KEW: I was incorrect in saying that we charged it on the RPT Apron service of the JUHI. We charged it here on the general aviation facility only, not on the JUHI, and we also charged it on the JUHI facility at Alice Springs, but not at Darwin.

COMMISSIONER LINDWALL: Oh, okay.

MR KEW: So, I mentioned earlier that there were two forms of leases, one where you could charge for fuel throughput fees, and it was

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determined independently, and that's why the rates are nearly all the same. We did that at Alice Springs and we have done that for ten years or more. We didn't do that at Darwin because the form of lease here could only - a fuel throughput fee could only be introduced if and when they became commonly due and paid around Australia. So, I was incorrect and I just wanted to correct that.

COMMISSIONER LINDWALL: Oh, thank you. No, that's all right. So, if - - -

MR KEW: Certainly I should also say that we did, now, introduce a fuel throughput levy with the new lease, so I want - I want that to be clear.

COMMISSIONER LINDWALL: So there is now one on the JUHI at Darwin?

MR KEW: YEs, there is.

COMMISSIONER LINDWALL: Ah, okay.

MR KEW: So, apologies for any - - -

COMMISSIONER LINDWALL: That's all right. No, I just want to - - -

COMMISSIONER KING: Sorry, just to follow up on that.

MR KEW: Yes.

COMMISSIONER KING: Is fuel throughput levy on the JUHI at Darwin - is it the same as, you know, just CPI adjusted from what the fuel - more limited throughput levy was before, or - - -

MR KEW: Yes it was. It was consistent with what we were charging at Alice Springs, and also at the - at the general aviation arrangements here in Darwin; it's a separate facility. It's not an underground hydrant facility. It's where they pump fuel to planes by tanker truck.

COMMISSIONER KING: Yes.

COMMISSIONER LINDWALL: Can I just ask, have you had - I know you don't know the actual contracts between the jet fuel suppliers and the airlines, but did you get feedback from the airlines when you introduced the more general throughput levy, and my reason for asking that is my reaction would be that if you put a throughput levy on the only thing that

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happens is the fuel companies pass it through to the airlines. Any evidence that I'm either right or wrong in that conjecture? What did the airlines say to you? Were they - did they say anything? Were they upset by you putting the - or extending the levy? Just some thoughts on that.

MR KEW: Well I think airlines have consistently not wanted to have a fuel throughput levy applied because the oil companies have written into their agreement that if one is applied that it will be passed through, and I would suggest that probably reflects the lack of competition for jet fuel supply on airports, that any costs that they incur, that they can just pass it through. You know, they'd incur lots of costs. Not all of them are passed through, and indeed many are in the - in the presence of a strongly contestable market with lots of competition, then that's just another charge. The fuel throughput levy really is a form of rent for the site, and, you know, we - we of course - we seek and recover return for that facility in a number of ways: a fuel throughput fee, a site rent, and also an infrastructure charge for the investment that we make there. So - and you know, we've obviously got costs associated with the infrastructure now we've bought into it, and also the maintenance for some of the structure.

COMMISSIONER LINDWALL: Now, could I go back, Ian, to the question I was asking, which was about the process you moved to open access? Did you have to terminate any existing leases, or was this a new agreement really at the end of previous leases?

MR KEW: We didn't have to terminate the existing lease because the lease expired.

COMMISSIONER LINDWALL: Okay.

MR KEW: And we reached an agreement with them to enter into a new lease at that time.

COMMISSIONER LINDWALL: Okay.

MR KEW: It wasn't easy to reach that agreement, but we did.

COMMISSIONER LINDWALL: And could I ask about, if we now move away a little bit, and we might come back to it, but about the security of supply to Darwin and Alice Springs, because that has been an issue, and obviously, as you say, they're currently trucked in. how much disruption are you - do you ever have any black light or red light events, traffic light events, and what contingencies do you have to ensure that you have sufficient fuel looking forward?

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MR KEW: Well indeed, that was probably one of the initial reasons why we looked at investing in fuel infrastructure here, because we believe that there - that we have only limited tankage jet fuel storage here, and we wanted to - that to be increased. The oil companies were somewhat reluctant to invest in it, and would only invest if they got a new lease - new long-term lease on the - on similar terms.

COMMISSIONER LINDWALL: All right.

MR KEW: So that's what got us, firstly, interested in it. So now we are preparing with the oil companies - and we'll talk with the airlines - a long-term investment program for updating the fuel infrastructure over - you know, in five year blocks. So that's what we're doing, and we will be investing in new extra tankage at Darwin Airport within the foreseeable future. So going back to the supply arrangements into Darwin, all of the fuel shipped into Darwin. It's stored in one facility that's owned by Vopak at the port, and all of the products move through that one facility, so - and because it's only 16 kilometres away we're probably at risk, because Vopak is undertanked in some ways, and that the civilian fuel facility here at Darwin Airport is undertanked.

So that does put us at risk if there is a supply chain hiccup, and indeed, on the other side of the airfield here is RAAF Base Darwin, and - and in August we had, you know, the largest military exercise in Australia, Exercise Pitch Black, and anecdotally we heard - I think it was raised in parliament - that there were restrictions on flying towards the end of that program because of limitations of jet fuel availability through the port facilities.

COMMISSIONER LINDWALL: Okay. So, what's the average daily margin you've got of the tanks currently at Darwin?

MR KEW: Well I think we've got about 1 million litres of storage, and the throughput on an annualised basis is about 130 million litres, so what, we've got three days storage or something like that.

COMMISSIONER LINDWALL: Okay, which is about what I think IATA says is about right. I mean, that's compared to Melbourne. They testified, I think it was, 1.2 days they had.

COMMISSIONER KING: Yep. Can I just - I - - -

MR KEW: It depends on how much fuel you've got pushing up the supply chain into it, so - but yes.

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COMMISSIONER KING: Sorry, and I just want to clarify something that you mentioned. So there are plans for more tankage at Darwin Airport I think you said, and you mentioned the importance of long-term - the long-term lease for the oil companies to invest. Is that investment in new tankage - the airport is investing in that, or funding it, or is it the oil company?

MR KEW: Yes.

COMMISSIONER KING: Okay.

MR KEW: So, to be quite clear here, we entered into a new 15 year lease with the two oil companies. We would own all of their infrastructure - existing infrastructure at the time of the commencement of the lease within 12 years.

COMMISSIONER KING: Yes.

MR KEW: So, 15 years down the track, or 14 or 13 years down the track, we will go to market for a new operator in a facility that we fully own and control ourselves at the end of it. Any new investment during that 15 years, like today, if we were investing today, will be funded by us. So the oil companies don't need to ask for a long-term lease because they're investing their own money; we're investing all the money. We invest, you know, $50 million a year into aviation infrastructure here, runways, taxiways, aprons, terminals. There are only two things you need to make an airport operational: a runway and fuel. So we really - we're of the view, in our airport business, that it's an appropriate long-term investment for us, that we should market, plan and control, and invest in the fuel infrastructure on our airport.

COMMISSIONER KING: Okay. Who is the operator during the current lease? Is it Shell or BP, or who?

MR KEW: It's both of them together in a joint venture arrangement.

COMMISSIONER KING: Okay, so - okay, so they're jointly operating it. Just one of the things that - - -

MR KEW: BP are the operator. I should say, BP are the operator.

COMMISSIONER KING: Okay.

MR KEW: They both have leases, but - and they obviously choose who the operator will be.

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COMMISSIONER KING: Yes.

MR KEW: And it might be different at different airports.

COMMISSIONER KING: Yep.

MR KEW: But they're in it together, but BP are the - have the physical staff and do operate it themselves.

COMMISSIONER KING: Okay, at Darwin. We've been - just coming back to the open access regime you've put in place, we're being informed by some other parties at other airports about, perhaps, the non-price barriers that can be put up to gaining access. Has the airport, or have you, put in any processes to be able to evaluate over time how successfully that open access is going? Is there a way, for example, that a fuel company that feels that it's actually not getting appropriate access - perhaps it appears that the conditions in the lease agreement are being met but there are many ways that an operator who has a vested interest could - could make it difficult for a new supplier. How are you dealing with those, or how do you intend to deal with those sort of issues over time?

MR KEW: Okay. Well in the lease we tried - we attempted - Your Honour, hopefully we're successful. We put in some clauses there around the access regime, that there had to be non-discriminatory pricing for the - for the terminaling task. So, you know, the price that BP would charge, theoretically, Caltex should be the same price that they would charge themselves for the task of moving the fuel through to it. So it would be - for example, in this instance there would be Caltex putting their own fuel from a ship into the Vopak terminal tanks at East Arm. That would be tracked by a Caltex contractor to the site here, and the fuel would be managed through the site and into the plane by BP.

BP's charges to do that to Caltex should be similar - similar to the prices that they would charge themselves. Now, whether that happens in reality or not time will tell. I guess we'll know that it's been successful if other oil marketers start selling fuel through the facility, and we're certainly in constant conversations with other oil marketers who are keen to do so.

COMMISSIONER KING: Okay. Presumably the Vopak facility is a common user facility.

MR KEW: It is.

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COMMISSIONER KING: Yeah, so do you know - presumably the fuel is tested and made sure that it's up to spec before it goes into the Vopak facility; is that correct?

MR KEW: As the fuel is taken off the ship it is tested and stored in Vopak. As it is taken out of the tank at Vopak it is tested as it goes into a truck.

COMMISSIONER KING: Yep.

MR KEW: As it is taken out of the truck and put into the tanks here at Darwin Airport it is tested again, and as the fuel is delivered and about to go into the plane it is tested along the way. So there are many testing processes along the way to make sure that the quality and the integrity of the jet fuel is correct.

COMMISSIONER KING: Okay, thanks.

COMMISSIONER LINDWALL: In your submission and what you just said today, Ian, you said that - in the wording in the submission it says

> *There are indications on a like for like basis that Darwin jet fuel costs has reduced because the market's now contestable.*

Is that evidence based upon this Fueltrac monitors, or is there something else that you've got that would support that?

MR KEW: No, that's what we were told at the time based on the Fueltrac monitoring.

COMMISSIONER LINDWALL: Okay.

MR KEW: We have got no other evidence to support that claim.

COMMISSIONER LINDWALL: No, that's all right, and several stakeholders, including the Department - federal Department of Infrastructure and BARA have proposed a jet fuel planning coordination forum between airports, airlines, the jet fuel suppliers, the governments, could discuss incapacity and investment constraints and future demand forecasts. Do you think that would be a useful process for Darwin Airport and perhaps Alice Springs Airport too?

MR KEW: Personally not really, but that's - it sounds like a big group, but you know, there are lots of dynamics in all of that. My background to this, just so that the Commission is aware, was that I worked for Exxon

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for two years and then Shell for 20 years, and one of my roles was Northern Australian Manager for Shell, running the distribution task and tank farms and everything else. So I have had a strong understanding of the supply chain and the marketing arrangements and how they work.

COMMISSIONER LINDWALL: I would suggest that - please go on.

MR KEW: And, you know - and I was involved in forums in that role, you know, in a planning role with, for example, the RAAF around Australia in a partnering arrangement to - you know, to look at those things, jet fuel supply and everything else. I think a large group like that - I'm not going to say that it shouldn't be done, but I just can't see it adding much value in a place like Darwin.

COMMISSIONER LINDWALL: Okay, okay. It may be different, obviously, in the larger airports like Melbourne or Brisbane or Sydney and Perth.

MR KEW: Yes, because there are different supply chains in there - road and pipelines that are owned by different people.

COMMISSIONER LINDWALL: Yes.

MR KEW: And you've got many more participants as well.

COMMISSIONER LINDWALL: Do you think your long background in working for Exxon and Shell has helped you reach the conclusion that an open access regime which doesn't involve the fuel companies is an optimal system?

MR KEW: Yes I do. I mean, really, from - just from my perspective, the JUHI arrangements around Australia are probably the last bastion of where the oil companies will have, you know, much - a much greater level of control over their market and their customers than any other retail fuel business. You know, it doesn't exist in the high street for gasoline retailing or a road transport terminal for diesel, or anything like that. So, you know, the fact that so few JUHI arrangements have changed over the last 40 years is a testament to the structures that were put in place at the time, for very good reasons, around refinery access and, you know, airports at that point in time didn't have the money and didn't want - didn't have the knowledge and expertise, and didn't want to invest in fuel infrastructure, but you know, in most other businesses, you know, you had company owned and company controlled service stations back in those days as well. You know, if the market today has to speed up and is much more competitive. Just it hasn't been the case on airports.

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COMMISSIONER LINDWALL: Okay, yes, and Ian, the - what do you think the minimum scale of an airport would be to justify a pipeline? You were mentioning that Darwin is - might consider building a pipeline at some stage in the not too distant future. What size of airport do you need to justify the major expense of a pipeline? Would you say Darwin's about that level, or anything a little bit smaller than Darwin?

MR KEW: No. Darwin's nowhere near that level.

COMMISSIONER LINDWALL: Okay.

MR KEW: The only justification for a pipeline here is to supply fuel to the military site, the RAAF Base Darwin.

COMMISSIONER LINDWALL: Oh, okay.

MR KEW: And what the pipeline does do, it won't be cheaper than road transport. With road transport in the Northern Territory, we can run double, triple, and quadruple road trains, you know, the most efficient way to move fuel on a road, but what pipeline can do is push up a lot more volume quicker than trucks could ever deliver it. So there are some strong strategic and from a supply chain resilience perspective, to have a pipeline delivering to their facility, and of course we can just T off on that to the civilian side.

COMMISSIONER LINDWALL: Yeah.

MR KEW: So, if you ask me what I would have thought you'd need, or the volume of fuel to go through a facility to justify a pipeline, I'd say it would be up around a billion litres.

COMMISSIONER LINDWALL: Okay.

MR KEW: Seven hundred to a billion litres a year. So, you know, seven or - six or seven times our volume at the moment.

COMMISSIONER LINDWALL: Yeah, okay.

MR KEW: So not many airports would require a pipeline, or could have a pipeline delivering economically, and of course that pipeline then, it's what's the cost to them and what's the cost to, you know, delivering it by road. There are lots of things in there, but I'd say, you know, getting towards a billion litres a year.

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COMMISSIONER LINDWALL: Okay, that's great. You, Ken?

COMMISSIONER BAXTER: Yeah, I've got a question on pricing. Have you got many airlines based in either Indonesia, Malaysia, or Singapore that fly into Darwin and refuel and go back to any of the Indonesian ports or Asian ports? And if so, do they refuel in Darwin, or do they basically refuel in the port of origin?

MR KEW: Good question. Most of the aircraft that come to Darwin are narrow bodied aircraft, so aircraft types like Boeing 737s and Airbus 320s. In nearly every instance the flight times to Darwin are four hours or so - four hours plus - except flights from Bali, which are two and a half hours here, so - and four and a half hours is getting towards the range of a narrow bodied jet. Particularly if you're flying over water, you need to effectively carry or reserve more fuel. So, I don't know the answer to how much fuel would be picked up by the Bali-based carriers here. I would - I don't know what the price of fuel is in Indonesia, for example, but if it's anything like - I think there was subsidised gasoline over there, so if jet fuel is similarly priced the, you know, they would probably pick up as much fuel at that end of the trip rather than this end, but I don't know the answer to that. But there's not - they can't - they have to carry a fair bit because they're flying over water.

COMMISSIONER LINDWALL: Did you have any questions?

COMMISSIONER KING: Yeah. Just a slightly different tack. Just coming back to the approach that you've taken with moving from the lease to, essentially, a movement of the facilities over to ownership by the airport. So, there's in a sense the two models. There's the traditional lease arrangement which you had. There's the model you've gone to, which is where the airport will essentially own the relevant refuelling facilities, storage facilities and so on, and we're aware of other airports that have that approach. Did you consider any alternatives to those two approaches, and if so, what were they and why did you choose to go in the direction that you did?

MR KEW: Well, yes, before we had the traditional lease with two oil companies, the (indistinct words). The new arrangement is we're progressively buying the infrastructure. We still have the leases with the two oil companies, but we have the open access regime as well. At the end of this lease term, 15 years, we would envisage, whoever my successor is, that then we would just go to market and have someone come in and operate the terminal. So, we wouldn't necessarily have a split lease with Shell and BP. We would have - we would go to the market, get the most efficient, capable, and cost-effective terminaler to run

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the facility, and then it will be a truly open access arrangement with, you know, not being controlled by one oil company, and they would be shorter term agreements and we would mark them to market, you know, probably a good five or seven years or eight years, or something like that.

So that would be the next iteration of the agreement that we would have. It was just a bridge too far to go to that in this instance, and that was predominantly around gaining an agreement for them to sell part of the infrastructure that we needed, the hydrant system. So, the next agreement down the track will be different to the one we've got today.

COMMISSIONER KING: Okay. I guess the other part behind my question, and you wouldn't have heard this because they were on before you this morning, but Melbourne Airport similarly have just renegotiated a new agreement, but they made a conscious decision not to go down the airport ownership route, and rather to go to a long-term lease with the oil companies, but - the existing JUHI participants, but with an open access regime under that. Did you consider that alternative sort of arrangement that Melbourne Airport has gone down, and I was wondering your thoughts on that?

MR KEW: No we didn't, because we wanted to invest the money and get a return on the capital ourselves, and Melbourne aren't doing that and won't get a return on the capital invested there for the next 20 years. Our business is about finding good investments where we can get, you know, good long-term returns, and there's nothing better than investing in runways and fuel infrastructure. So, that's - but every airport's circumstances are different, and the pressures and the timeframe at the end of their lease and what's happening is probably what dictates, you know, an - you know, their outcomes, but certainly we wanted to invest and we wanted to get a return on the investment.

COMMISSIONER LINDWALL: Well, Ian, did you have any final points, because I think we've asked you all the questions that we would want to?

MR KEW: No, nothing more than what I've said. It was a - it was, you know, quite difficult to put our arrangement in place, where we - we've gone a step of the way. We certainly hope that there will - this will encourage competition in jet fuel prices, because that's very important for airports to have - have that competition and that low cost base, so that we can, you know, have lower airfares for people coming to our airport. So - and we also saw that having control over - and some control over the destiny about the investment into that critical infrastructure was import for ourselves as well.

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COMMISSIONER LINDWALL: Okay. Well, thank you very much for speaking with us today.

MR KEW: Thank you for listening to me.

COMMISSIONER LINDWALL: Okay, bye.

COMMISSIONER KING: Thank you.

COMMISSIONER LINDWALL: Well, I think we can have a bit of a break for morning tea. We've got wonderful cake out there and instant coffee if you want, I think.

COMMISSIONER KING: Hopefully wonderful cake out there.

COMMISSIONER LINDWALL: But the Productivity Commission doesn't go beyond the instant coffee, much to my complaints.

COMMISSIONER BAXTER: But it's great with cake.

COMMISSIONER LINDWALL: So, shall we - we might - it's 11.45 officially, but do you mind if we start a bit earlier than that? Maybe 11.40 or something.

COMMISSIONER BAXTER: Let's say 11.35.

COMMISSIONER KING: Yeah, we'll (indistinct), yep.

COMMISSIONER LINDWALL: Thanks very much everyone.

SHORT ADJOURNMENT **[11.16 am]**

RESUMED **[11.36 am]**

COMMISSIONER LINDWALL: Welcome. Mark, if you'd introduce yourself for the transcript, and then if you'd like to give an opening speech or statement.

MR WILLEY: Okay. I was proposing to give an opening statement, and within that statement I'll introduce myself. Am I able to be heard? That's going well?

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COMMISSIONER LINDWALL: The microphones are purely for the transcript.

MR WILLEY: Okay, so - and after that, happy to take questions and attempt to answer them.

COMMISSIONER BAXTER: Thank you.

MR WILLEY: So, Brisbane Airport Corporation Ltd, BAC - I'll refer to it as BAC from now on - is an unlisted public company that secured the long-term lease for Brisbane Airport, which commenced on 2 July 1997. That lease was secured through a successful offer to the competitive first tranche of airport privatisation bidding processes conducted by the Commonwealth Government, a process which eventually resulted in all Australian capital city airports, major regional airports, and major general aviation airports operating under privatised ownership regimes. So BAC is responsible for the operation, planning, and development of Brisbane Airport, which is currently processing around 24 million annual passengers, 210,000 annual aircraft movements, and has an on airport workforce of around 24,000.

As the Head of Airport Development within BAC's strategy - Strategic Planning and Development Department, I have lead responsibilities for Brisbane Airport's terminal development strategies, master planning, aviation capacity monitoring and growth, and the maintenance of industry relationships relating to those airport disciplines. Aircraft fuel services at Brisbane Airport are provided by the Joint User Hydrant Installation - JUHI partnership or joint venture - which is made up of the current participants, Air BP, ExxonMobil, Caltex Australia, and Viva Energy Australia, which is a recent partner, previously Shell. With the exception of ExxonMobil these participants provide inter aircraft operations, with each participant company having their own staff and vehicles to service the contractual arrangements they have established with airlines and aircraft operators.

The inter aircraft operations are a separate entity from the JUHI joint venture. JUHI hold long-term leases and licences for their main depot facility and the various fuel pipeline installations at Brisbane Airport. The JUHI facilities constitute a main depot site with large on airport fuel storage facilities and an administration building, an extensive and complex underground pipe network, an associated hydrant and valve put system, servicing both the international and domestic aircraft parking aprons. There is underground supply pipe connections to off airport regional bulk terminals that are under control of the supplying terminal,

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and the mobile equipment required to service aircraft are supplied and operated by the inter aircraft operators.

JUHI manages the storage and hydrant pipeline facilities. The into aircraft operators provide the into fuel services by fuel tanker to aircraft on non-hydrant equipped apron stands, and by hydrant car to aircraft stands equipped with hydrant systems. The arrangement between BAC and the JUHI participants is such that BAC licenses to JUHI the right to operate the storage facilities and network. Fuel supply and aircraft delivery is managed by the into aircraft operators directly with the airlines. Airlines are able to contract with any of the fuel suppliers in respect of their fuel requirements, in a competitive environment between the suppliers.

BAC does not have any visibility on the arrangements that fuel suppliers have with the airlines for the provision of bulk supply from regional fuel terminals to the on airport storage facility, the service level arrangements for into aircraft services or fuel pricing arrangements. BAC understands that each fuel supplier sales department brokers contracts with those end users for those services. Efficient, reliable fuel services are an essential element for major airport function, with feedback on this issue specifically elicited from the major domestic carriers confirming that they are satisfied with the services provided by the JUHI partnership at Brisbane Airport.

BAC, as does other major airport operators, receives notifications from the NOC oceanic fuel supply summary services of risks to aviation fuel supply delivery systems to Brisbane Airport in the form of a traffic light notification. Warning notifications that Brisbane Airport receives generally relate to late supply by shipping to the regional fuel terminals. At times there's also been warning notifications for out of spec shipping delivery. Fuel volumes consumed at Brisbane Airport doubled from around 1.6 million litres daily in 1995 over the following 20 year period, and will be around 3.75 million litres daily by 2020. JUHI currently has three bulk storage tanks. The number of tanks were augmented around 2011/12, the current capacity of around 6.4 million litres, providing around 1.5 to two days fuel reserve at Brisbane Airport.

The JUHI on airport bulk storage tanks have two supply feed pipelines, one to the Pinkenba Terminal and the other to the Bulwer Island Terminal. So they're terminals off airport. They're the terminals that shipping provide to. JUHI is currently in the final project stages of commissioning a fourth large storage tank of around 6.4 million litres. So that tank in itself is the same size as the rest of the storage tanks that exist at Brisbane Airport. That will extend the fuel volumes available for Brisbane Airport, catering for the expected short-term growth in airline services and frequencies, while maintaining a reasonable redundancy cover by

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extending the duration of fuel reserves. So that will extend out that one and a half to two days fuel reserve we currently have.

BAC meets regularly with JUHI on planning and development issues and has established agreements on project notification timelines, construction protocols, and cost allocation principles and responsibilities that guide the aviation fuelling response to aviation expansion projects and modification works to existing aircraft stands. It is expected that Brisbane Airport parallel runway system will reach peak hour operational saturation levels in the mid-2050s, at which time the aviation fuel demand is expected to be around 12 million litres daily. Aviation growth beyond that peak period saturation will occur with peak spreading into shoulder periods across the normal daily operating profiles, requiring even further daily fuel supply volumes. We're not sure how much that will be.

BAC will continue to engage with JUHI on planning and development strategies, and on the forecast level of aviation growth expected at Brisbane Airport, to ensure the development of a robust facility siting and staged expansion strategy fuel supply, fuel storage facilities and the into aircraft services. In consultation with the JUHI partners BAC is currently developing it's 2020 airport master plan, which will identify a medium to long-term strategy, 20 year, for locating the major airport fuel facilities and the facilitation of efficient aircraft servicing to a significantly expanded passenger terminal and aircraft stand footprint, including potentially completely new major terminal facilities.

COMMISSIONER LINDWALL: Thank you very much there, Mark. That new tank that you mentioned, which will double the capacity - because I think IATA says that three days' supply at tanks is about optimal, or more - at least three days. When is that likely to be in operation?

MR WILLEY: I believe within weeks or a month.

COMMISSIONER LINDWALL: Oh, okay.

MR WILLEY: It's a project that's been rolled out - been rolling out for some time.

COMMISSIONER LINDWALL: Okay, and you mentioned, of course, the strategic planning workshops you have with the JUHI, the joint venture - BAC does. I'm not sure if you're aware that the Department of Infrastructure and BARA, amongst others, have proposed a jet fuel planning consultative forum, and Melbourne has - was - operated

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something like that through the Victorian Government. What would be BAC's view on that?

MR WILLEY: That we would probably have an interest in understanding the scope or the terms of reference for that group and whether - as an airport operating company, whether we could add value to that process, or whether we could extract value from that process. I'm unsure of that at this stage.

COMMISSIONER LINDWALL: Yes.

MR WILLEY: It's - from our perspective at Brisbane Airport, that's probably more of interest to the airlines than the airport, as we are not involved in the provision of those fuel services.

COMMISSIONER LINDWALL: Yes, so - but overall you're - from what you've been saying, you're satisfied about the security of supply and the redundancy if there's a supply disruption, or?

MR WILLEY: We have - as demand has built up since the last tank was put in in 2011/2012, yes, the duration of reserves has reduced. So we have been concerned about that, and through those consultative processes with JUHI we've encouraged the delivery of a new tank, and this is a very large tank. It is a big project for the partners. You know, it's probably in the vicinity of $10 million dollars to install one of those tanks at an airport.

COMMISSIONER LINDWALL: Yes.

MR WILLEY: So it does take time, but it also takes time to get agreements among four equal responsible partners. So, we're positive about that, and obviously in securing that agreement JUHI also look forward to the length of tenure they have on that site, because they need to, you know, capitalise those costs over a certain number of years, and they - through the master planning process that we're going through at the moment JUHI have identified a pipeline, additional tanks, that would take us through to the 2050s, that - you know, that demand level I suggested of 12 million litres per day in the 2050s.

COMMISSIONER LINDWALL: Yes, yes.

MR WILLEY: So, there is an opportunity at Brisbane Airport if JUHI was to be successful in securing an even longer term lease, that they are able to address the demand at Brisbane Airport over that long period.

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COMMISSIONER LINDWALL: What do you think about - you - I think you were here for the Melbourne and Northern - Darwin testimony?

MR WILLEY: I heard the Darwin. I didn't hear much of the Melbourne.

COMMISSIONER LINDWALL: Okay. Melbourne's changed its scheme to an open access scheme, which they required when the renegotiated the leases with the joint venture fuel companies. Darwin of course has gone more to the purer open access. What do you think about those type of schemes, and is there any intention that BAC would go in that direction?

MR WILLEY: The commercial agreement with the JUHI partners is non-exclusive. The reality is that to deliver fuel to aircraft you need access to a very complex, a very costly in-ground hydrant system. Now, there is only one hydrant system. That is owned by the joint venture partners through a licence arrangement with that long lease term. It would be very - in reality it would be disruptive for another entity to come in, establish a new depot, and establish a new series of pipelines under our aircraft aprons.

COMMISSIONER LINDWALL: To duplicate, yes, no doubt.

MR WILLEY: Yes, to duplicate it.

COMMISSIONER LINDWALL: But to have a different way of operating so that it was more - other fuel companies could come in and enter the market more openly than what you've currently got.

MR WILLEY: Again, we don't have visibility of what the JUHI partnership would allow with new entrants to join that partnership or otherwise. We're not sure. That's something that we don't fully understand.

COMMISSIONER LINDWALL: Okay, yes.

MR WILLEY: Whether there's an opportunity for an - rather than four partners, to have six or eight partners, or - yeah, and deliver some different arrangements, or a - different competition outcomes through that process.

COMMISSIONER LINDWALL: Okay.

MR WILLEY: But it would be extremely difficult for a whole new entity to come in.

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COMMISSIONER LINDWALL: Yes.

MR WILLEY: The JUHI depot at the moment is served to two off airport, and I know Ian Kew was talking about the Darwin situation, where they're just considering a pipeline. Well, Brisbane has two pipelines to two different bulk storage facilities - regional bulk storage facilities. So again, there's a - there's redundancy in that, and that reduces our risk.

COMMISSIONER LINDWALL: Yes.

MR WILLEY: Because they're very large volumes we're talking about.

COMMISSIONER LINDWALL: Yeah, I can see.

COMMISSIONER BAXTER: But I just - while you're on that, with the new runway going in at Brisbane Airport, will there be a pipeline extending on the existing pipelines for feed into aircraft that will be using that runway, or will it be from where the existing facilities are?

MR WILLEY: The runway is not delivering new terminal facilities. It will be delivering growth to Brisbane Airport and growth opportunities.

COMMISSIONER BAXTER: Right.

MR WILLEY: It basically doubles the capacity of Brisbane Airport. Now, it would be nice for BAC if the capacity doubled the day we open that runway, but it won't. It'll climb steadily at the typical industry 5 to 7 per cent. So, working with JUHI on this master planning process, they're confident that their site is well positioned. At the moment it's a one way flow to each of the aprons. JUHI is basically in between the international facilities and the domestic facilities, and there's a pipeline going out from the depot both ways, very complex pipeline with low points and drain points and air valves and isolation valves and things like that. Part of the master planning process we're working up with JUHI is their ability to service terminal expansions at Brisbane Airport into the very long-term, and that may require that one directional flow that's heading towards the domestic terminal to be turned into a ring main, which travels around those new terminal footprints.

COMMISSIONER BAXTER: Yes.

MR WILLEY: And they're quite receptive to that.

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COMMISSIONER KING: Can I - just stepping back, really, a bit just on some of the mechanics that I may have missed. So, the lease contract that the airport has with the current JUHI, what's the length of that contract, when does it come up for renewal? Just those background contract mechanics.

MR WILLEY: Basically the end of the current contract - and there is renewal opportunities in the contract - is year 2032.

COMMISSIONER KING: Okay, so - and when you saw renewal opportunities, is it a renewal - automatic renewal that both sides agree, or?

MR WILLEY: No, it would be a negotiated renewal. There's actually - five years before 2032 there is a renewal option at JUHI's discretion.

COMMISSIONER KING: Okay. So, I mean, that's a fair way in the distance. Was the JUHI contract renegotiated in 2012 or something? I mean, presumably it wasn't a two year - - -

MR WILLEY: It was around about that time, yes.

COMMISSIONER KING: Okay, so around 2012. Do you know anything about the negotiations that took place at that time, around the 2012 period?

MR WILLEY: On some of the principles that were included in the contract I do, from a planning perspective, not from a commercial perspective. You know, things like Brisbane Airport was running with a fuel throughput levy previously. I think it was the first airport to introduce that, but that was abandoned and incorporated into the leasing commercial arrangements with JUHI. So we no longer have a fuel throughput levy.

COMMISSIONER KING: Okay. So - sorry, just I'd like to touch on - I'm sure we all want to touch on a couple of points there, but just again, just a clarification. So, you mentioned about potential new equity stakeholders in the JUHI at Brisbane Airport. Do you know if there is anything in the JUHI joint venture that allows for somebody else to buy in?

MR WILLEY: No I don't. No I don't.

COMMISSIONER KING: No, so - - -

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MR WILLEY: I don't believe we have any - even our commercial departments don't have any visibility on that.

COMMISSIONER KING: Okay, so unlike Sydney Airport, where obviously Qantas was able to buy in, you've just got no - - -

MR WILLEY: No.

COMMISSIONER KING: No, okay.

MR WILLEY: So, the other change that occurred when this - the current lease term was negotiated, was be adjusted the site boundary on the lease side to allow future expansion.

COMMISSIONER KING: Okay.

COMMISSIONER BAXTER: So this is for additional tanks, if needed?

MR WILLEY: Yes.

COMMISSIONER KING: Yeah.

COMMISSIONER BAXTER: Sorry, keep going.

COMMISSIONER KING: Other things I'm happy to follow up.

COMMISSIONER BAXTER: No, you (indistinct). You've got a good brain.

COMMISSIONER KING: Yeah, do you - and again, this may be on the commercial side rather than the planning side. There's obviously been a number of JUHI renegotiations that we've already heard about this morning, with Darwin, with Melbourne Airport. Brisbane's renegotiation obviously preceded them. Do you have any knowledge of the options that the airport itself were thinking about at that stage? I mean, you're obviously aware of what they did in Darwin, where they took back ownership. Melbourne Airport negotiation led to a - quite a different 20 year agreement, but with quite explicit open access written into the contract, as I understand. Are you aware of whether Brisbane Airport considered any of those sort of options, or other options?

MR WILLEY: Yes, it was considered at that time, and certainly the provision of fuel services into aircraft was not seen as part of BAC's core business at that time. The - having a reliable high level of service that our main airline customers were satisfied with is part of our core business, and

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we were aware that we did have that. so at that time, when that lease was renegotiated, no, there was no intention to change the arrangements, and it's particularly relevant given the extent of the hydrant systems, and also the off airport bulk storage facility connections. You know, you're talking many, many kilometres of pipeline to those off airport facilities. One of those feeds has only recently been renewed. Again, that is a - was a major project, to thrust bore under runway systems and taxiway and apron systems all that distance across airport. So no, we've seen that we're satisfied with what we've been provided with, but we don't have visibility on pricing.

COMMISSIONER LINDWALL: Does the - do your airline customers talk to you about concerns about the price?

MR WILLEY: No. No. No, and generally our relationship with airline customers is at that regional or local level. My understanding is many of these - the fuel supply contracts are negotiated in a fairly exclusive head office arrangement for the major airlines.

COMMISSIONER LINDWALL: So not even - I think Melbourne Airport noted that, whilst they obviously are unaware of exact prices, they had anecdotes - they were told by the airlines that the airlines were concerned about prices. Brisbane Airport hasn't similarly - - -

MR WILLEY: I have had no exposure to that in my role at Brisbane Airport. As I said, we specifically - we meet - again, we meet with JUHI monthly, and quarterly for more senior level meetings with JUHI. We also meet with the airlines on infrastructure development issues monthly. We specifically ask them their experience with provision of fuel services at Brisbane, and both the major carriers expressed a high level of satisfaction, and it's interesting because the trend with, particularly domestic airlines at the moment, is to continue to shrink turnaround times to get great aircraft utilisation.

COMMISSIONER LINDWALL: Yes, yes.

MR WILLEY: Now, that requires an even more efficient response from fuel handlers. So - and they express satisfaction.

COMMISSIONER KING: You mentioned the two domestics. Any feedback from the internationals? Are they part of these meetings or not?

MR WILLEY: Ah, well, Qantas and Virgin Australia have an international arm.

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COMMISSIONER KING: Qantas obviously being - yeah. No, the other international airlines I was thinking.

MR WILLEY: No. No, I haven't had any discussions with BARA representing the other international carriers.

COMMISSIONER KING: Yep, okay.

COMMISSIONER LINDWALL: Now, there was a trial - Bioenergy Australia told us the other day that there was a trial of biofuel proposed in Brisbane.

MR WILLEY: Yes.

COMMISSIONER LINDWALL: Promoted by the Queensland Government, I understand. We were told that there were many more tests required by that fuel than there was for other types of fuel. We were also told that it's a more dense form of fuel with less impurities in it, and that the negotiation time had spun out to months and months and months - like, more than three months. Do you have much that you can say about that particular trial?

MR WILLEY: I have a very basic understanding of what transpired with that trial. So the trial was a small amount of biofuel generated aviation fuel. It was inserted in the Caltex regional storage system, so then it's mixed.

COMMISSIONER LINDWALL: Yes.

MR WILLEY: I think it was somewhere between 20,000 and 25,000 litres. So, when you're talking the volumes we go through every day it's pretty small.

COMMISSIONER LINDWALL: Yes, yes.

MR WILLEY: so then it was - it's piped across to the JUHI facilities and distributed out to aircraft. So, basically that fuel - a bit of that fuel went into all aircraft that was fuelled over that day, or the two days, depending on, you know, how it was mixed in the on airport tanks. The issues, apparently, were relating to the current accepted standards for testing that fuel, which were not fully promulgated at the time the trial rolled out. So that meant we had to be quite cautious for a 24 hour period that no military aircraft were fuelling at Brisbane Airport, because they have quite strict adherence standards for the testing regimes before that fuel goes into

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their - any of their fleet. But I also understand that since that time, since that trial, which I think was in September, the standards have now been defined. It think it's a US-based standard.

COMMISSIONER LINDWALL: Yes, we were told, I think, that the military planes in America, they were up to 100 per cent biofuel. All right. Is there anything about - more about - I don't think there's any more questions about biofuel.

COMMISSIONER KING: Whilst you're thinking.

COMMISSIONER LINDWALL: Yes, please.

COMMISSIONER KING: Can I come back to the fuel throughput levy, which from memory goes back to the first day of privatisation of Brisbane Airport.

COMMISSIONER LINDWALL: Yes.

MR WILLEY: It may have been. It may have - I'm not sure. It was introduced quite soon after we took over the operational of Brisbane Airport.

COMMISSIONER KING: I think it was day one, because I was doing research on privatisation at the time and made some predictions, but I didn't pick the fuel throughput levy, I picked the taxi charge on the land side. So, it's now been eliminated, or just reduced?

MR WILLEY: No, no, there's no more fuel throughput levy.

COMMISSIONER KING: So it has been eliminated, yep.

MR WILLEY: Yeah.

COMMISSIONER KING: What was the logic behind that decision? Why did the airport decide not to have a fuel throughput levy?

MR WILLEY: I'm not sure. I can't answer that, but I - yeah. I suppose its introduction was a little bit contentious. It did operate for a number of years. I cannot give any definite answer on that. I don't understand, but all I know, it has been removed and there - the commercial agreement with the joint venture sort of incorporates, to some degree, the concept. I'm not sure.

COMMISSIONER KING: Okay.

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MR WILLEY: Yeah.

COMMISSIONER KING: Okay.

MR WILLEY: So whether it was a different rent rate, it's based on pipeline length, I'm not sure, but it's - was built into the new commercial agreements.

COMMISSIONER LINDWALL: Okay. Do you think it would be better to have more transparency about the arrangements for the JV for potential new entrants and pricing, for example? Would there be a benefit there, because I would have thought that both the airport and the airlines have some mutual interest in that type of - there's a lot of things where airports and airlines have diverging interests, and we've seen that in some of the submissions we've received to this inquiry, and no doubt we'll hear about that in our later hearings, but in the case of fuel you would think that it's - you have a fairly common interest and that greater transparency might lead to better outcomes for your customers, and therefore improve your outcomes as well.

MR WILLEY: It - from an airport development perspective it would be good to understand if fuel pricing at Brisbane was constraining growth.

COMMISSIONER LINDWALL: Yes.

MR WILLEY: So that would be - yeah, that would be useful information to us.

COMMISSIONER LINDWALL: Okay.

MR WILLEY: And it - certainly what would be useful was - if there were significant differentials to what was achievable at other ports, not just in Australia but overseas.

COMMISSIONER LINDWALL: So as you say, you're not aware of any of that at this stage.

MR WILLEY: Knowing the airlines I imagine that that's not the case, because I don't think they'd let that happen.

COMMISSIONER LINDWALL: You've got the JUHI with the four joint venture members and then the into plane service, I think, you had three; is that right?

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MR WILLEY: Three of the partners have into plane operations as well, and into plane equipment.

COMMISSIONER LINDWALL: So do you know why one of them - which one was it? Anyway, one of them is not a member of that into plane - - -

MR WILLEY: No, I don't know why, but apparently they also have arrangements with the other three partners to supply their services on their behalf.

COMMISSIONER LINDWALL: Okay, yes. Ken, did you have anything?

COMMISSIONER BAXTER: Not on that, but in your submission you talked about the land planning arrangements, and also that you're working with the Queensland Government on putting a third air train into Brisbane Airport.

MR WILLEY: Yeah, putting a train station.

COMMISSIONER BAXTER: Station is it?

MR WILLEY: Yes, just a station.

COMMISSIONER BAXTER: But no duplication of the line?

MR WILLEY: No, no. The air train line itself, it's a private entity, the air train operation. The line has secured volumetric lease allocations to allow duplication of the track in the long-term. Whether that's ever needed is probably questionable, but they do preserve the ability to grow into the future. The current discussions and the current focus is on securing the ability to deliver a third train station. So we've got one at each of the domestic/international terminals.

COMMISSIONER BAXTER: Yeah.

MR WILLEY: This is down more of the business part of the precinct.

COMMISSIONER BAXTER: Right.

COMMISSIONER LINDWALL: Anything else, Ken?

COMMISSIONER BAXTER: No, no, that was the only other one I had.

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COMMISSIONER LINDWALL: Stephen?

COMMISSIONER KING: Yeah, just - the only other thing, so there's two separate pipelines actually coming into the - so, from the offsite storage into the on airport storage - fuel storage?

MR WILLEY: Yeah, the bulk supply. There's two bulk supply pipelines. As I said, one of them has only been recently renewed.

COMMISSIONER KING: Yep.

MR WILLEY: Because previously it was in a fairly poor legacy position that connected up with a former JUHI site for the old Brisbane Airport. So it's now come on a more direct route across to the new JUHI depot in between our two operating terminals, and there's another one across the Bulwer Island. So there's one from the Pinkenba area, there's one from the Bulwer Island area. So again, there's a bit of redundancy in that.

COMMISSIONER KING: Yeah. Now, those off - given the location of Brisbane Airport, those off airport storage facilities, they're actually in port terminals?

MR WILLEY: Yes, yep. Yep.

COMMISSIONER KING: Okay.

COMMISSIONER LINDWALL: So, getting back to that into plane services, if I'm - I've got a truck and I want to provide it to, you know, your plane, would I have to get approval from those three into plane service providers before I could do so?

MR WILLEY: A very good question. I'm not sure. I imagine if you want to get fuel from them you'll have to have some sort of agreement with them.

COMMISSIONER LINDWALL: Yes, yes, obviously, but if I had my own - - -

MR WILLEY: So whether you've got a tanker or a hydrant car, it's your - you're supplying their fuel into an aircraft.

COMMISSIONER LINDWALL: Yes, exactly.

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MR WILLEY: Yeah, so - yeah, no. I'm not sure of the restrictions on that.

COMMISSIONER LINDWALL: Yeah, okay.

MR WILLEY: Whether, you know, you can go out and purchase a truck and start operating it, presumably.

COMMISSIONER LINDWALL: No, I don't know either, but - so, you've got no more questions?

COMMISSIONER KING: Only one other. Again, you mentioned that the agreement with the JUHI - I think you said a nonexclusive agreement.

MR WILLEY: Yes. If - it doesn't prevent another operator from coming in and establishing fuel services at Brisbane Airport.

COMMISSIONER KING: But it would have to be - it would have to duplicate at least part of the actual (indistinct).

MR WILLEY: Unless it was a tanker operation.

COMMISSIONER LINDWALL: Yes.

COMMISSIONER KING: Okay.

MR WILLEY: Yeah, and that's quite likely, because we do still have general aviation activities and charter facilities, and fixed base operations that aren't hydrant serviced.

COMMISSIONER LINDWALL: Okay, yep.

MR WILLEY: So, you know, you could come in and start a tanker service to some of those.

COMMISSIONER BAXTER: So that'd be fairly small scale by comparison, yes.

COMMISSIONER KING: Yeah, okay. I see.

COMMISSIONER LINDWALL: Yep, that's - - -

COMMISSIONER BAXTER: No, I'm fine.

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COMMISSIONER LINDWALL: Well, I just wanted to ask you something. There's an article in today's Australian and it talks about BARA Managing Director, Barry Abrams, saying that Sydney, Melbourne, Brisbane, and Perth airports were

> *Luxury shopping strips within international airports are being blamed by BARA for distracting and confusing passengers to the point of causing flight delays.*

Do you have anything that BAC could - - -?

MR WILLEY: I am not aware of that occurring at Brisbane. Yes, we do have good retail offerings in our terminals. I think it is an expectation now for passengers flying that they - part of the experience is using food and beverage outlets, and retail outlets.

COMMISSIONER LINDWALL: Yes, yes.

MR WILLEY: So it's a positive experience for them. I'm not aware that it's - - -

COMMISSIONER LINDWALL: Causing flight delays.

MR WILLEY: - - - causing flight delays. No, there's other issues causing flight delays, not passenger shopping.

COMMISSIONER LINDWALL: Yes, okay. Okay. Well, thank you very much, Mark, for appearing today.

MR WILLEY: My pleasure.

COMMISSIONER BAXTER: Thanks Mark.

COMMISSIONER LINDWALL: So, did you want to go straight on now? Are you happy to do so? Yep, good. All right. Are you happy to continue straight on?

COMMISSIONER KING: Yeah, I'm more than happy, yep.

COMMISSIONER LINDWALL: Yep. Well, Leonie, if you could just introduce yourself, and then if you want to give an opening statement that would be fantastic.

MS HORROCKS: Thank you. Thank you. So, good morning to the Commissioners and thank you for the opportunity to be here today. My

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name is Leonie Horrocks. I'm General Manager Airports in the Department of Infrastructure, so the Commonwealth department. My role in that - in the Department is to regulate the 21 operational federally leased airports. Obviously there's another airport coming, but it is not under my jurisdiction at this point in time. So, Western Sydney Airport is still under construction. So, in our role as regulator of the federally leased airports, and the primary basis of our submission, was to convey what we feel is the importance of adequate jet fuel infrastructure at and into airports, and that is to support the growth - the predicted growth and the long-term growth of the aviation industry.

As part of that we see that appropriate long-term planning by airport lessee companies and jet fuel providers should really take into account the broader national interests in that planning scenario, and the other issue that we're focused on is in the rare situations of fuel shortages, particularly when bulk allocations are made, that the impact on the industry is taken as a measure in how that is allocated, and particularly focused on the differences of the impact between domestic and international operators. So, we're interested to see that the investment in on-airport and off-airport infrastructure proceeds appropriately, and obviously the Department has a very strong interest in that, but also understands that in that we have very little scope to actually do much about that.

COMMISSIONER LINDWALL: Yes.

MS HORROCKS: So, we can influence, certainly, the airport operators. We have no particular direct influence with fuel contractors and providers, so that leaves us with an idea that we can't really understand the intricacies of the details between those commercial negotiations, between the fuel suppliers and the airlines, and indeed between the airports and the fuel JUHIs as well. So we would see opportunities for increased transparency would be beneficial, noting of course the commercial confidentiality of the situation. We would need to take that into account. The other issue that we have been focused on over the last couple of years is the traffic light notification system.

We're particularly concerned that the way that the current system works - it's a monitoring system run by the industry, and there is planned and then there's unplanned interruptions, but - however, the - once that traffic light is issued it's primarily the airports which are impacted in their reputational outcomes from those notifications. So, we feel that perhaps there is a better way of looking at that and dealing with that as well. So, the other issue that we found is the understanding of the arrangements at each federally leased airport for onsite storage and planning going forward

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could perhaps be enhanced, with a bit more detail and a bit more transparency.

We would see an opportunity perhaps for that to occur in the airport Master Plan process. Some airports are already doing that, but the detail that is provided through the Master Plan process is not necessarily consistent across all of the airports. So we could look at some way of promoting that type of information provision and transparency as well. So, that's basically it.

COMMISSIONER LINDWALL: Thank you, Leonie. Could I go back to the master planning process?

MS HORROCKS: Sure.

COMMISSIONER LINDWALL: How much as the Department, or - and the minister can change that through the rules of the master planning, and perhaps insert new requirements for greater detail, or the consistency of that.

MS HORROCKS: I think there are two opportunities, and not wishing to pre-empt the minister's decision or anything.

COMMISSIONER LINDWALL: Yes.

MS HORROCKS: But firstly there may be the opportunity that the minister would express his expectation that in the master planning process there could be details provided in the plan. The other opportunity of course for government would be through legislative change into the Airports Act.

COMMISSIONER LINDWALL: Okay, yes.

MS HORROCKS: We have a light-handed regime.

COMMISSIONER LINDWALL: Yes.

MS HORROCKS: So legislation changes are, you know, last resort.

COMMISSIONER LINDWALL: Of course, but ministers' expectations in the past, have they been generally adopted?

MS HORROCKS: Certainly.

COMMISSIONER LINDWALL: Okay.

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MS HORROCKS: Yep, yep.

COMMISSIONER LINDWALL: So it's quite a powerful tool in a way.

MS HORROCKS: Yes. Yes, it is.

COMMISSIONER LINDWALL: Okay, and does this link up with the Department's view about having a - consultative forums at the various airports?

MS HORROCKS: We were very appreciative of participating in the Victorian process, and I think it was a very useful process for the Department to have that on the ground exposure to the JUHI operators and how their process works, and what their industry - how their industry operates. I personally was not aware of that in detail and it was definitely a learning opportunity for myself, which I appreciated. So I think it is useful. I do take on board the points that were made earlier, that there needs to be an issue to be focussed on.

COMMISSIONER LINDWALL: Yes, yes, yes.

MS HORROCKS: You have to have an objective, you have to have an outcome that you're seeking.

COMMISSIONER LINDWALL: Yes.

MS HORROCKS: And I do note that the time and the place for each of the federally leased airports, where they are in the negotiations, is different. So I'm not sure that a national forum would work under those circumstances.

COMMISSIONER LINDWALL: Yes.

MS HORROCKS: Perhaps a jurisdictional forum might be of some value.

COMMISSIONER LINDWALL: So you found, in the way - the case - which I understand the Victorian Government catalysed that.

MS HORROCKS: Yes.

COMMISSIONER LINDWALL: That having the Victorian Government involved was quite helpful then.

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MS HORROCKS: Absolutely. Absolutely. We've created, in my personal view, some very productive relationships and interactions which are still ongoing.

COMMISSIONER LINDWALL: So perhaps it might be something useful for, in initial terms, the four major airports.

MS HORROCKS: Agreed. Agreed.

COMMISSIONER LINDWALL: Say, with Western Australian Government and so forth.

MS HORROCKS: Yep. Yep, yep.

COMMISSIONER LINDWALL: Okay, and would that be part of the master planning process itself, or not? Or are they separate?

MS HORROCKS: I think it would be separate, but - however, the master planning process does require consultation with state and other authorities.

COMMISSIONER LINDWALL: Okay.

MS HORROCKS: So that's already mandated.

COMMISSIONER LINDWALL: Yes.

MS HORROCKS: So it could form part of that. There's an opportunity there, yeah.

COMMISSIONER LINDWALL: And - - -

MS HORROCKS: I think the forum was also useful, if I could venture an opinion - - -

COMMISSIONER LINDWALL: Please.

MS HORROCKS: Is that the - having the state and the Commonwealth very vocal at the meetings conveyed to the industry - the fuel industry - the importance with which both governments were focused on this particular measure.

COMMISSIONER LINDWALL: Okay.

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MS HORROCKS: And I think it also conveyed the understanding of the impact of interruptions to fuel on the economy, which of course is a bigger national interest that perhaps the fuel industry may not have been as focused on.

COMMISSIONER LINDWALL: Yes, exactly. Now, sorry, if you don't mind me, a couple more.

COMMISSIONER KING: No. Well, just a slight (indistinct) from that one.

COMMISSIONER LINDWALL: Yeah, please.

COMMISSIONER KING: We've heard this morning about the fact that the Melbourne Airport - the new lease arrangements are adding significant capacity. Do you feel that the consultative arrangements were at least - can take part of the credit for that? Is that one of the benefits of those consultative arrangements?

MS HORROCKS: I think so. I think so, because - well, I think there are a number factors that - the factor, obviously, that the existing lease was, you know, ending. I think that the competency of the airport to look strategically as to going forward, so the new runways coming on, the third and the fourth - eventually the fourth. So that was a factor which of course is driven by the master plan process, and the major development plan process. So I'm thinking all these things, you know, sort of built on each other, and then I think the forum coming in on the top of that and them seeing just the importance that the government - both governments were placing on having this matter settled, and then I think another factor to that was the actual interruptions to supply that happened in Melbourne as well.

COMMISSIONER KING: Yes.

MS HORROCKS: All of that kind of, you know, perfect storm at that particular time. So I think yeah, it all came together. Yeah.

COMMISSIONER LINDWALL: So, the NOC process, I think you said it could be improved in some fashion.

MS HORROCKS: Certainly.

COMMISSIONER KING: How would you do that? Through the master planning, or some other process?

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MS HORROCKS: The NOC is run by the Department of the Environment and Energy. So not wishing to speak out of turn, but I – the actual process for deciding what colour traffic light is applied is not terribly well known. The timeframes through which the traffic lights are applied seem to be, even if it's a planned outage, the notifications seem to come through maybe 24 hours ahead.

So I wonder at the – if that lead in span could be lengthened so that airports and airlines could be more well informed, and perhaps better plan for any impact of that.

And supply interruptions obviously, domestically, for domestic operators, is not as catastrophic as it is for internationals.

COMMISSIONER KING: Exactly.

MS HORROCKS: Yes. My department has had representations from the Melbourne supply outage from an international aircraft saying that that cost them significantly more, because they didn't have a fuel contract with an alternative airport, but with the outage they had to fill up because they're international. So that was a significant impost on them.

So I wonder if the NOC had earlier notification, whether that could have, in some ways, mitigated the impact, the financial impact on that particular international operator.

COMMISSIONER LINDWALL: Well, I heard, and in since it was confidential, let's call it airport A.

MS HORROCKS: Yes.

COMMISSIONER LINDWALL: Airport A had an issue where the airport operator, the owner, knew something was a problem with some of the software at particular storage facilities, and it took hours to get notification through to the NOCs system, because it had to come from a fuel company apparently. So do you think that that's something that could be improved about - - -

MS HORROCKS: Well, I do wonder at the efficacy of having fuel companies making these notifications. I understand the NOC was originally chaired by an independent member.

COMMISSIONER LINDWALL: Yes.

MS HORROCKS: That, as I understand it, is no longer the case.

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COMMISSIONER LINDWALL: It's no longer the case?

MS HORROCKS: So it's a monitoring process which is a notification to the NOC, and then the NOC just disseminates that notification. So I'm wondering at the governance, I guess, not wishing to put any aspersions on that. But I'm just wondering whether that governance could be enhanced in some way.

COMMISSIONER LINDWALL: Okay. Yes.

MS HORROCKS: Yes, and the timeliness, I think.

COMMISSIONER LINDWALL: Now, I think as IATA has minimum requirement – recommended of three days - - -

MS HORROCKS: Correct.

COMMISSIONER LINDWALL: - - - of supply at that storage facility. Do you concur with that, or do you have some other view as a Department?

MS HORROCKS: We don't actually have a view, but we are aware of that as a benchmark, and I'm aware that, apart from currently Brisbane and Melbourne, the federally leased airports meet that benchmark.

I guess one concern for us sort of going forward in a general matter is the impact on communities and the environment of increased trucking on the roads to keep the supplies topped up. So I think there are sort of some ancillary issues about that process.

And, of course, they're – you know, with roadworks and things like this, whether the reliability of that particular methodology is, you know, going to carry the day.

COMMISSIONER LINDWALL: So you heard the testimony from Darwin about the minimum type of scale to have to justify a pipeline. Does that sound about right to you?

MS HORROCKS: It sounds about right to me, yes. And obviously, they're in that specific position with regard to the defence base on the other side.

COMMISSIONER LINDWALL: Exactly.

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MS HORROCKS: Yes.

COMMISSIONER LINDWALL: And as for Australia, compared to overseas countries in terms of security of supply for jet fuel, and redundancies, and built-in, would you say that we're okay in Australia? Or not so good, or ahead of the pack, or whatever?

MS HORROCKS: I think, generally speaking, we're okay. When you take into account the size of the market, and the throughput generally, I think we're okay.

I'm personally a little concerned about the projected forecasts, and how we're going to meet that going forward. Because as, obviously, we see the masterplans coming through, and the numbers are, you know, very impressive.

COMMISSIONER LINDWALL: Quite large, yes.

MS HORROCKS: And we hope they all come out, but yes, I think – I'm worried about the future, to be honest. I think the current structure was put in place so long ago, and there have been seemingly very few opportunities for that situation to evolve. So I'm interested to see how it goes.

COMMISSIONER LINDWALL: So, and when you compare the different arrangements, now I think you were here for Melbourne airport with their new open access arrangement for 20 years, and Darwin a more pure one.

MS HORROCKS: Yes.

COMMISSIONER LINDWALL: And, of course, Brisbane, do you, as a Department, or your own view, have a superiority of one system over another? Or one arrangement over another?

MS HORROCKS: I think it's important that the arrangements reflect the local conditions, and obviously they're commercial arrangements, so we don't have – the Department doesn't have input into those.

But I do see there would be an advantage if we could share best practice, noting again the differences in the timeframes for each of the lease arrangements. I would see that there would be an advantage in some degree of transparency over best practice outcomes and options, I think.

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COMMISSIONER LINDWALL: Would you prefer open access more than a restricted of entry?

MS HORROCKS: I guess, on a personal view, I can't see – I would see that open access actually provides the opportunity for more competition, just as principle. So, yes.

COMMISSIONER LINDWALL: And I must ask about Western Sydney, but I know that it will ultimately come into your domain.

MS HORROCKS: It will, yes.

COMMISSIONER LINDWALL: Now, it's going to have to have - - -

MS HORROCKS: Agreed.

COMMISSIONER LINDWALL: It will start a – maybe a pipeline, but initially, it will be trucking, I presume.

MS HORROCKS: Yes.

COMMISSIONER LINDWALL: That gives an opportunity for the government who's building it to set up a proper open access arrangement for it (indistinct) do you see that as – has that been thought of? Or you're not aware of that?

MS HORROCKS: So, there is a specific unit in the Department that deals just with Western Sydney unit, Western Sydney airport, and I'm – we have relationships in regard to how things work in the Airports Act, and they can be applied. So I have sort of peripheral knowledge of them.

As to the arrangements for the jet fuel for that airport, I really don't have the detail, so I'll probably – I can take it on notice.

COMMISSIONER LINDWALL: Yes, all right. Yes.

COMMISSIONER BAXTER: While you're on that, I notice there's a mention in the document about the Western Sydney airport, and also there's a mention about the regional access schemes.

MS HORROCKS: Yes.

COMMISSIONER BAXTER: Is your view there would be any likely reason for changes, existing regional flights with the implementation and the operation of Western Sydney?

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MS HORROCKS: No. I don't believe there'll be any changes to them, and that's because the government has basically said that. But also, there are arrangements, agreements between Sydney Airport and the government, and – as to which guarantees regional access to Kingsford Smith. Kingsford Smith Airport.

COMMISSIONER BAXTER: (Indistinct)

COMMISSIONER KING: So, just we had a brief discussion on open access and competition, and I note in the submission from the Department, you state, "Local differentials for Australian airports are typically higher than other major international airports around the world."

Now, the submission goes on to partly explain that by, you know, points out that further away from trading hubs like Singapore, or economies of scale.

MS HORROCKS: Yes.

COMMISSIONER KING: I guess, what was the information that you were using to judge that? So did you actually have - - -

MS HORROCKS: Certainly.

COMMISSIONER KING: Or did the Department actually have comparative pricing information, or a comparative information rates of return, or any – what does it – yes. What's the reason for that?

MS HORROCKS: Certainly. So, originally, Western Sydney unit commissioned a report from a company to look at the overall status, and off the back of that, I commissioned a specific report and we looked at the ranges for federally leased airports, and what were the impacts and the outcomes from that.

And then, obviously, as part of the Victorian round table, there was a further report commissioned which was quite in depth as well. So a combination of information from all of those three reports is what we used as a reference point for the points made in our submission.

COMMISSIONER KING: Okay. Were these reports public, or?

MS HORROCKS: No. No.

COMMISSIONER KING: Your shaking your heads at the back.

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MS HORROCKS: I'm just liaising with my colleagues.

COMMISSIONER KING: I suspect somebody from team will be chatting with you later.

COMMISSIONER LINDWALL: Well, could I say that obviously we'd prefer public, that the information – so could you take that on notice?

MS HORROCKS: I will take that on notice to see what I can provide. Yes.

COMMISSIONER KING: Realising, obviously, that given they're confidential, you're limited in what you can say, are there any particular airports around Australia that, in a competition and pricing sense, give the Department more reason for concern than others?

MS HORROCKS: I don't think so. I think, just generally speaking, we're focused on the national interests, and making sure that the travelling public and, you know, business public have access to the services that they require, and we really see that one of those key support issues is steady supply of jet fuel.

Obviously, in respect to the Melbourne situation, we were aware through the forum of a number of international airlines indicating that they were having trouble getting fuel contracts. If that is magnified across other international airports, then I see that as an issue.

COMMISSIONER KING: That's on the reliability side. What about on the pricing, or the price differential side?

MS HORROCKS: Both of those issues were mentioned during the – as part of the Melbourne forum.

COMMISSIONER KING: Okay.

MS HORROCKS: Yes.

COMMISSIONER KING: Do any airlines come to the Department with complaints relating the pricing of fuel at particular airports?

MS HORROCKS: None that come to mind. I'm obviously aware that a major airline is a partner of the JUHI in Sydney. So, you know, we're aware that that airline obviously has more readily available access than other airlines.

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So I think if there was going to be a specific representation, it might come from that particular airline. But given their situation, perhaps that's the reason that they haven't come forward. Don't know. Yes.

COMMISSIONER LINDWALL: Do you think there's a prima facie case for JUHIs, or to be independent of fuel companies, and perhaps also, independent of airlines?

MS HORROCKS: I would hazard my personal view, not the Department's.

COMMISSIONER LINDWALL: That's fine. Yes.

MS HORROCKS: So I would see that that would be of value, and I understand that that is a situation which occurs in a lot of other countries.

COMMISSIONER LINDWALL: Yes, yes.

MS HORROCKS: And has proven very successful because they are independent and they are, you know, separate from both of those parties. Yes, I personally think that that would be a good outcome.

COMMISSIONER LINDWALL: Is there anything you think that the government could do about that, or is that purely something for individual airports to – when they are renegotiating their leases?

MS HORROCKS: I think it's the commercial negotiation, because obviously the JUHI operators would want some degree of commercial compensation for moving out of the scene.

COMMISSIONER LINDWALL: Yes, yes.

MS HORROCKS: And whether or not that could be facilitated by particular airports would be a commercial matter.

COMMISSIONER BAXTER: Can I just take a slightly different tack on that? In the planning for Western Sydney, and whatever arrangements might be made over JUHI, presumably at some stage there'll have to be conjoint Commonwealth, State negotiations about (indistinct) access of the pipeline, and who controls that and how it's controlled. Do you see it as a role for Commonwealth involvement in that discussion?

MS HORROCKS: I can't really hazard an opinion of that, given my distance from the particular area. But, obviously, the Commonwealth and

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the State are – have been negotiating on the whole project itself. Of course, there is a company, Western Sydney airport company, which is running the job. So that's been established to do that project.

So I imagine that that – you know, there would be a role in that respect as well, but I wouldn't want to answer on their behalf at all. I could take it on notice, if you - - -

COMMISSIONER BAXTER: I think it would be worth taking on notice.

MS HORROCKS: Yes. Absolutely.

COMMISSIONER BAXTER: I mean, it is inevitable, knowing the state of feeling about a lot of this stuff.

MS HORROCKS: Sure.

COMMISSIONER BAXTER: Because the pipeline's going to travel relatively long distance, presumably, from somewhere on Sydney Harbour to – out to - - -

COMMISSIONER LINDWALL: Botany.

MS HORROCKS: Yes, yes.

COMMISSIONER BAXTER: Or St Mary's, that there will be the normal groups who will fear that they've got an exposure running underneath them, or about to run underneath them.

MS HORROCKS: Yes.

COMMISSIONER BAXTER: And secondly, the comment you make about, I think in document, about the regional access arrangements being improved with the introduction of Western Sydney, would you see in your planning for the future any likely changes in the current regional slot arrangements for Sydney, vis-a-vis Western Sydney. I mean, will there be thought given to that, and how it might be managed?

MS HORROCKS: So the government has said that there will be no curfew and no slot arrangements to Western Sydney airport. The government's made that statement.

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In regard to Kingsford Smith Airport, the slot arrangements there are – there is what's called regional ring fenced slots, which are specifically dedicated to regionals.

The curfew arrangements already exist, and the government has said that clearly – it is willing to consider amendments to improve efficiency for the airport overall, but it needs bipartisan support because it will require legislative change.

And the other thing that needs to be balanced, of course, is amenity to the local community in that circumstance, if there's any changes to the current protection arrangements.

COMMISSIONER LINDWALL: And I've heard of threats, again I won't name any airports, but where if it is moved to an open access system, that the pipeline would be filled with concrete.

MS HORROCKS: I've heard that as well.

COMMISSIONER LINDWALL: Okay. Now, that would be, arguably, something that would be very difficult for an airport wanting to do something to negotiate. Maybe that is something the government should be trying to stop happening, I suppose?

MS HORROCKS: Obviously, that would be something we would want – avoid that at all costs. What mechanisms the government would have to intervene in that situation, I'm not clear on. Because, obviously, the scenario that you presented is in relation to off airport infrastructure.

COMMISSIONER LINDWALL: Yes, exactly.

MS HORROCKS: So I think there would be a lot of complex issues to work around. Legal, commercial, jurisdictional, that would need to be reviewed.

COMMISSIONER LINDWALL: Exactly.

MS HORROCKS: Yes.

COMMISSIONER LINDWALL: I'm sorry, Stephen.

COMMISSIONER KING: Yes. Just coming back to investments, and the Department's potential concerns. Sydney Airport, it's known that, publicly known, that there's concerns from the JUHI members about the

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uncertainty with regards to ongoing lease conditions there. But, in a sense, it's on a short – they're on a short period of time.

It's been suggested that that's affecting investment at Sydney Airport. Does the Department have any view on that, or any concerns about that situation at Sydney?

MS HORROCKS: As I understand it, the lease negotiations for the JUHI are underway at the moment. So, I'm not quite sure what terms are being offered. Obviously, I don't have oversight of that, but certainly with two pipelines into Sydney Airport, there's opportunities for redundancy, opportunities for new entrants, and capacity there.

So I'm not quite sure – I mean, obviously the term of the airport site, the overall site, there's no change to that, so I'm not quite sure what terms they're concerned about, whether it's the sublease of their site on the airport, which would be a matter of what's currently under negotiation.

COMMISSIONER KING: Okay.

MS HORROCKS: Yes.

COMMISSIONER KING: You heard our conversation earlier about biofuels.

MS HORROCKS: Yes.

COMMISSIONER KING: Do you have anything to say about that?

MS HORROCKS: I think it's important that - obviously, safety is a huge issue and that needs to comes first, and I am – not being a technician in the fuel space, I think that the benchmark should be that safety comes first.

COMMISSIONER KING: Of course.

MS HORROCKS: And if that requires, you know, one test or five tests, whatever the efficiency is in that, I think that should be applied.

COMMISSIONER KING: Okay, yes. Yes.

MS HORROCKS: Yes.

COMMISSIONER LINDWALL: Do you have any other questions?

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COMMISSIONER KING: No.

COMMISSIONER BAXTER: The only other one is I notice your observation in the documents about negotiate and arbitrate proposal, and knowing that that's likely to be, if it does occur, and extended process. Has the Department got a view about (a), whether that's the most appropriate way to deal with what could well be a problem, and do they want to see another process introduced which extends into another set of negotiations.

COMMISSIONER LINDWALL: Slightly beyond our fuel terms.

COMMISSIONER BAXTER: Yes, I know.

MS HORROCKS: He's just having the opportunity.

COMMISSIONER BAXTER: I was in there.

COMMISSIONER LINDWALL: You don't have to answer that, but you can if you wish.

MS HORROCKS: Personally, over the – I've been in this role for seven years now, and the negotiations, the air service negotiations between airports and the airlines have been challenging through that whole time. They have been – they're very complex. There's a lot of moving parts, but in the end, they've always seemed to be worked out, and I think the evidence is the level of investment that has occurred between the airports, and over the period since privatisation, and since the removal of price capping.

Really, you know, you've got runways Brisbane, Melbourne, Perth, you've got significant terminals. You know, there's been a really significant investment which has occurred, all of which was predicated on successful conclusion of air service agreements.

Personally, I'm not convinced that it's completely broken. I think there may be opportunity for, perhaps, some degree of rules of engagement, for want of a better term, in those negotiations to perhaps increase the efficiency and the timeliness of it, but I've yet to be convinced that it's completely broken.

COMMISSIONER LINDWALL: Well, I think you've exhausted our questions, definitely on jet fuel. Thank you. I'm sure we'll have an opportunity in our hearings next year, if you care to come to talk about more general issues. So thank you very much.

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MS HORROCKS: Thank you very much.

COMMISSIONER LINDWALL: Now, officially, that's it until lunch, isn't it? It's a bit early.

COMMISSIONER LINDWALL: We're a half hour ahead of time. Is it possible to get Perth a half an hour early, perhaps, and still have a - - -

COMMISSIONER LINDWALL: If not, we'll start at 1.45. If so, we'll start at 1.15. If we can get 1.15, if we can start again, that would be good. We can all get away a bit earlier then. All right. We may as well go out and have a quick lunch now, if you're all happy. Thank you very much for that.

LUNCHEON ADJOURNMENT

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RESUMED **[1.17 pm]**

COMMISSIONER LINDWALL: So welcome to our Perth Airport colleagues. If you could identify yourself. I'm Paul Lindwall, the presiding Commissioner. I've got Ken Baxter on my left.

COMMISSIONER BAXTER: Hi guys.

COMMISSIONER LINDWALL: It doesn't matter, left or right. And Stephen King is the other Commissioner. So just say hello.

COMMISSIONER KING: Hello folks.

COMMISSIONER LINDWALL: And if you could just say who you are and give us an introductory statement, if you wish to.

MR PEREIRA: Sure. Yes, so there's three of us here from Perth Airport. Brian Pereira CFO Perth Airport.

COMMISSIONER LINDWALL: Hi Brian.

MR MASON: And Allan MASON, Chief Project and Development Officer.

COMMISSIONER LINDWALL: Hello Allan.

MS BLASKETT: And Deb Blaskett, Chief Corporate Services Officer.

COMMISSIONER LINDWALL: Hi Deb.

MS BLASKETT: Hi.

COMMISSIONER LINDWALL: Okay. Did you want to say an opening statement?

MR PEREIRA: Sure. I guess our position we've outlined very much in the confidential submission to PC I guess we're – we've got several objectives that we're trying to achieve as part of a renegotiation of the jet fuel arrangements here at Perth Airport.

We have a current lease with a JUHI that ends in March 2022, and for us, the timing has just started in terms of our notice period under that lease, to commence our negotiation that we outlined in the submission to mission

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our objectives, about trying not to, I guess, provide security supply and make sure that we've got adequate security and redundancy of supply.

And also to, ultimately, try and see if we can actually achieve a open access arrangement currently here at Perth Airport, as we recognise, or we've had feedback from airline customers that there may not be enough choice in terms of competition in being able to procure jet fuel supply at Perth Airport.

But I think that's one thing, the negotiations are just about to commence. We've our first meeting on 7 December to kick off what should be a six month process under the lease provisions negotiations, before we head into a (indistinct) we can't find an outcome with the current operators.

I guess that summarises it. We're happy to take questions on anything in particular in our submission, or any other questions.

COMMISSIONER LINDWALL: Thank you very much for that. We appreciate the – letting us know that the negotiations are about to start. That's a fascinating time where you have the opportunity to observe what other airports have done, for example, Melbourne Airport, and Darwin.

So, perhaps it might be good initial state – question is, how would you compare what Darwin has done, which is a much smaller airport, of course, but it's basically the airport operator is owning the asset, and it's the fuel companies then have open access to it, but they don't actually operate the JUHI.

And then, to Melbourne, where they've got a new 20 year contract where the fuel companies have the equity position, but it is open access.

MR PEREIRA: Yes. So, I think, and Allan might jump in here as well. I guess we have looked at different operating models around the country, and obviously the two you've mentioned are ones we're familiar with.

We've also looked abroad, and we've looked at an operating model at – in Hong Kong, which is held up as being a best in class type operating model, and I guess, in terms of the negotiations that we're approaching with, the JUHI, that's something that's very much in our minds how we might, I guess, open up the process by perhaps the airport owning the infrastructure.

I think for us, one of the barriers of entry for new operators into the JUHI has been the equity type model that the JUHI has operated under, whereby new operators are required to buy in to the asset, and if anyone (indistinct)

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we don't have the (indistinct) what the repercussions are, but I can imagine there were barriers of entry, they would be around the price of entry might preclude competition.

So, for us, one option is, and similar to the Hong Kong option, is for perhaps the airport to own the infrastructure, and to then make it relatively easy for new operators to come into (indistinct) for the infrastructure.

COMMISSIONER LINDWALL: And – sorry, you go.

COMMISSIONER BAXTER: No, no. You go.

COMMISSIONER LINDWALL: I was going to say, who are the current fuel companies that operate at Perth in the JUHI?

MR PEREIRA: BP and Viva.

COMMISSIONER LINDWALL: Yes.

MR PEREIRA: So BP and Viva own the JUHI, which own the hydrants under the apron and the storage facility at the airport. The majority of the infrastructure, including the leasehold arrangement of the land on which the (indistinct) and the pipeline into – out of that – outside airport facility for storage, and the pipeline all the way to the refinery, including the refinery, is BP owned.

COMMISSIONER LINDWALL: Yes, and are all of your airlines customers supportive of you negotiating to get a more open access to your field supply?

MR PEREIRA: In the conversations we've had with, I guess, the two main domestic carriers, and with BARA, they are supportive of the overall objectives that we're trying to achieve.

However, the conversation does keep coming back to, tell us what cost it might have on the airline, especially if it's going to involve Perth Airport owning the infrastructure. Obviously, the returns on that infrastructure would have to be recouped somehow through aeronautical type agreements.

I think the conversation has got to that point. They're supportive of the objectives. One key objective that we are also trying to achieve over this process is to physically move the current (indistinct) airport storage facility, which are, for a couple of reasons, one port (indistinct) opportunity for the airport terminal (indistinct) reason.

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We'd like to relocate that asset, so that potentially might add some legal costs and it's why the airlines are interested in – or what, ultimately, the cost is. So we're working on the (indistinct).

COMMISSIONER LINDWALL: But you're, aside from the cost of moving storage facilities, your prior would be that having a more open arrangement would lead to lower fuel prices for your customers?

MR PEREIRA: I guess, from a simple economics point of view, yes. We've got not visibility on – that the – what prices are charged, if we're not a party to those agreements between the JUHI and the airline.

However, our expectation is if we grow, we can encourage competition into those facilities, and we're – we're only going to – there should be a reduction in price.

COMMISSIONER KING: Can I just follow up on that last point? What evidence have you been able to get, I guess, to back that up? Have the airlines been discussing with the airport that they feel the prices are higher than they would otherwise expect? Has the airport done any of its own analysis? Is it aware of any third party analysis?

We've obviously heard different situations at different airports, some where the airlines don't seem to raise the issue with the airport, others where they do. What's the situation at Perth? Why have you reached this decision, that there is room for prices to move?

MR PEREIRA: So, I think our position is (indistinct) Perth, airlines haven't been open enough with us about the price of fuel at Perth versus other airports, or what price differential they may need from the attraction of competition.

I think they point to commercial-in-confidence agreements they've got, which I think they protect, and they are wary of sharing with other airlines, or somehow other airlines finding out what the arrangements are.

However, we're led to believe in high-level competition with (indistinct) and the airlines that potentially there could be a one a two cent premium per litre of fuel, and to the airport, in terms of prices.

COMMISSIONER KING: Okay. But no direct empirical evidence? Just simply that - - -

MR PEREIRA: (Indistinct) raise the group levies (indistinct).

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COMMISSIONER KING: Okay. Just to come back to the existing arrangements, you mentioned that there is the possibility of access at the moment, but equity access, and you noted a couple of potential problems with that. Are you aware of any parties that have sought equity access to the Perth JUHI?

MR MASON: I'm trying to work out where I've heard it, but I think we are aware of, I think, one or two who have attempted to buy into the JUHI in recent years, but have been frustrated by the timing – the time to actually negotiate now (indistinct) and price. I'm trying to work out where I heard that from now.

We've had a consultant (indistinct) work, and I think that's to do their network's (indistinct) provider as that information, how factually correct it is. I guess we can't determine.

The point with regard to that is the attendance, and we understand that the deals that are done are done on a kind of three year basis, three to five years, and we, our lease, the JUHI lease, expires in 2022, and so with the equity deal and a combination of that with our JUHI, (indistinct) expiry as well as the shortish contract to provide fuel makes it very difficulty for equity to be thrown into the pot, from that perspective.

COMMISSIONER KING: Okay.

MR PEREIRA: So just to add to Allan's point, I think from the product potential entrant point of view, having to buy in a third share, for example, in the current JUHI, might cost them quite a bit of money, and if they've only got a back-to-back three year contract with an airline, it makes it hard to get a return on that capital, all in (indistinct), and overlaying that is obviously the fact that our lease with the JUHI and (indistinct).

But I think there are some elements around that certainty which have added a barrier for their tender.

COMMISSIONER LINDWALL: May I ask that, and you may not be able to tell us, but I'll ask anyway. The leases end in, you said March 2022, what happens to the infrastructure if there's no agreement?

MR MASON: Yes, so the lease, I guess, talks to – makes good arrangement that the current – the current JUHI would have to make good. So, that varies in terms of what that means. Everything from the high (indistinct) under the apron to the actual storage facility, they would have

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to make good that, so that obviously would be quite impractical, to remove hydrants from underneath the apron.

So, I guess, one aspect that we would be considering should the JUHI currently (indistinct) continues for us to have to purchase that off the JUHI.

COMMISSIONER LINDWALL: Yes, it's an – sorry, go on.

COMMISSIONER BAXTER: No.

COMMISSIONER LINDWALL: I was going to say, that has an interesting dynamics, both for the owner of the infrastructure, as it is, and you, of course, as an airport, because the make good would be quite expensive for the oil companies, and they perhaps might be willing to sell it for a fairly low price, perhaps. I don't know, otherwise.

MR PEREIRA: Yes, I think from their point of view, that they would argue it would be quite expensive for them to move, but they would be willing to do it, as they're not short of capital. So they do have a very funny negotiating condition, as well (indistinct).

COMMISSIONER LINDWALL: I'm sure. I'm sure. Now, what's the type of supply to Perth in terms of the reliability and the redundancy and the capacity should there be disruption?

MR MASON: So, there's a single source of supply (indistinct) the pipeline, a major pipeline, to Kewdale, which is an off airport fuel storage facility. That has, we understand, 11 days of (indistinct) of field supply for the airport, which runs in a further pipeline, which we understand to be slightly constrained in terms of its capacity to pump fuel to the on-airport storage, the site.

But there are plans to upgrade that, and so then it flows onto the pipe into our on-site storage facility, which we understand to have about two to three days of storage capacity. I do know that that storage capacity on-site does not meet the IATA guidelines, and I believe that it's similar at other airports.

So there's no – so the big issue for us, then, with regard to security of supply, there's no alternative method of getting fuel to the airport. So we are very keen, in negotiations that we are about to commence, that there be – to get a road bridge in – capability into the airport, such that should any of the infrastructure that supplies fuel to the airports go down, that we have an alternative in place.

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COMMISSIONER KING: Yes. So just to be crystal clear, so at the moment, it would not be possible to truck jet fuel into the airport?

MR MASON: No, there is an ability to take some element of trucking, a trucking redundancy element, into the current storage facility. However, it would be limited, as it is at the moment, and part of the reason why we won't move the facility to a different site is also in issue, which is really around, yes, we can take trucks, but to – that the sheer logging of traffic would be competing with normal airport traffic along the arterial roads into the terminal precinct.

So, it can take it, but it's certainly not a (indistinct), and I just need to add that the other issue is the ability of supply redundancy, so there's security of supply that make the supply chain efficient from that perspective. So we would like to see a road bridging facility at either the current or at a different site. At a different site.

COMMISSIONER LINDWALL: In terms – sorry, did you?

COMMISSIONER KING: No, no.

COMMISSIONER LINDWALL: In terms of your, you know, you said that the storage on airport of two to three days doesn't meet IATA standards, and given that the leases are expiring in March 2022, that period from now to then would seem to be a period where your airport will probably grow in traffic, so the actual - - -

MR PEREIRA: Grow in traffic.

COMMISSIONER LINDWALL: Can you hear me?

MR PEREIRA: Yes, yes.

COMMISSIONER LINDWALL: So I was going to say that it could get worse, and yet there'll be very little incentive for the current leaseholders to invest, given the termination of the lease, and the renegotiations in 2022. So, I guess, what are your contingencies for that?

MR PEREIRA: So, we're not expecting – I guess, if you think about traffic at Perth Airport, we're at – volume wise, we're actually down from where we were about four years ago, and so if we look forward three years, even on a pretty optimistic growth profile, we're not expecting the storage issue (indistinct) being a limitation in the next three years.

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You're right, in terms of the longer term, hence, it's part of this negotiation which we're having for new facilities, we'll be looking at outside storage for that new facility.

COMMISSIONER LINDWALL: Okay. Yes. Now, the Department of Infrastructure and BARA have proposed a – that there be a sort of a consultative forum set up involving the state government and the federal government, and so forth, and the airport operator and fuel companies and airlines.

What do you think about that? There was something – this was done in Melbourne Airport, we heard earlier. What do you think about the prospects?

MR PEREIRA: So there's a little bit of feedback from the last (indistinct) I think the concept that involves the stakeholders - - -

COMMISSIONER LINDWALL: Could we stop there for a second, and see if we can regenerate this, or. So, if someone has dialled on, could you put yourself on mute? Hello.

COMMISSIONER KING: So long as everybody as except Perth Airport's on mute, please. All right. Let's try again.

COMMISSIONER LINDWALL: Try again. Yes, please.

COMMISSIONER KING: Hello Perth, welcome back.

COMMISSIONER LINDWALL: Hello Perth, again. I think we can hear you a bit clearer now. Did you hear my question about consultation, the forum, and how Melbourne had a forum set up?

MR MASON: Yes, yes. We did. So, I think we would support that. I think, for us, that consultative forum which involved all the key stakeholders and interested parties would be a valuable, sensible thing to do, as long as didn't impact the commercial (indistinct) negotiations. For me, that would be between ourselves and the JUHI.

COMMISSIONER LINDWALL: Yes.

MR MASON: But adding into the process would be (indistinct).

COMMISSIONER LINDWALL: Okay. Sorry, you can ask now.

COMMISSIONER KING: I was going to shift directions. Can I - - -

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COMMISSIONER LINDWALL: Completed this. There's nothing more – anything more on consultation?

COMMISSIONER KING: No.

COMMISSIONER BAXTER: No.

COMMISSIONER LINDWALL: No, I think that's probably – I just wanted to see that you would generally support it, basically.

COMMISSIONER KING: What I'd like to do, you'd be aware that Sydney Airport, five, six years ago now, there was an application for declaration under part 3A, for their JUHI facilities.

Now that was unsuccessful, but obviously, Perth is not Sydney, and things change over time. Are you aware of any interest in going down that path in Perth, to the degree that there's issues with getting access to the JUHI. In particular, has Perth Airport itself actually considered whether it should go down that direction?

MR PEREIRA: We're not aware of anyone going down that path, or interested in going down that path. That would be an aggression, and in terms of the second part of the question, no. No, we haven't considered going down that path either. I guess we're in good faith negotiations at the moment. We don't believe we've gone down that path far enough to even have a view on that just yet.

But we think we can find the outcomes privately in commercial negotiations. If we can't, then we've also put out an expression of interest recently to see if there are interested parties in working with us on a preferred model.

COMMISSIONER LINDWALL: I think you said in the submission, or somewhere, that somewhere, that you don't have a formal avenue for the airport to have input into the management of the infrastructure of fuel. Does the current lease of – does that prevent you from requiring infrastructure owners to modify the infrastructure?

MR PEREIRA: It does require – we can't really talk too much about the lease, because we're just about to enter into negotiations.

COMMISSIONER LINDWALL: Yes.

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MR PEREIRA: But certainly, it does the require the JUHI to undertake the works, and I guess without – we do find the process a little bit cumbersome, in terms of getting the (indistinct) in terms of our planning, the ability to expand our network as required. Don't get caught up in those negotiations with the JUHI.

COMMISSIONER LINDWALL: Okay, yes. What type of – once you come to the new arrangements of an open access setup, which is what your objective is, would you see that being a 20 year contract? Or how do you determine the duration of your contracts?

MR PEREIRA: It would have to be long term in nature to support the investment, but the term we'd be flexible on. It could be anywhere between 10 and 30 years, to allow that (indistinct) negotiate – negotiation (indistinct).

COMMISSIONER LINDWALL: I see, yes. Ken, you wanted to say something, by the looks of it?

COMMISSIONER BAXTER: Mine was only a technical question about the state of the pipeline, and you mentioned that you're concerned there's a lack of transparency over the current conditions. I'm wondering whether that's advanced at all, and what's your real concerns about that?

MR PEREIRA: Yes. So our understanding is that the main pipeline that connects the refinery to BP's off airport storage facilities, which are just next to airport estate are some years old, and I guess we've been seeking assurances on the state, or the reliability of that infrastructure, and what would be their undertaking to keep that pipeline in adequate operating condition.

So we have been struggling on – in getting that information. However, we recently had a productive conversation with theAirBP CEO. They've given us the assurance that they will make that part of that information available so we can get – we can satisfy ourselves as to the reliability of that pipeline.

MR MASON: Can I maybe add to that? One of the Metronet rail projects opened a portion of their (indistinct) the rail reserve, and there's a road expansion project about to commence, and the pipeline needs to move, and I guess our other concern was what – what assurances do we have when the pipeline is moved, and connected and reconnected that we (indistinct) caught short.

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Again, with the meetings of the three of us, senior members of the (indistinct) they will provide us that – assurance that three should be no issue with that. But I think that just heightens the, you know, our visibility and our concerns around (indistinct).

So we can certainly (indistinct) we've got the submission in, but a lot of work to do to get back being able to share that information, or we have not (indistinct).

COMMISSIONER KING: A slightly different direction. Does Perth have a fuel throughput levy?

MR PEREIRA: No.

COMMISSIONER KING: No. Any reason for that? I mean, obviously, there are different practices around the country, and it would be good from our perspective to understand why different airports pursue these different practices. Why did Perth decide not to have such a levy?

MR PEREIRA: I think, I guess, we don't have one for a couple of reasons, and it's primarily around the fact that we are quite a remote airport, and face competition and making sure that the – that the costs of operating Perth Airport are as low as possible makes sense.

For us, that's something that we wouldn't change, unless the throughput levy was (indistinct) some sort of recovery of infrastructure that we had invested in, we don't see a need to do that, and in fact, we're all about trying to make sure there is increased reliabilities and securities that (indistinct) of fuel, so that it allows us to be more competitive to attract new airlines to Perth.

COMMISSIONER KING: Okay.

MR PEREIRA: Again, we're effectively the landlords for all of the infrastructure owned, operated and maintained. So there's no – we don't believe there's any good reason for us to be seeking any sort of levy yet.

COMMISSIONER KING: Yes.

MR PEREIRA: It's not in the best interest for the airline.

COMMISSIONER LINDWALL: Obviously, if you moved to say a Darwin type of arrangement where you actually own the infrastructure, you'll have to think about the types of mechanisms to recover the cost of that infrastructure over time.

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MR PEREIRA: Yes, and – yes. But I think in that particular situation I don't think we would link it to volume. It would simply a return on that infrastructure that might be linked to the aeronautical price for airlines operating, not a throughput levy.

COMMISSIONER KING: Okay. You're quite adamant there not to use a volume based charge. We've certainly heard from other airports that they consider that a volume based charge, together with some sort of fixed charge, is just standard, what you'd expect in a rental agreement for facilities like the JUHI. So, I'm interested in how strongly you're pushing back against that?

MR PEREIRA: I think that's our preferred option. I'm not ruling out that we would go down – go down that path. But from our viewpoint, it makes more sense to simply - similar to the building block approach in how we determine prices for (indistinct) price for passenger landing rates. Our charges would need to do that, rather than a throughput levy based on volume of fuel. We see that (indistinct) a return on capital investment.

COMMISSIONER KING: Okay.

COMMISSIONER LINDWALL: What's the process for approving into plane services providers. If an entrant has a refuelling truck and customers, would they be able to supply fuel at the airport, if they're not part of your JUHI members?

MR PEREIRA: We probably can't – I can't comment on that, because we don't have that (indistinct) very much into the JUHI and other fuel operators and with the airlines (indistinct).

COMMISSIONER LINDWALL: Okay. Now, I'm sure you're aware the NOC system for notification, where there's a traffic light system about warnings for supply disruptions and so forth.

MR PEREIRA: Yes.

COMMISSIONER LINDWALL: What do you think about how it's worked for Perth Airport and what – if you have any problems, what would you change in it?

MS BLASKETT: Probably we're not the right people to comment on that. I mean, I've had some experience with NOC during the MH370 crisis. You know, when they identified the likely resting place of MH370, (indistinct) in terms of – and I can't remember that their system is, it either

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goes to black or red, whatever the system is in terms of identifying when we're at a critical stage in terms of shortage of fuel, but our chief operating officer is the person who gets those notifications, so we're probably not best placed to respond to that.

But I can certainly follow up and we can get some information back to you on that question.

COMMISSIONER LINDWALL: Okay. Thank you. That would be appreciated.

MS BLASKETT: I 'm sorry, I should actually get you to remind of just one thing, just on NOCs, and the issue of compliance with the IATA requirements and the amount of storage off-site and on-site. Obviously, there's an issue around security and failure of supply, but we did, during – in March 2014 when MH370 was identified as being likely to be found in the Southern Ocean, and then we had a number of search and rescue teams from around the world, and all the media came to Perth Airport, and that went on for two or three weeks.

We did actually get that critical notification from NOCs about fuel supplies running out at Perth Airport, and there had to be alternative arrangements put in place due to the that.

So I think there's issues there around – so we get that (indistinct) I anticipate that – and also, on the flipside, that issue of failure, but that might something to follow up with NOCs. I can't remember the detail around that.

I do remember, however, that that went (indistinct) to the joint agency coordination centre for MH370, and that was something that had to be dealt with at the time.

COMMISSIONER LINDWALL: I remember going to Perth during the middle of the global – sorry, the mining investment boom, where it was – not much space for passengers to sit down, and it was very, very busy, and 747s were flying from Melbourne and Sydney to Perth. What was the fuel supply system situation back then?

MS BLASKETT: Again, I'd need to get that information from the operations chain, but we will get back to you (indistinct) around that question around NOCs fuel supply. Yes.

COMMISSIONER LINDWALL: Okay. Thanks. Ken, did you have anything?

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COMMISSIONER BAXTER: No, I haven't got anything further.

COMMISSIONER LINDWALL: Do you have anything?

COMMISSIONER KING: I think that's about it, except for one thing that's slightly left of field that I asked the other airports. That, in today's Australian, there was an article where BARA, Barry Abrams, said that – out to Perth and Sydney and Melbourne and Brisbane, that luxury shopping strips within international airports are being blamed for distracting and confusing passengers to the point of causing flight delays. Is that something that you'd like to comment upon?

MS BLASKETT: Yes, absolutely, we'd like to comment upon it. So we're looking to any sort of, you know, investment in our departure lounges or, in fact, in our terminal, we obviously consult with the airlines. The international airlines, in particular, their commercial teams and also at the AOC level, they need to (indistinct) of the bid, for example, and the timing of the bid, but we had a situation here at Perth Airport, we really wanted to improve the FIDS at Perth Airport, particularly departures, and in terms of getting those videowalls up, they are actually very, very expensive, and we negotiated with the local airline operating committee around – in terms of the price, the cost of the FIDS system, and the videowall, and what price they were prepared to pay, and what proportion of the FIDS system. Therefore, the cost would be offset through that sort of retail aspect.

And that was an agreement with the airlines, because the bigger the videowall, the more expensive, and they were only prepared to pay a certain amount, so the cost is offset through that retail advertising.

The other point I'd make about the retail, particularly in the air side areas, which is what we're talking about, the departure lounge, you know, there is a – we've got an interest in getting passengers – passengers through those processing points. So, check-in and security screening as quickly as possible so that they're in that air side area, so that we don't have delays.

And one of the ways in which we do that is to have a good retail offering in the air side area, because every time, what happens with passengers, either come to the airport late, because there is nothing to actually entice them, I guess, to go through the security screening process into air side, or they (indistinct) and they think land side, for an extended period of time before they go into the air side area.

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So, we just don't think that there is anything in that, and at Perth Airport, for example, we consistently have the highest on time performance rate across Australia to the aircraft departure and arrival. So I don't actually think there's much in that assertion.

COMMISSIONER LINDWALL: I think you've answered that very well. But could I just clarify for the transcript, when you called, I think you said "FIDS". Is that a flight information display system, or something?

MS BLASKETT: Yes. Yes, that's right.

COMMISSIONER LINDWALL: Okay. It's handy for the transcript. Well, unless we've got any more question, thank you very much Brian, Allan, and Deb.

MR PEREIRA: Thank you.

MR MASON: Thank you.

MS BLASKETT: Thank you.

COMMISSIONER LINDWALL: Have a good day. Bye.

UNIDENTIFIED SPEAKER: So Caltex will be appearing a few minutes after 2 o'clock.

COMMISSIONER LINDWALL: Okay.

UNIDENTIFIED SPEAKER: So if you want grab a coffee or tea. They're appearing half an hour before schedule, which is - - -

COMMISSIONER LINDWALL: Excellent. Well, I might quickly go and get our taxi changed to 3 o'clock then.

UNIDENTIFIED SPEAKER: They should be there a minute or two after 2 o'clock.

COMMISSIONER LINDWALL: Sounds good. I'll be back in a sec.

SHORT ADJOURNMENT

COMMISSIONER LINDWALL: Hello, is that Philip?

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MR SKINNER: Yes, this is Philip and Rohan Dangerfield from Caltex.

COMMISSIONER LINDWALL: All right. Hello Philip and hello Rohan. I'm Paul Lindwall, the presiding Commissioner. I'll get my colleagues to say hello so you can hear their voice.

COMMISSIONER BAXTER: Hi, I'm Ken Baxter.

COMMISSIONER KING: Hi Philip and Rohan, I'm Stephen King.

COMMISSIONER LINDWALL: And if you wouldn't mind just saying your name so that our transcript gentleman can identify who's speaking, and also, if you want to give an opening statement, that would be fantastic.

MR DANGERFIELD: Okay. My name's Rohan Dangerfield. I'm the General Manager of Supply Operations at Caltex Australia.

MR SKINNER: And I'm Philip Skinner. I'm the Adviser for Government and Industry Affairs at Caltex Australia.

COMMISSIONER LINDWALL: Welcome.

MR DANGERFIELD: Have you seen it?

COMMISSIONER LINDWALL: Yes, please.

MR DANGERFIELD: So, good afternoon, everyone. I'd like to thank the Productivity Commission for allowing the opportunity for Caltex Australia to discuss our submission and take questions on the Australian jet fuel market.

Caltex has been operating in Australia since 1900 through various antecedent firms, and has developed a strong reputation for the safe and reliable supply of liquid transport fuels.

It's the largest Australian transport, fuel, and convenience company which is on the Australian Securities Exchange. Caltex is responsible for the supply of one third of the liquid transport fuels supplied in Australia to consumers from defence to maritime customers, and aviation partners to motoring enthusiasts.

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Caltex is also a strong and longstanding participant in the supply of jet fuel to Australian airports, and the design, construction, operation and maintenance of key supply infrastructure for jet and other fuel types.

Caltex markets jet fuel at nine airports in Australia, we're joint venture participants in the Joint User Hydrant Installations, or JUHIs, of five major airports, and are the sole owner, or JV partner in two key jet supply, pipelines in Sydney and Brisbane.

Caltex Australia firmly believes that the jet fuel supply market in Australia operates in an effective and competitive manner through the presence of multiple supply participants competing for volume and through various established supply infrastructure routes, which provide efficient, cost-effective, and competitive methods of delivery.

Furthermore, the presence of multiple supply competitors in the jet fuel market, coupled with the ability for airlines to tender for new supply partners on a regular basis, provides continual competitive pressures to ensure that fuel suppliers provide attractive offers.

We also don't believe that there are barriers to prevent new market entrants, as has been claimed by some parties in their public submissions.

It should be noted, though, that under existing market structures, mechanisms exist for new market participants to enter the various supply chains throughout Australia in a number of capacities, not least of all as equity partners in existing infrastructure networks, such as JUHI's, contracting through the supply chain, or through tendering access to existing infrastructure networks.

An example of this exists in Sydney at Kingsford Smith Airport where Qantas operates as an equity partner in the Sydney Joint User Hydrant Installation, and imports their own supply with a fuel partner.

Another example of opportunities for access is that Caltex has been undertaking a tender process for parties looking to utilise excess capacity within our pipeline network.

These are regular occurrences which demonstrate the opportunities which do exist within the current market for new entrants.

When looking at comparative fuel prices at an international level, it's important to note that as a net importer of liquid transport fuels in Australia, we are beholden to international factors which impact cost, at

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which jet fuel, and indeed all transport fuels, can be supplied to the Australian market.

Given the costs associated with sourcing product, coupled with the cost of transport to Australia, storage and distribution of product, supply prices for jet fuel in Australia reflect reasonable cost associated with supplying product to market.

This has been looked at in the past, not least of all by the National Competition Council, when they were investigating the jet fuel supply infrastructure in Sydney, who found the argument that jet fuel differentials did not point to excessive pricing or abuse of market power was compelling.

In closing, Caltex Australia welcomes the opportunity to discuss this matter with the Productivity Commission. However, we do note, that given its commercial sensitivities, there may be some areas of questioning which we will not be able to respond to in a public forum.

We will, however, note that two members of the Australian Institute of Petroleum have supplied the Productivity Commission with comprehensive public submissions, seeking to address the items raised by the inquiry. Caltex Australia has reviewed both of these submissions, and believe they present an accurate reflection of the jet fuel supply market in Australia.

I welcome your questions.

COMMISSIONER LINDWALL: Well, thank you very much, Rohan and Philip. Maybe I might start on security of supply, since that's been a bit of a topic, and that's about your views of how the NOCs system of reporting the traffic light system is working. Should it be improved? How do you find – well, there were some black light issues in Melbourne, and what would you say are the biggest issues that lead to that type of risk, and what are the best ways of ameliorating that?

Now, I understand that, as a bit of background, that the IATA guidelines say that there should be a supply of about three days or more in storage at each airport. So perhaps you could comment on that type of topic.

MR DANGERFIELD: It's a very broad ranging question.

COMMISSIONER LINDWALL: Yes.

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MR DANGERFIELD: I might just check in my IATA guidelines. I'm familiar with the IATA guidance on airport fuel storage capacity. My read of the guidance is that it does not specify a number of days. It rather sets out a methodology where people should review the supply chain infrastructure to an airport, and use that to make an assessment of what is the right level of storage in a market. It does not give a specific answer.

So that's the first point on the IATA guidelines. So, if some people refer to that three days coverage number. It's not actually in the IATA guidelines.

COMMISSIONER LINDWALL: Okay.

MR DANGERFIELD: So there's that point, and then back, you were asking about the NOC process?

COMMISSIONER LINDWALL: Yes.

MR SKINNER: I think, from our point of view, the NOCs process does provide a reasonable mechanism for observing the current situation at major airports around Australia and New Zealand. I note that over the last, well, few months, they had – sorry, last year, they had a consultation to bolt that into the NOSEC as well, to ensure that both within companies and industry participants that there are the appropriate supply personnel who would be linked, and receiving information.

So I think that we would be advising that that's currently an effective system of monitoring occurrences, and think just to touch on the Melbourne Airport situation, that's probably a good indication of how a situation can occur when there isn't certainty of tenure to allow for suitable infrastructure developments to occur.

That's something which since the new agreement the industry has been taking steps to increase storage capacities, and other facilities at Melbourne Airport.

COMMISSIONER LINDWALL: Okay. Overall, in Australia, you've spoken about Melbourne, are there other airports you've been – you're involved with where you would have more concerns about lack of redundancy of supply? Or risk to supply?

MR DANGERFIELD: Each situation carries its unique risks, but I don't – I think probably the industry would have acknowledged Melbourne was one of the tightest. There's been significant investment in Melbourne by ourselves and other off-airport in recent years, and Philip referred to some of the current works that are underway.

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At Melbourne JUHI at the moment, I think, Melbourne Airport, in their discussions this morning, commented on some of those as well.

COMMISSIONER LINDWALL: Okay. Any more on supply, do you think?

COMMISSIONER KING: No.

COMMISSIONER LINDWALL: No, I think we might move on from that, unless Ken, you've got something on supply?

COMMISSIONER BAXTER: No, no. Only just to ask the question, I presume that Caltex, these days, brings its aviation fuel out of somewhere like Singapore, or it does it refine it in existing Australian refineries?

MR DANGERFIELD: So yes, we've got a refinery in Brisbane at Lytton, where we produce jet fuel. We also have import orders of jet fuel into Australia from a range of locations around Asia and further afield. We also buy jet fuel at a wholesale level in country as well.

COMMISSIONER BAXTER: Okay.

COMMISSIONER LINDWALL: Now, perhaps you could comment on what you as a company feel about entering a market which is in different structures? So Darwin, for example, is moving to a more pure, open access scheme. Melbourne has a JUHI which has open access as part of it. Brisbane has a more traditional setup.

So of those three, I mean, if you're providing fuel, does it – how do you view each of those options?

MR DANGERFIELD: So, in any – in any market, we would choose to use whatever facilities were available.

COMMISSIONER LINDWALL: Yes.

MR DANGERFIELD: Or set up our own in parallel, if we thought we could do so more efficiently.

COMMISSIONER LINDWALL: Okay.

COMMISSIONER KING: Well, just on that, I note that you said – sorry, please continue.

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MR DANGERFIELD: I'm not quite sure if that answers your question, but - - -

COMMISSIONER LINDWALL: Well, I mean, I think it does, in the main. But effectively, you're neutral. I mean, obviously, if you're a JUHI participant and you have a contract, then you run the JUHI and its investment according to the other operators in that joint venture.

But if you're going to Darwin, you would compete with other fuel providers to provide fuel to customers in Darwin just as easily, I guess. So the only difference is that in one you've got an equity ownership.

MR DANGERFIELD: Just to be clear, the JUHI structure is a joint venture arrangement for the owning of infrastructure, and we have some access rights by nature of our equity participation. But the fuel supply and marketing is done by ourselves. The JUHIs have no role in marketing.

COMMISSIONER KING: No. No, I understand that. Can I just go into a bit more detail on that? So, from your opening remarks, I think you said that Caltex is a joint venture member in five JUHIs, or JUHIs of five airports, but you're supplying at nine airports. So, is that correct?

MR DANGERFIELD: That's correct.

COMMISSIONER KING: Yes. So the four airports where you're not – or you're not in the JV, the JUHI JV, how are you supplying at those airports?

MR DANGERFIELD: So, one airport we own the fuel facility ourselves, outright and lease land off the airport. Another location we've chosen to not invest in the new facility in the airport, so we're contracting through the owner of the infrastructure of that airport.

Another one, it's owned by an independent company. We operate that facility for them, and - - -

COMMISSIONER KING: The fourth one.

MR DANGERFIELD: I've covered them all.

COMMISSIONER LINDWALL: I think there was one more.

COMMISSIONER KING: So there's one facility that you own, one you operate.

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MR DANGERFIELD: There's another airport where we're a joint venture member of the fuel storage facility on site, and we contract with another company for into plane service.

COMMISSIONER LINDWALL: Okay.

COMMISSIONER KING: Okay. So, just the one where you're contracting with the owner of the infrastructure, are you able to say which airport that is?

MR DANGERFIELD: That would be Canberra.

COMMISSIONER KING: Okay. So Canberra. Every fuel supplier there would be on an equal footing, because as I understand it, the Canberra Airport owns the JUHI.

MR DANGERFIELD: No. So Canberra Airport don't own the fuel facility. The fuel facility's owned by a company called Southern Aviation.

COMMISSIONER KING: Okay. And who owns Southern Aviation?

COMMISSIONER LINDWALL: Ask him, if you wish.

COMMISSIONER KING: Well, who's the ultimate owner in Southern Aviation?

MR DANGERFIELD: I'm not sure.

MR SKINNER: I think you'd have to look at that company to get that information.

COMMISSIONER KING: Okay. So, none of those airports where there is a JUHI – well actually, no. I'll just check. The last one where you said you are joint owners of the storage; do you then access a JUHI that's owned by a joint venture? Again, I guess I could ask first off, are you able to say which airport it is?

MR DANGERFIELD: I don't quite understand the question.

COMMISSIONER KING: Sorry. The last one that you mentioned, you said you had – you were a participant in a joint owned storage facility, but you didn't have any interest in the actual hydrant facilities.

MR DANGERFIELD: No, that airport doesn't have a hydrant facility.

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COMMISSIONER KING: Okay.

MR DANGERFIELD: It's all tanker refuelling.

COMMISSIONER KING: Okay. Apologies. I misheard that. Okay. So, that leaves us in a situation where you've said that you believe that there's competition, and that with the JUHIs, or where there are joint venture JUHIs, you use the same example that everyone uses, which is Qantas was able to get equity access to a JUHI in Sydney. A nice, simple, interesting example, but I get very worried about examples of effective regimes where you can only come up with the one example, and everyone comes up with the same example.

What other evidence can we take from you that the equity access approach for JUHIs is actually efficient, rather than just simply being a closed shop, leading to a small group, an oligopoly of fuel – of fuel suppliers controlling the critical infrastructure?

MR DANGERFIELD: So, at a range of airports, where other parties have expressed interest in joining, but have chosen not to, I guess we do note that around the country, I think we referred to a couple of examples, there's a variety of models starting to exist.

Melbourne Airport, for example, you referred to, and they covered it in their submission this morning, and Darwin Airport's making changes as well.

COMMISSIONER KING: So those changes appear to have been driven, at least in part, by the relevant airports being dissatisfied with the traditional JUHI approach. So we see people dissatisfied with that JUHI approach. We see only one example, historically, of anyone being able to gain access there, and that's the Qantas equity access, and that all paints a picture for us that the traditional JUHI approach is, at best, flawed, and at worst, not working.

MR DANGERFIELD: I think it comes to the point of the what JUHI arrangements are, and it's to provide an efficient model for owning infrastructure on airports that it makes sense to have joint users rather than people owning infrastructure in parallel, and that helps reduce investment costs, provide efficiency, and I think that was shown in the feedback to the NCC investigation into infrastructure. I think that what's it found, that indeed it was delivering on that.

COMMISSIONER LINDWALL: I certainly agree that a joint venture can produce efficiencies and that by not duplicating infrastructure. But,

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you know, if you look at the Telstra example, where it was both the infrastructure supplier as well as the supplier to customers, a vertical integration problem there. Wouldn't it be true to say that a joint venture which doesn't have fuel companies in it is likely to be more competitive than one that does?

MR DANGERFIELD: So I think the point of the joint ventures are infrastructure, ownership, and operation arrangements. They're not marketing entities, or where fuel suppliers make their own marketing arrangements quite independently of each other, and I think that's our observation, it's a very competitive market.

COMMISSIONER LINDWALL: Okay.

MR DANGERFIELD: I think we'd also note, after some feedback from our customers and potential customers, that across locations we see evidence of other companies contracting their way through the supply chain with various infrastructure and asset owners and fuel suppliers to gain access in a different part of the supply chain from international supplier, right through to the airplane wing.

COMMISSIONER LINDWALL: Could I ask, if you've got – just to tell the mechanics of this – if you're in a JV JUHI with, say, four members, three other members, plus Caltex, and you're supplying, I don't know, let's say 25 per cent of the fuel at that airport, and then you reach a new agreement with an airline to – and it now means that you're 40 per cent of the fuel supplied in the airport, do you then arrange to get a larger percentage of the JUHI joint venture, or do you continue with your original 25 per cent?

MR DANGERFIELD: As an equity participant, equity percentage is not directly relevant to the throughput percentage.

COMMISSIONER LINDWALL: Okay. Yes, I thought that was the case. So it doesn't adjust.

MR DANGERFIELD: So there's an equity ownership share, and your percentage of throughput somewhere from 25 to 40 per cent, and that's quite separate.

COMMISSIONER LINDWALL: Okay.

COMMISSIONER KING: So, just on the – well, so first off, the joint ventures that run the JUHI, are they for profit, or not for profit, in the sense of, do they own – is there a formal part of the arrangement in the

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joint venture that they only recover cost, or they are priced to make a profit?

MR DANGERFIELD: So, the standard arrangement for JUHIs in Australia is they're unincorporated joint ventures, and so the operator adjusts apportioned costs between the equity owners and the throughputters. There's no profit and loss within the entity.

COMMISSIONER KING: Okay.

MR DANGERFIELD: It's just a cost-sharing arrangement.

COMMISSIONER KING: I have heard that – sorry, go on.

MR DANGERFIELD: Yes, so if there's a capital investment made equity, participants contribute. So equity investments in capital items, and then there's a cost-sharing for operations.

COMMISSIONER KING: And new investment, obviously.

MR DANGERFIELD: There's no profit or loss within the JUHI structure itself.

COMMISSIONER KING: Although, if Caltex, just to pick up on Paul's example, if Caltex was supplying more fuel through the JUHI, there would be a charge from the JUHI to Caltex for the increased fuel that Caltex put through, which – so the JUHI members would only be liable for any difference between the fees collected and costs, presumably.

MR DANGERFIELD: So, the arrangement is slightly different between locations. But as a general principle, some costs are shared by equity, and some costs are shared by throughput.

COMMISSIONER LINDWALL: Okay.

COMMISSIONER KING: Okay.

MR DANGERFIELD: So as a larger throughputter you would pay a larger share of the costs.

COMMISSIONER KING: Yes, okay.

COMMISSIONER BAXTER: And is that a fixed arrangement across all the JUHIs in Australia, or is it just a case by case?

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COMMISSIONER LINDWALL: It's different, by the sound of it.

COMMISSIONER BAXTER: Yes.

COMMISSIONER KING: It sounds like they're different.

MR DANGERFIELD: Case by case, these joint ventures are established, or change over time, their discussion between joint venture partners on how they wish to structure their joint venture arrangement.

COMMISSIONER LINDWALL: Now, I mean, has Caltex ever tried to enter an existing JUHI which you're not a member of? For example, I don't think you're a member of Adelaide's JUHI. I mean, have you ever attempted that?

MR DANGERFIELD: Yes, we have.

COMMISSIONER LINDWALL: And you've been successful?

MR DANGERFIELD: We've chosen not to proceed.

COMMISSIONER LINDWALL: I understand that one of the issue about entry into an existing JUHI is that the prices charged for the new entry is based upon the current valuation, and then the returns that they receive as a member are based upon the historic cost, and that generally would mean that it's – the returns are not really worth investing in. Would you care to comment on that?

MR DANGERFIELD: Any particular arrangement is unique to the location.

COMMISSIONER LINDWALL: Okay. Fair enough. Yes. Could I now move onto something that we had a testimony a couple of days ago from Bioenergy Australia, and they were talking about a biofuel trial in Brisbane, which I understand, and they said that Caltex was involved in, and they said that it took an inordinate amount of testing, well above what – and I'm not an expert, I'm just telling you what they told us.

That the fuel apparently, there's less impurities, it's a higher energy content, or thermal content, more dense, in other words, and that it was tested many more times than other fuel, and that the process took many, many months. That's what I pretty much (indistinct).

So do you have any comment on that, since I understand they worked through you to provide the mixing of that biofuel with the normal Avgas?

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MR DANGERFIELD: Yes. So I'd better comment on that. So yes, we worked with one of our customers, being Virgin, in Brisbane to help facilitate a trial of putting Biojet through the supply chain in Brisbane. So we worked with Virgin on that. We had it added to our supply chain back at our Lytton refinery, and transitioned that through the supply chain to Brisbane Airport.

We worked with our various infrastructure partners, and both on and off airport, then with the JUHIs to facilitate that, and that was done quite successfully. There was a public function run between the state government, the airport, and Virgin and ourselves, to announce that when that happened.

With regards to the quality checking through the supply chain, I think it's an area that's been developing in the industry. I think we worked with Virgin, as I said, and also the other joint venture members in the JUHI, and that was done successfully, and that would (indistinct) successfully achieved.

I should also note that since that trial, it was done under trial conditions, so there was sort of extra focus on making sure it could it could be done safely and reliably, that some of the industry standards they could continue to evolve in that space to document how those things should be done all around the world.

MR SKINNER: If I could just add to that. It completely derives from it being a jet fuel. Jet, by its very nature, is tested far more stringently than gasoline or diesel utilised for road transport purposes, and there's very specific rationale behind that. Effectively, you do have to take greater safety precautions with a jet aircraft, and with the specific fuel.

On the Virgin Biojet trial, this was our first trial of utilising established infrastructures, including our pipeline to the airport, and the Joint User Hydrant facility for a Biojet, that at the time, was still going through the process of being assessed for inclusion in international fuel standards for jets.

So, with it being the first trial of its kind in that nature, there was, I believe, one or two additional test undertaken, but the remainder of the tests were actually in line with similar tests that we undertake to supply standard jet fuel to airports all around Australia.

COMMISSIONER LINDWALL: Okay. I think – sorry.

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MR SKINNER: Sorry, I would also note, if I could just add to that, that since then, that particular Biojet created through that technical pathway has now been approved for use under both the ASTM and DEFSTAN. So that means that for future trials, and I believe we are going through the process of undertaking a second shipment currently. It will be a lot easier in that process in terms of other processes we did have to go through at the time to allow for it to be supplied through the JUHI system.

COMMISSIONER LINDWALL: Okay. Now, one of the things that's come out from a number of participants is that the whole nature of the JUHIs, and the entry conditions, and the prices, costs, and profits, are very opaque and not – well, they're opaque. They're not transparent.

Why is that so? And I also note that most of the fuel companies that have participated with us have tended to provide confidential submissions, rather than public ones. Why is that the case, and why should that be the case?

MR DANGERFIELD: I think it's the case because they're privately owned assets, and there's arrangements between different private companies. Then there's still many elements to the supply chain, both petrol, jet fuel and diesel, and jet fuel sales to customers that are individually negotiated, and they're confidential between ourselves and them.

COMMISSIONER LINDWALL: If you want to add anything to that?

COMMISSIONER KING: Well, whilst I understand why parts of the supply chain confidentiality would be important, if the JUHIs are just being run on a cost recovery basis, it does strike me as being – the degree of confidentiality does seem slightly odd. I can't see what would be the problem, if it really is cost recovery, what would be the problem with the details of that cost recovery being public.

MR DANGERFIELD: So, I guess it I would – so some JUHIs, the through putters, the (indistinct) they have poor visibility on the costs, and can ensure things are done efficiently. Through various parts of the supply chain, we contracted others and pay a throughput fee that's individually negotiated and doesn't – you know, is (indistinct) its own right. It's obvious that some of those other locations where we contract with others.

COMMISSIONER KING: Okay. So, for example, you've got pipelines at Sydney and Brisbane, but so you would charge a throughput levy for

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those pipelines, presumably? Well, sorry, throughput charge. I shouldn't call it throughput levy.

MR DANGERFIELD: So, in Sydney, when a – it's going back maybe (indistinct) eight years now, so it's making significant investment in the order of tens of millions of dollars in our pipeline on Sydney Airport. Probably now coming up to 15 years, we contracted with other parties for access to our pipeline. They've taken a number of different – they've been structured a number of different ways over the – over that time.

At the moment, we periodically run a tender for access to our pipeline in Sydney and many fuel suppliers would get involved in the fuel supply chain have participated in having a contract with a number of parties for pipeline access.

COMMISSIONER KING: So when you say many fuel suppliers.

MR DANGERFIELD: Sydney, Brisbane. Sorry, I'll just say, in Brisbane we – the pipeline to the airport, we had a joint venture with another fuel company on that. We only supply ourselves through that line.

COMMISSIONER KING: Okay. So, in the case of Sydney, for capacity to the airport, presumably the only parties who could track for that are the JUHI participants? And Qantas, I guess, would be the other one, because – sorry, it is a JUHI participant.

So, I mean, does anybody other than the JUHI participants tender for pipeline capacity to Sydney Airport?

MR DANGERFIELD: Over the years, we've received tender submissions from a wide variety of companies beyond the JUHI participants.

COMMISSIONER LINDWALL: Have they been successful?

COMMISSIONER KING: You can ask that.

COMMISSIONER LINDWALL: Have any of them been successful?

MR DANGERFIELD: Yes.

COMMISSIONER LINDWALL: Okay.

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COMMISSIONER KING: Are you able to tell us what they were doing with the fuel at the other end? Were they then on-selling to one of the JUHI participants, or?

MR DANGERFIELD: We don't have direct knowledge of their arrangements.

COMMISSIONER KING: Okay. No, no. That's fair enough.

COMMISSIONER LINDWALL: Could I ask, to what – you know, there's been some testimony about the use of trucks versus pipelines, and obviously sometimes concerns about environmental safety factors in regard to trucks. Also congestion factors around Perth, for example, was said today.

To what extent do you think trucking fuel is a substitute to the pipeline, and where do you see the industry developing in respect to trucking versus pipeline development?

MR DANGERFIELD: Yes. I think our observation would be trucking is a very efficient way of moving transport fuels, even jet fuel. Smaller airports tend to be exclusively truck fed. So airports at places like that would be Cairns, Townsville, Gold Coast, Canberra. You know, those sorts of locations are exclusively truck fed.

Major airports, I think Brisbane, Sydney, Melbourne, Perth, tend to be pipeline fed. Some of those larger airport have both pipeline and truck. Some airports have multiple pipelines.

I think the high capital intensity of pipelines tends to mean that you need large volume flows to make that efficient, and to be cost competitive with trucking. Trucking, by its nature, more trucks can be, usually at lower capital cost, and more flexibility sort of added or taken off the task and were used elsewhere within the supply chain, whereas pipelines tend to be very dedicated for one product, from one location to another.

COMMISSIONER LINDWALL: Okay. Yes. But I don't know if you can reflect on what happened in Auckland, where the pipeline was disrupted, and I'm not sure how long it took to repair that pipeline. But obviously, they had to substitute in a number of ways. I think that Wellington Airport grew in capacity for a little bit and took up some of the load, and obviously they had a lot more trucks going into Auckland. How quickly they got that on line, I'm not sure.

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MR DANGERFIELD: Yes, so I think we would usually observe that having more than one supply route to an airport would be important for reliability. Both pipeline and truck, or more than one pipeline. I should also note that trucking, typically by its – you know, trucks can go by different routes.

COMMISSIONER LINDWALL: Exactly.

MR DANGERFIELD: And usually in location, they're portable. Trucks on the tar, so if one road is blocked or one company's truck or trucks is out of action, usually there's others that provide redundancy reserves. Yes, usually multiple methods is best to provide some redundancy.

And, obviously, on airport capacity, storage capacity is an important factor in that. How much extra capacity, if that's used by the different pipeline or trucking routes, is available, and the amount of storage and the like upstream, they're all important factors.

COMMISSIONER LINDWALL: Okay. Yes, yes.

MR SKINNER: I might add that if there's a significant incident like in New Zealand, where a pipeline is out for a significant period of time, that's not a surprise there is some disruptions to supply to an airport.

COMMISSIONER LINDWALL: Do the arrangements for taking – approving plane service providers, vary by airport, I presume? And if you wanted to be a new entrant, and buy a refuelling truck and supply fuel at the airport, would that vary, is there some common practices for that type of thing?

MR DANGERFIELD: So, on airport, there's a variety in into-plane arrangements. So when we talk about each plane, it's usually the trucks on the airports that sort of do the last bit of connection, either a tanker truck driving to the plane, or a hydrant dispenser connecting from they hydrant system to the plane.

They're both joint venture arrangements for those around the country. There's a lot of companies own their operations individually. Where companies own them individually, quite commonly, they contract that service out to others for a fee, and we also note, there's very low barriers to entry to enter into that space, given that the capital cost for purchasing refuelling trucks is better for it, and where joint ventures exist, usually there are provisions for people to join a joint venture also.

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COMMISSIONER LINDWALL: Okay. I mean, we heard that current into plane providers have been unwilling supply fuel for potential entrants. Do you agree with that?

MR DANGERFIELD: Could you just repeat the question? It sort of dropped out a little bit there.

COMMISSIONER LINDWALL: Sorry, current into plane providers have been unwilling to supply fuel for potential entrants.

MR DANGERFIELD: So, usually an into plane provider wouldn't supply fuel. They would provide an into plane service. Our observation, we contract both the – we contract with others both to do into plane for us, and we do into plane for other locations. So I'm surprised to hear that.

COMMISSIONER LINDWALL: Okay. What about various jet fuel throughput levies, that some airports levy, or charge, and others don't? Do you have any views on that?

MR DANGERFIELD: Yes. So there's a few different ranges – few different arrangements. I guess we – our overarching comment is really that Caltex firmly supports the ICAO principle there, what charges should be related to the cost of providing airport facilities and services.

COMMISSIONER LINDWALL: Okay. Yes, all right. Now, another thing that happened is that the Victorian government promoted a consultative forum in Melbourne Airport, which involved the state government, the federal government, I think, and airports and air – the airport and fuel companies, and airlines. Was Caltex part of that, and if so, what did you – how did find it? Helpful, or useful, or valuable?

MR DANGERFIELD: I think we were part of that process. There's been a number of forums like that that have come and gone over time. I think it's all a bit specific at each of the locations, the state of the supply chain, noting in some markets fuel supplies, infrastructure providers, and the like tend to self-organise individually, or jointly make an investment without those types of arrangements, and you know, they (indistinct) competitive infrastructure is usually built by multiple parties, you know, to provide multiple means of getting fuel to market.

But perhaps they can be – some of those forums can be useful at times, to address specific issues of concern. But in general, our observation is they wouldn't be – wouldn't be necessary, but usually if they exist, we would choose to participate.

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COMMISSIONER LINDWALL: Okay. I've also heard from AIP that the reason – well, the claim is that the underinvestment in jet fuel infrastructure in Melbourne Airport was due to a lack of lease tenure, and you alluded to that earlier when you said that the new contract has been brought to provide some scope for additional investment, and building up capacity.

What type of lease tenure do you think is optimal? I mean, I think that's a 20 year one. Is there a minimum period that you would consider viable? Or is 10 years too short, for example?

MR DANGERFIELD: It's a little bit dependent on the location, the historic investment, what future investment, for example, might be required. Where significant investment's required, for assets that have a life of 20, 30, 40 plus years, usually, we would expect that the tenure would be roughly in line with the asset life. So, the use of the asset can be achieved over the tenure of the lease. If you get 20 years into that 30 year period, (indistinct).

COMMISSIONER LINDWALL: Sorry, it's breaking up a little bit.

MR DANGERFIELD: So then (indistinct)

COMMISSIONER LINDWALL: Hello. We're missing a number of that, and I don't think we got the last minute or so. I don't know if someone else has come on and put the microphone on. Could you try again, sorry?

MR DANGERFIELD: Yes, I can say it again. So, investments in sort of steel and concrete to the tanks and pipelines would tend to be 20, 30, 40 year plus life.

COMMISSIONER LINDWALL: Yes.

MR DANGERFIELD: So, having tenures in line with the life of the assets would generally make sense. I guess we note that when you're partway through a tenure period, or as you approach the end of it, well then it's the remaining tenure that's the important piece, rather than overall term.

My other observation would be that the JUHI participants are usually very proactive. Say, five years out from a lease coming to a conclusion, to engage with the airports to talk about the next term.

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COMMISSIONER LINDWALL: Okay. Thanks.

MR DANGERFIELD: Provide (indistinct) for everyone.

COMMISSIONER LINDWALL: Did you have any - - -

COMMISSIONER KING: I've only got one other set of questions which, really coming back to a problem that we have. So, hopefully, you'll be able to help us out.

We're in the situation where we've heard a lot about complaints from airlines about the prices that they pay for jet fuel. Claims that our – for prices airlines pay in Australia are out of line with the rest of the world.

As you'd be aware from the public submissions, BARA's put in essentially an updated of the IATA data that they provided to the NCC for the Sydney declaration.

You'd be aware that the NCC said, well, unfortunately that data, by itself, doesn't give a great deal, or has very little value, because it doesn't provide any explanation for price differentials around the world, and you're probably also aware that a report was put in by RBB to the NCC, which apparently, although the – there's only a public version, which is redacted, available through the NCC.

But that, apparently, was an attempt to show that any price differentials in Australia could be explained by differences in transport costs, fuel – taxes, and so on. Obviously, we don't have access to that report at the moment.

That puts us in a bit of a quandary. We've got a lot of anecdotal material put to us saying that the prices are high, but we have very little hard evidence to say that the prices are high.

So, I guess my question really is, given that you're one side of these contracts, are you able to provide us with better information that we can use to evaluate whether the jet fuel prices in Australia are, or are not, out of line with what you would expect in comparison to other airports around the world.

MR DANGERFIELD: Yes. So, Caltex Australia only markets jet fuel within Australia, but I will make some – a couple of observations, and I can't just think which submission it was in, but I can talk generally to it.

Someone had a chart showing differentials above the MOPS jet price, doing a comparison of Australia versus other locations, including

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Singapore. I think it's important to understand how pricing around the world, and particularly in this case in Australia, work.

So, commonly in Australia, fuel suppliers price all fuels at an import parity basis into Australia, given Australia is a net importer of finished product, and that's certainly true in the case of jet fuel.

In Asia, the commonly traded jet fuel market is Singapore and Platts quotes a – daily quotes a MOPS Singapore price for what is traded in Singapore.

And so usually Australia trades at a high price that's reflective for the cost to get it here, because as you remarked, a comment of what is imported into Australia would be Singapore into Australia, and so freights, shipping freight in Australia is a significant part of that.

I guess our observation would also be, in respect to airlines, the common structure is that pricing would be offered to an airline at the fixed differential, and that differential takes into account all other costs, which covers product freight into Australia, to get import parity basis, and we would note that that's in the order of multiple dollars per barrel, commonly, and it would also cover wharfage fees and a port storage fee for a terminal, trucking or pipeline type, on airport storage charges into plane working capital charges, things like that. That's usually offered to an airline as a big fixed number above the Singapore price.

So what that means is the fuel supplies typically take the risk on a fall of the other pricing element, and the airlines take the risk just on the MOPS Singapore price, which then they know who that different airlines, usually with that difference in a hedging strategies.

But I think, in line, like a lot of the difference between (indistinct)

COMMISSIONER KING: I guess that still leaves us – here we go again.

COMMISSIONER KING: Hello. Is this - - -

COMMISSIONER LINDWALL: If there's a person joined the call by the name of - - -

COMMISSIONER KING: Malvyn Tan.

COMMISSIONER LINDWALL: Please go on mute. He's left the meeting. Very good. Perth, are you still there? Sorry, Caltex. Are you still there?

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MR DANGERFIELD: Caltex still here.

COMMISSIONER KING: Yes, sorry. I'm happy to accept all of that, but from our perspective, we have two alternative stories, if I can put it that way. One is running through what you've just said to us, which is that it's cost based, the differential on mops, just simply reflects the cost.

The other is the parties who have put to us that, not saying that it's not reflective of cost, but that there's a bit of extra added in there, maybe only one or two cents a litre, which is profit to the fuel companies.

Have you got any suggestions as to how we can differentiate between those, and can you provide us with information to help us differentiate between those different views?

MR DANGERFIELD: I think, largely, we would probably have a number of commercial concerns with supplying information of that nature, especially at a company specific level. Yes, I'm not sure whether we would be in a position to provide the Productivity Commission with information that could assist directly with that, at least not at a Caltex level.

COMMISSIONER KING: Well, but perhaps you can take it on notice and consult your – AIPs as well, and see if there's more at an industry level, rather than company specific level data that might be illustrative that it's not - - -

MR DANGERFIELD: No, certainly I think (indistinct) Yes, I think, happy to have that discussion with AIP. But I think, obviously, the other thing to note there is that each individual airport, or more importantly, port, would have differences again. It would change from market to market.

COMMISSIONER KING: Of course. Of course.

COMMISSIONER LINDWALL: We understand that.

MR DANGERFIELD: Yes.

COMMISSIONER LINDWALL: Well, I think that - - -

COMMISSIONER KING: But even the equivalent for an airport like Sydney, which the documents, the analysis provided to the NCC, an updated version of that would be invaluable to us.

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COMMISSIONER LINDWALL: I mean, even if it was provided to us on a confidential basis for us to make an assessment, with the understanding that the actual figures was not published.

COMMISSIONER KING: Along the lines of the NCC submission.

COMMISSIONER LINDWALL: Yes. Anyway, could we leave you to reflect on that, and I think we've got no more questions. So we appreciate your time today, Rohan and Philip. Thank you very much.

MR DANGERFIELD: No, thank you.

MR SKINNER: Thank you.

COMMISSIONER KING: Thanks.

COMMISSIONER LINDWALL: Have a good afternoon.

COMMISSIONER LINDWALL: All right. Well, that's the last of the formal ones. Does anyone else want to have a say now? You're most welcome to. Anyone?

COMMISSIONER KING: No.

COMMISSIONER LINDWALL: No.

MR SCOFIELD: Just with the class - - -

COMMISSIONER LINDWALL: Sorry. Yes. Formally, you have to come up and – so that it can be on the transcript.

COMMISSIONER KING: And then you've got to give your name and say what you want. It can be 30 seconds, a minute, doesn't matter. Whatever you want to say.

MR SCOFIELD: So, Ben Scofield from Freight Victoria. So I was just thinking, with that last – those last comments about Caltex, one would assume there is some formula, though, by which they calculate any profits that they're about to achieve.

I mean, you know, you're going to get differential rates for ports and airports, and whatever. But there must be some basis on which they can calculate their own pricing.

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COMMISSIONER LINDWALL: Yes. Okay. No, that's a good point.

COMMISSIONER KING: Yes.

COMMISSIONER LINDWALL: Anyone else? All right. Well, thank you very much. I think we'll adjourn these hearings. They will resume next year at a time to be specified, when they will be general hearings about every aspect of this enquiry, and we thank you all for being here, and good bye.

MR SCOFIELD: Thank you.

COMMISSIONER LINDWALL: And Happy Christmas.

COMMISSIONER KING: Indeed.

MATTER ADJOURNED AT 2.54 PM

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Australian Government
Productivity Commission

PRODUCTIVITY COMMISSION

ECONOMIC REGULATION OF AIRPORTS

MR P LINDWALL, Commissioner
DR S KING, Commissioner

TRANSCRIPT OF PROCEEDINGS

AT HOTEL REALM, CANBERRA
ON MONDAY, 25 MARCH 2019 AT 9:30 AM

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COMMISSIONER LINDWALL: Hello, everyone, we may as well get started because there's a bit of introductory stuff that I have to tell you about, including getting evacuated or something like that. So hopefully that won't happen. It happened in one of the hearings that I've had once when we had to be evacuated which was a bit unfortunate.

Good morning and welcome to the public hearings for the Productivity Commission, the inquiry into the regulation of airports. I'm Paul Lindwall, the presiding Commissioner and Stephen King here is my fellow commissioner on the inquiry.

We'd like to acknowledge the traditional custodians of the land, the Ngunnawal people. The inquiry started with a reference from the Australian Government in June 2018. The purpose of the inquiry is to investigate whether the economic regulation of airport services promotes the efficient operation of airports and related industries. We released an issues paper in July 2018 and have talked to a range of organisations and individuals with an interest in the economic regulation of airports. This has included representatives from the Australian state and territory governments, airports, airlines, industry representation, representative bodies, academics, researchers and individuals, pretty much everyone in other words, with an interest in the issues throughout the inquiry.

We have held focussed public hearings on competition in the market for jet fuel in Sydney and Melbourne in late November 2018. Following the release of the draft report in February 2019, the Commission called for further submissions and is undertaking consultations along with those public or these public hearings. We have received 88 submissions prior to the release of this draft report and 13 since the release of the draft report, noting that the closing date is today, but we still expect to receive further submissions and if people have knowledge of the PC and know that we're flexible in the receipt of submissions right up until last day actually, but after we give the report to the government it's very hard to take notice, too much notice of a submission I find anyway.

We are grateful to all the individuals and organisations that have taken the time to prepare submissions and to appear at these hearings. This is the first public hearing for the inquiry. Following today, hearings will also be held in Sydney and Melbourne. We will then be working towards completing the final report having considered all of the evidence presented at these hearings and in submissions, as well as other informal discussions. The final report will be submitted to the Australian Government in June. Participants and those who have registered their interest in the inquiry will be advised of the final report's release by

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government which may be up to 25 parliamentary sitting days after completion.

The purpose of these hearings is to provide an opportunity for interested parties to provide comments and feedback on the draft report and facilitate public scrutiny of the commission's work. We like to conduct all hearings in a reasonably informal manner, but I remind the participants that a full transcript is being taken. For this reason, comments from the floor cannot be taken, but at the end of the day's proceedings I'll provide an opportunity for anyone who wishes to do so to make a presentation.

Participants are not required to take an oath but are required under the Productivity Commission Act to be truthful in their remarks. They are welcome to comment on the issues raised in other submissions or by other participants at the hearings. The transcript will be made available to participants and on our website following the hearings and they are also, well, for any media representatives attending today, some general rules apply. Please see one of our staff at the back there. We've got Catie and Natalie there who can give you a handout which explains the rules.

To comply with the requirements of the Commonwealth Occupational Health & Safety Legislation, we are advised that in the unlikely event of an emergency requiring the evacuation of the building please listen for instructions over the emergency warning system. There are two types of tones which may be used, the alert tone followed by the evacuation tone. In the case of evacuation tone, please evacuate directly and quickly to the assembly area through the emergency exit as directed by the emergency wardens which are basically down the stairs and out that way. The National Press car park is the assembly point.

If you believe you're unable to walk down the stairs, it's important that you advise the wardens who will make alternative arrangements for you. You are invited to make some brief opening or some opening remarks and keeping them brief and asked not to discuss the matters in greater detail. I would now like to welcome Dr Harry Bush, an independent regulatory and former board member for Economic Regulation, United Kingdom Civil Aviation Authority. Welcome. Do you mind if I call you Harry?

DR BUSH: No, do, please.

COMMISSIONER LINDWALL: We're Stephen and Paul.

DR BUSH: Please. Hi.

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COMMISSIONER LINDWALL: We like to be fairly informal. So could you, just for the transcript, could you identify your name and position and representation here.

DR BUSH: Yes, so Harry Bush. I was a regulator, the economic regulator at the UK CAA for something like eight years. Prior to that I was at the UK Treasury. Since leaving the CAA in about 2010 I've been on the board of our air traffic control provider in the UK as a non-executive director and that's a regulated entity. I am also on the board of a major teaching hospital, which is again a regulated entity and I've been an independent adviser on regulation and related matters to companies, governments and other bodies.

COMMISSIONER LINDWALL: Okay. Harry, thank you very much for your comments and submission, but do you want to make any introductory comments?

DR BUSH: Yes, I thought I'd just make a few. Well, thank you very much for taking the time to see me.

COMMISSIONER LINDWALL: Pleasure.

DR BUSH: I have to say, a lot of my friends in the UK are envious that I've managed to get as far as it is physically possible away from the Brexit chaos that has descended the United Kingdom.

COMMISSIONER LINDWALL: Yes.

DR BUSH: As I've mentioned, my background really is a regulatory practitioner rather than a regulatory theorist, and I've been over the years, (because it's been very relevant to what we've been doing in the UK) following at least at a high level some of the things that have been going on in Australia. Prior to the last commission review I had a chance to talk to some of the commissioners before that was all launched.

I think the paper I put in is pretty self-evident, pretty self-explanatory, but I thought it useful to set out just two pieces of context (and the question is how much of this you draw out as relevant to Australia) that have informed the way I've thought about these issues. One of these is what I would call the shift in the balance of power between airports and airlines over the last, say, 20 years. This is very striking in Europe as a whole because you've got the growth, at the expense of legacy airlines, of point to point business models. You have very mobile entities able to fly between any two points on the Continent, which can change their plans at relatively short notice and can choose which points. They don't have to

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serve anywhere, unlike a lot of legacy airlines in Europe which while not confined to their hub, mainly serve their hubs. The point to point airlines are very, very flexible.

And they have placed airports very much in competition with one another, but their countervailing power, if you delve below, comes not just from their ability to do that, but from some basic facts of their businesses and their scale- the fact that they have mobile assets versus the fixed and sunk assets of airports; the sheer scale of some of the major point to point carriers, I think Ryanair and easyJet particularly, but not just them, and the fact that this is a growing segment of the market, the point to point, which makes it very difficult for an airport to grow its business without bringing them in, which gives them a certain amount of power.

Because they're negotiating all the time with airports, they're able to bring a professionalism to their negotiating approach, they're dealing with scores of airports on an annual basis; and of course they have a public voice and the influence that brings. So their countervailing part comes from that and a number of other features.

And I would say that in Europe, and to a lesser extent the UK, regulation hasn't kept up - airport regulation hasn't necessarily kept up with these developments; better in the UK but even there responses have been belated. My view was that Stansted Airport, the third London airport, should have been deregulated when it was first proposed in around 2008/9. Eventually it came around 2015. Europe's been much slower. Partly it's been struggling with the concept of how to undertake market power tests. Partly, I think, it has been struggling with how to treat the voices it hears as evidence or not evidence, complaints versus evidence you might say.

There's also sort of tradition in Europe, I think, of treating regulation as almost as equidistance between the two parties, so if you reach somewhere in the middle, that sounds like a good place to be. The resulting problem: "Are you really conforming to the underlying economics?". There is a failure, I think, to grapple with some of the conceptual issues which feature in the Commission's report; the concept of scarcity versus the exercise of market power, the fact that airlines can discipline airports by making changes at the margin (you don't have to shift all your business from an airport to exercise a very considerable amount of influence). One plane taken out, you know, with all the passengers and the associated retail revenues and the fact that costs remain behind from the airport's point of view is a very powerful trigger.

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I also think we are only now getting to grips with the fact that the ultimate aim of airport regulation should be the passenger. Elsewhere than in the UK you're talking about, balancing commercial interests; one party against another. Interestingly in the UK, up to about 2012 that was where we were because the Airports Act 1986 said that we had a duty towards both airlines and passengers or airlines and their end users. It became much clearer in 2012 that the duty was to the passengers so you should see through the airline, and I think we've better in the UK at doing that.

So that's one set of things and I think the second - I'll be very brief - is the growing generalisation, if you like, of capacity pressures in the system. So we've had, in the UK Heathrow and Gatwick extremely full and that's been true for years for a number of policy reasons. Heathrow's very much an outlier in terms of the scarcity of capacity and the impact that that has had, but Europe is moving in the same direction, as indicated by various publications, Heathrow shows the extent to which if you don't get investment in time (and the reason we haven't done it there is because of government decision making), there is very significant detriment to passengers.

People who are dealing with airport regulation have got to realise that relatively small changes at the margin to airport charges can be swamped by much bigger decisions that are or aren't made on making sure that capacity is available, so that scarcity does not develop in the way it has in the UK. So I say that one of the consequences of this is that regulators should focus, not on building before time or anything like that, but actually making sure that capacity does come onstream as soon as policymakers allow it to.

So that needs to be recognised as a priority, and I think regulatory frameworks need to be supportive of timely investments. They need to look beyond the immediate commercial interests of the commercial parties involved because quite often airlines will be adversely affected by putting on capacity; they will of course obtain some capacity to run extra business but they will have extra competition from other airlines and they will also have a decline in scarcity rents that have built up. And so the real focus from regulators must be on the passenger and societal interests in ensuring that you've got an efficient, functioning airport sector.

COMMISSIONER LINDWALL: Thank you very much, Harry. I might ask a few questions and then get Stephen to ask some too. But along your lines about how the relationship between airports and airlines has changed over a number of years, how would you think Australia should be viewed given that we are quite different geographically with large population centres well apart from each other?

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DR BUSH: Yes. So you won't have the same degree of airport competition and I think that's reflected in the findings of the Commission. In the UK we've got two regulated airports with market power, one at - not classically regulated in terms of a classic cost based system, and you've got four despite a smaller economy. So I think that airport competition is not there in Australia to the same extent as in the UK. There may well be, at the margin, the ability of overseas airlines to decide between different airports as to where they put their capacity because they don't necessarily have to serve particular locations in Australia. They are internationally focused, and can make a that decision on how much product that they're offering in Australia. So at the margin I think there's competition there.

But some of the broader points I was making about countervailing power I think do apply - the scale of airlines, the degree of professionalism they can bring from negotiating multiple times with airports. I think those points do apply and of course, who knows, as time goes on you may well find there are more competitive pressures build up. But it's a very different geographical space and I'm not saying that, except to the margin, some of these factors apply, and they would also apply very differently.

COMMISSIONER LINDWALL: No, fair enough, yes. Now, I think you've noted in here comments about our building block methodology that's been used in negotiations between airports and airlines and also that we use individualised contracts, air services agreements, and you've said that it's a bit surprising to use building block methodology. Who do you think drives the use of that or does the mere existence of using a building block methodology comprise some level of countervailing power, do you think?

DR BUSH: I think the reason I was surprised was because you've had the system for 20 years or so, getting on, and the potential for individual airline contracting has been there that amount of time. Now, clearly the origins of it were in a more regulated system where you would have had the building block methodology. I was contrasting a little bit with where Gatwick is trying to get to.

So Gatwick has been given what you might call "some precautionary regulatory arrangements" and then it is able underneath those to negotiate individual contracts with airlines which it has been doing pretty successfully. It doesn't any longer publish a regulated asset base figure. So its trying to divorce itself from that old building block methodology, and actually has made quite a lot of progress in actually talking to the airlines about price and service. Airlines are able to make the comparisons with what they get elsewhere. They are able to say, "Does that represent good

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value?" and at the margin they say, "Well, if it doesn't maybe I can take my flight somewhere else?"

But I was a bit surprised that the building block approach still existed to the extent it appears to here, and I just wonder whether it doesn't set up tensions between airports and airlines in an unhelpful way because at every point it means that airlines are trying to second guess the cost of the airport including the sort of completely zero sum game of the WACC which always gets a lot of focus whereas if airlines were focusing much more on the service they were getting, and I thought there was some stuff in the BARA submission which I thought was quite interesting in that area, and were trying to move things towards that and where there would be a lot of discussion about, "Is the service right?" This is what's happened at Gatwick - "Is the service right?", Is the on time performance right?", "What can be done to improve it?", rather than, you know, "Could you knock ten per cent off this because we think you could get the terminal built much cheaper or this bit of the terminal cheaper?" and get your WACC down and all of that, which I think just leads into the sort of old-fashioned regulatory dispute despite not having the old-fashioned regulatory framework. This just strikes me as odd.

COMMISSIONER LINDWALL: That's very good. In your comments you've also said about the constructive engagement used in the UK and you alluded to it there where that perhaps the Commission or some other body might think about a different way to provide guidance to negotiations between airports and airlines. On the other hand you've also said that there are problems with regulators trying to put conditions in which often become embedded in the expectations of both the airline and the airport so where do you draw a line between a boilerplate provision, if you like, becoming effectively a de facto regulation?

DR BUSH: Yes. So what I think I was trying to do in those points was say what I think is essential "not" to do – that is to become too prescriptive, particularly where you're dealing with, as you are here, with individual contracts between individual airlines and individual airports. They will be taking place at different times, there will be different circumstances. What's important for one airline won't necessarily be important for another so there's a whole range of things that would need to be taken into account.

Whereas when you're dealing with a more traditional regulatory arrangement, where you've got CapEx and OpEx and all the building block stuff, having properly clarified information requirements, timetables, procedures, can be extremely helpful to build trust. I just wondered, and this was more a question really, is whether it would be

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possible at least to provide an umbrella for the parties themselves to get together to try and see whether there was common understandings that they could come to at least as a starting point for discussions.

For instance just trying to move from focusing so much on building block type methodologies - is there some way in which they could shift more towards service and a service level agreement type of methodology which it seems to me would be helpful. I thought the thing about having these boilerplate clauses, standard clauses, where there were common features that struck me as time-saving, I think what one was trying to say is maybe there are frictions here which contribute to some of the ill feeling that always comes out in these sorts of processes that could be reduced.

COMMISSIONER LINDWALL: All right.

COMMISSIONER KING: Can I just follow up on that?

COMMISSIONER LINDWALL: Yes, yes.

COMMISSIONER KING: When reading the sort of proposal that AAA and BARA put forward - - -

DR BUSH: Sorry, that?

COMMISSIONER KING: I come from a competition economics background so I guess my immediate thought is it would be a fantastic collusive device so is there a risk of collusion? Certainly you move to standard boilerplate clauses but at the same time they can become standard clauses that all the airlines have in their contracts and it could reduce airline competition.

DR BUSH: Well, it depends which they are doesn't it. If they are standard things around how airports operate, I guess these agreements have lots and lots of different elements in them but I'm not talking about, you know, for instance standardising things around SLAs, those should be individual and that's where the discussion should be. It's just there may be some elements which involve them all going away to their lawyers, they all turn up, they all end up broadly in the same place but in the process they've wasted a lot of money, time and effort. The question would be in my mind is whether by having that all sorted you actually can get to a better place on the stuff that really does affect competition between airlines and the service that airports provide. That's where I was going. There's a risk but I don't think it's a great risk if it's defined properly.

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COMMISSIONER LINDWALL: Some of the participants to this inquiry have suggested that we need a negotiate-arbitrate framework which would involve a compulsory arbitration process. That would presumably be still based upon (indistinct) a building block methodology because I can't see how it would work otherwise but would you say that there would be - well, if you understand the proposal, how would you explain its benefits and costs if you like?

DR BUSH: So I include some comments on this in my paper. I mean, at one level it seems perfectly intuitive. Here are two parties, why not have an arbitration if they disagree. The problem that you run into, and which we run into whenever we try to liberalise arrangements within a regulated framework, is that it's difficult to get the regulator out of the room - and by "regulator" in this context I mean "arbitrator" as well, if that's the ultimate authority. Because the parties will be looking towards what the arbitrator will do, that becomes almost more important.

So you find this in negotiations, whether it's within constructive engagement or where Gatwick was allowed to go off and conduct individualised negotiations with airlines, until the regulator very firmly got out and wasn't hanging about and instead says, you know, here is the framework, I'm out of it and I'm no" going to come and arbitrate between you, the issues are for you to deal with commercially. You've got the safeguard arrangement but underneath that you get on with it. Until that was absolutely clear it was very difficult to get these negotiations going properly and I think that's inevitable because if you've got somebody out there who's going to make the ultimate decision parties are concerned with what are they going to say if it goes to them and that conditions then the sort of discussions they have.

And so I think that's the real risk with embedding arbitration as a clear and constant feature of these arrangements. Of course if you'd found, you know, that market power was being exercised the balance of argument might shift but I think where you haven't found that and what you're trying to do is encourage these commercial arrangements between airports and airlines as a good way of getting decent outcomes, then I think there is a real possibility of negotiate-arbitrate undermining the thrust and dynamic of that.

COMMISSIONER KING: Sorry, could I just follow up on what you were saying there. Because you said earlier in your comments about the importance of, you know, looking through to the consumer and one of the questions I have about any arbitration proposal between an airline and an airport or airlines and airports, is that who represents a consumer? How does a consumer fit into there? And I was wondering your views on that.

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DR BUSH: This is why it starts to take on the attributes of regulation because I think for exactly that reason you'd have to start saying, "Well, what is the job of the arbitrator here?" and the job of the arbitrator to some extent would be to take into account passengers, and as your report indicates it would also have to take account of the interests of other airlines not just the ones that have initiated the arbitration. It would have to take account of maybe different timeframes because what might be right for that an airline now may not be right for all airlines at a later stage and consideration needs to be given now to that later stage.

So by the time you finish it's actually quite difficult in an interconnected system like an airport to actually confine the particular dispute and the particular problem, we're now actually broadening it out to include a whole set of other parties and considerations. I think that's one really difficult point here.

COMMISSIONER LINDWALL: If you were to look at negotiate-arbitrate and what it would likely lead to in terms of investment, would you be able to say that it's - would it lead to less or more investment and if so could you be definitive about that do you think?

DR BUSH: No, I don't. I would find it quite difficult to be definitive about whether it would lead to more or less. I can see that where there are going to be big disputes, they are likely to be around the point where airports are introducing new facilities and those are going to be putting charges up and therefore to the extent that, you know, you provide a route whereby that can almost as a matter of routine be challenged, I think that might tend to delay and make it more difficult to invest but I'm not sure I'd be utterly definitive and I don't know what the scale of the impact would be.

COMMISSIONER LINDWALL: But to the extent that it did reduce investment, would that be relevant to your comments earlier about congestion and leading to - - -

DR BUSH: Yes. I don't know precisely where you stand in relation to congestion across the Australian airports, but you know, it's clear, I think, both in the UK, and Europe, and quite a lot of other countries, I mean India is another example, where there's a need for huge amounts capacity as it's growing so quickly, even the airports that were recently built, and now need to be expanded, very dramatically, that you have got to have systems and processes and approaches here, which enable decision on investment to be taken relatively speedily where they can be, because there are public constraints. But where those are overcome, or can be set

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aside, then I think the economic regulation should enable those decisions to be taken speedily, because even a couple of years delay, when you've got real capacity constraints, represents a big loss. Those years are now.

COMMISSIONER LINDWALL: So, if that evidence, you cited from frontier economics at Heathrow, led to the congestion, if I'm not mistaken, led to - well, rents, I suppose, to airlines, is that how you'd - - -

DR BUSH: Well, yes. So, I mean, as part of the airports commission works - so, let me go back a stage. There had always been a vague discussion about the existence of scarcity rents in the London system, because, of course, there are very high slot values demonstrated by slot trading at Heathrow, and some extent at Gatwick.

COMMISSIONER LINDWALL: Yes.

DR BUSH: And the result is you have very high slot values, which actually represents scarcity rent, because you wouldn't have them without such scarcity. So, that there is a clear relationship there. So rents were there, often denied, interestingly, at the same time as the money changed hands. But, what the airports commission framework provided (this was the investigation of where the third runway - or second runway in Gatwick's case - should be) was work which sought to quantify what those were, because actually, getting rid of those rents, or reducing them was actually part of the cost benefit appraisal, so you need to have some degree of quantification. I haven't got precise figures to mind, but they are very large, and of course, as the scarcity increases, over the period until the new runway, comes on they are getting larger, and at an increasing rate. So, you know there are very few places quite in that category, but you can see certain airports in Europe starting to get there.

COMMISSIONER KING: Okay.

COMMISSIONER LINDWALL: Can I just ask - yes.

COMMISSIONER KING: To follow up, you mentioned the importance - - -

DR BUSH: Actually, you know, when we talk about scarcity rents, it sounds, you know, rather theoretical, but let me be clear. That's a cost borne by passengers, and then a - in a building block, methodology type of approach, such as in the classic regulation at Heathrow, or where charges are set informally on that basis, those rents go to airlines.

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COMMISSIONER KING: So, in your introductory comments, you also mentioned the importance of capacity investment. And one way you discussed in your short report to us is we've got pre-financing by the airlines.

DR BUSH: Yes.

COMMISSIONER KING: I guess, two things: from someone who's an outsider to airports, pre-financing looks slightly odd. I'm used to things like take or pay contracts in areas such as energy, but pre-financing does strike me as being a slightly unusual way of financing. So, I'd like your view on that. And secondly, what alternatives have you seen overseas, for example, in Europe?

DR BUSH: So, actually, I think it's the other way round. I think not having pre-financing is odd. Where you have a building block methodology, which takes the costs that you are incurring in the airport today, and comes up with a price, part of those costs today will be the work you are doing to open a new terminal, or whatever it may be. So, those are costs which are being incurred today, to produce the new facilities tomorrow. So, it seems to me odd to exclude them.

Now, if you've got a different sort of economic regulation, where it's looser in some way or other, or where you have a price path, which takes account of the fact of scarcity and the need to invest for the future, some sort of long-run, incremental cost type of path, you wouldn't need pre-financing - the whole subject wouldn't arise. The subject only arises because you have these very tight, cost-based systems. And at that point, airports are not throwing off, inevitably, the cash to help them finance new investment. And I think the other angle, particularly for larger items, is that if you don't watch out, the way in which the building block type of methodology works is that you end up with low prices now, and magnifying the pricing increase when it comes on later.

Which is not how a market would work. The market would allow at least some of the scarcity rents to go to the airport. I mean if regulators weren't interfering. Let's assume that there isn't classic market power, but there's, you know, scarcity. The airport would, to greater or lesser extent, take some of that rent, and at that point we wouldn't be talking about pre-financing, because they'd be throwing off the cash from the scarcity rents, that would enable them to finance new investment.

It's because you hold the prices to - so closely to cost, that this problem arises. So when airlines say, "Oh, but this doesn't happen elsewhere, because you only ever, when you're in a normal market, you only ever pay

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when a facility opens, or a new product comes on stream". But the whole point of a normal market is price isn't held that closely to cost in every single year.

COMMISSIONER KING: The airlines, I suspect, would respond by saying that the pre-financing puts an odd risk on that, so airlines today who may not be using the new runway, let's say, when it comes on stream in five years' time, are actually paying for it, rather than the parties who use it. Any comments on that?

DR BUSH: Yes. They have a point, as a factual point, that will be right. But actually, you know, the point about an airport is it's got some facilities that have been there for 50 years, some that have been there for 30, some for 20, some for 10, and then there are others that will be there in the future. And actually, just to isolate that one particular investment is odd. Those airlines who are there today,\ may not have been there yesterday, so they are benefiting from investments that have been made in the past.

And so, just segmenting this particular investment seems to me conceptually wrong. I think that needs to be looked across the whole airport. There are inevitably some rough and ready approximations across the life of the airport, and this is one of them. You're not asking them to bear the whole cost, you're asking them to bear some of the cost in pre-financing, and what you're asking them to do is bear the cost, where if it's a very big change in capacity, they are getting - already getting the benefit from scarcity - any scarcity rents that are generated. It also produces much better price paths and signals. I mean, this is the other thing.

So, if you take the Heathrow example, again, which is classic, and at the extreme. But before T5, terminal 5 came on (that was a - essentially, a replacement piece of investment; it wasn't actually expanding very much, the overall capacity). Before T5 came on, you know, the natural forces of depreciation running through, were pushing prices all the way down, so that by the time you come to the new terminal, you've got a big problem in terms of price increase.

So pre-financing, enables you to smooth that somewhat, as well, and start sending signals to airlines that costs are going to be rising, providing also more credible regulatory price paths, because it's very difficult to introduce very big increases. And it is far better to smooth them over time, both for the airport, but also I think for airlines making decisions about, really, where they want to base themselves.

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COMMISSIONER LINDWALL: Just on the - just the last one on this. Other examples that you've seen. I mean, is pre-financing used, for example, for more regulated airports in Europe, or how do they - - -

DR BUSH: They are - it varies. Some use it, some don't, and I suspect it's salience is going to grow as the capacity issue grows. So, you know, it comes down to national regulation, some - some are using it.

COMMISSIONER LINDWALL: So, scarcity rents, which of course could be split between airlines and airports, although the evidence is we mostly go to airlines - - -

DR BUSH: They go to airlines where you set the price according to cost rather than, as it were, market forces.

COMMISSIONER LINDWALL: But to the extent that scarcity rents also went to airports, they don't have an incentive to delay investment to keep some of that rent?

DR BUSH: There are a lot of pressures on airports to expand. I mean, they've got several income streams. They've got their retail, their car parking, their other income streams, which are actually pushing them towards expanding an airport.

COMMISSIONER KING: Yes.

DR BUSH: So I think they've got some very powerful forces offsetting your concern. Plus if you sit there and your airport is very full and passengers' experience is deteriorating, you have got a lot of public and political pressure to grow it and to deal with those problems. Certainly that's been the experience in the UK, where airports generally stay below the public horizon, except where things get really bad. And when they get really bad, you're in the press.

Of course, at that point it's very difficult to do anything quickly because you are years behind the game. So I think a sensible airport which is interested in what you might call its licence to operate within a community or within a society will need to balance the issue you're talking about here, against the need to ensure that passengers and others aren't overly inconvenienced.

COMMISSIONER KING: Can I push back a little bit against that.

DR BUSH: Yes.

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COMMISSIONER KING: By saying that while the airport may have some incentives, it's going to be balancing up the scarcity rents versus the political pressure. Wouldn't a more firmly regulated regime result in more investment? Because then the regulator can require the investment to come on stream earlier. Given that there is more regulation in Europe, is that the case or is it the opposite or what line?

DR BUSH: Well, I mean, I sort of contrast if you like the regulated sector in the UK and the unregulated. Most of the airports have never been regulated in a classic sense, they're smaller. We never really have complaints or difficulties about those airports having insufficient capacity – they build little bits here and there, they build capacity as they need it.

Manchester now deregulated has just been building a large amount of new capacity both to replace some of its existing old capacity but also to expand. So those unregulated airports don't seem to have a problem. The problems we've had have been in the regulated sector. Now, I'm not saying that those problems were due to regulation, but regulation didn't necessarily overcome the problems, and the airports were pressing for new investment. They couldn't get there, partly because of public policy issues.

The regulatory frameworks themselves can involve delay. You tend to have five-yearly investigations of cost and price. So your investment programs tend to have to be lined up in order to meet those deadlines. They will then require a lot of detailed invigilation and examination by the regulator across several years. So you're adding, in addition to the sort of discussions you would have had with your airlines, you're adding a lot of process and some delay into the pot.

COMMISSIONER LINDWALL: I'm conscious of time, so I wonder if – unless you've got some other questions on those themes - - -

COMMISSIONER KING: No, no.

COMMISSIONER LINDWALL: - - - we could touch on some jet fuel and noise issues.

DR BUSH: I think you're not going to find me very helpful on those, but anyway.

COMMISSIONER LINDWALL: I mean, you were at the National Air Traffic Control Services, as you said, and you have different approaches to handling of aircraft noise in, say, Heathrow, because obviously Sydney Airport's a critical area here in our inquiry.

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DR BUSH: So the noise issue is a big issue around the third runway at Heathrow; it's requiring a great deal of public consultation. But in addition to that we are having to – and I come to this through my place on the board of our air traffic control system –change the air space in the UK because it is running out of capacity. So capacity issues don't just apply on the ground (one of the things people forget when they build new infrastructure) but even without building new infrastructure the airways themselves can become very constraining.

That is involving us in – the airports are often in the lead for the lower level of airspace where the noise problem arises. But we are becoming more proactive in trying to join with the airports in explaining to people what's going on. In general, this modernisation should lead overall to less noise, but often to a shift in noise. And this is one of the big problems you run into, that you may be shifting noise around as you modernise airspace, or you may be concentrating noise, because modern equipment enables you to fly much more directly, and therefore something that was diffused by accident becomes concentrated by design.

So that's where you run into difficulty. All I can say is we have had problems in introducing these changes and some delays have been imposed because of problems with consultation. So I think what we have found is we have to have a very, very well set down consultation process. Because if you don't have that, you find at the end you're in court and the whole thing goes back to the start.

So one of the things that's come out of the recent experiences is some new CAA processes which mean that a lot more work is done up front in terms of explaining to the people affected, and I think that is the key thing, is to get everything out on the table right up front and ensure that everybody's aware, you've consulted fully, everyone's aware of the impact of the various choices that can be made and what the consequences are, and that you then lead on to a full process and the decision-making that's based on that.

I think it sounds obvious, but actually we didn't do it properly to start with. So it just shows you it can go wrong.

COMMISSIONER LINDWALL: On jet fuel, I don't know if there's anything to say. I mean, in Australia of course at our major airports we have joint ventures which are usually fuel providers providing the infrastructure and servicing the uploading of Jet A-1 to the planes. Is there anything you can comment there about the competition, say, in the UK?

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DR BUSH: I don't think so. I don't think this subject's emerged while I was in situ.

COMMISSIONER LINDWALL: No, that's all right.

DR BUSH: It doesn't seem to, and just in recent regulatory documents and proceedings I don't – I haven't come across it.

COMMISSIONER LINDWALL: No, that's okay. There are other questions I could ask, but we're running out of time. Did you have anything?

COMMISSIONER KING: No, I didn't.

COMMISSIONER LINDWALL: Any final points, Harry, that you - - -

DR BUSH: No, thank you very much.

COMMISSIONER LINDWALL: Thank you very much for coming and seeing us.

DR BUSH: Thank you.

COMMISSIONER LINDWALL: Well, I think we're now hearing from Geoff Breust from the Regional Airports Users' Action Group. Geoff, hello.

MR BREUST: Good morning.

COMMISSIONER LINDWALL: Morning. So, Geoff, if you wouldn't mind just saying your name and organisation and then if you'd like to give some introductory comments, that would be perfect.

MR BREUST: Yes, that would be great, thanks. Thanks very much.

COMMISSIONER KING: We're obviously taking as much time to stretch as we possibly can.

MR BREUST: Do you want a 10 minute break?

COMMISSIONER KING: No, a break comes after you, so it's all right. We're following a schedule here, so it's all right. We know from past experience that a few days of these hearings you tend to find you sit a bit too much.

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MR BREUST: Well, thank you very much for giving us the opportunity to come along and talk to you.

COMMISSIONER LINDWALL: Pleasure.

MR BREUST: My name is Geoff Breust, I'm convenor of the Regional Airports Users' Action Group, which is a very fancy name for a Facebook page basically. I'm the convenor of that, and I think we've got about 400 members, but basically that page is just simply to allow people to post comments and discuss some of the issues.

My personal background – and I actually submit in the context also as an individual as well. My background is very much regional aviation, I was general manager and CEO of Kendell Airlines back years ago, and you remember the days when Kendell used to fly in and out of Canberra to Sydney.

COMMISSIONER LINDWALL: Yes, I used them several times.

MR BREUST: And then more recently I was managing director and CEO of Regional Express and I retired from there a few years ago. I'm currently just a general aviation pilot and aircraft owner and so forth, but I still retain a very strong interest particularly in regional aviation, and on that basis could see a number of the issues and was really pleased that this time the Commission was given a reference to look at the regional airports as well, because the whole thing is really tied together, and it gave us an opportunity to make some comments to you.

Just in terms of opening, and I'll just run through it, but we did provide at the end of last week a further submission to the Commission.

COMMISSIONER KING: Thank you, yes.

MR BREUST: But I think I'll just very briefly just run through. I've always had a very positive view of the Productivity Commission, because I always believe that you look at things rationally and look at it from an economic point of view. But I must admit, I was a little disappointed with this draft report, I thought it was a little too academic. I was really hoping that there would have been some more robust investigation and sort of forensic look at some of the real issues, and particularly the areas of disputes between the airlines and the airports.

I think when you get into that you really start to understand really where the market power lies. I'm really not in a position to be able to comment about the Kendell and Rex days because I'm not involved with those

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organisations now, but I did have during those periods some fairly significant negotiations, particularly with Sydney airport, but also with Canberra, Melbourne and Adelaide and so on.

Those arrangements were difficult, they took up a lot of the time with the airline, and we believe very much that, from where we stood, that the level of power definitely remained with the airport. So I was a little disappointed, particularly in the main finding, that on balance the Commission was satisfied that the airports have not systematically exercised their market power in commercial negotiations with airlines to the detriment of the community.

The reason in saying that I don't really believe that's a great finding is that I look at things fairly simply and I just don't believe it passes the pub test, and I don't believe it passes the pub test because – for a number of reasons, there are six in particular that we put in. That airport profitability is high and continues to grow year on year and it's well above the inflation rates. It's certainly better than many other industries.

The dividend returns to airport shareholders are increasing at very high rates; I think their shareholders should be particularly happy. The average revenue per passenger is increasing, but at the same time total passengers over the year are increasing and increasing at quite high rates. The airports' return on aeronautical assets, particularly for the major airports, continue to be around 10 per cent or above. I note that Sydney airport's ROA was in the order of 14 per cent for some years.

Now, that's very, very high, given the long-term nature of the assets that are involved there. I think as a general rule in business if you're looking at long-term assets, a rate of return of around 5 percent or even a little less is probably more closer to the mark. So we raise that as an issue.

There's obviously been conflict between the airports and the airlines and there's been some very notable exercises in relation to that. I also come back to the continued comment by the ACCC that the light-handed approach is not enough to constrain the market power. So on that basis, I was disappointed that it was same, old same old in the sense that we continue on the same way, and I thought we would end up with something a little different.

But having said that, really very, very pleased that regional airports got the coverage that it did in the report and the consideration. Whilst I was a little disappointed that you didn't recommend a national airport infrastructure fund, which we'd put in our submission, we understand that there might be some limitations in relation to that from your terms of reference.

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But the issue that a lot of the regional airports have is just simply funding the infrastructure. They all rely very, very heavily on Government grants, and a lot of the Government grants are very hit and miss. Success can depend on a whole range of issues, that I'm sure you're aware, but politically in particular.

Having said that, I was really pleased with recommendation 10.6 because we believe that it heads in the right direction, particularly the inclusion of considerations on a regional level rather than just simply the local government area. Because even at local government level, there is a lot of political interference and we thought taking into account the sort of broader regional level issues was a good approach.

The independent evaluation at the end of or as part of the funding process, we also believe is extremely important and a good part of that recommendation. Most airport infrastructure projects funded by grants are just built and then there's no evaluation after the event. There have been quite a few infrastructure projects which have turned into semi-white elephants.

Your recommendation 10.7, which draws on the Western Australian approach to arrangements in that state, I think again is very, very good and we'd certainly support it. The only issue we believe that you would have is getting the Governments and all the parties to support it all, and I think that's going to be a chore. But I think the approach is heading in the right direction.

I'm involved – or I have been over the years involved in a number of airport advisory committees, and in particular I'm on the current one that's established for the Wagga airport, which is where I come from. That's been going for almost two years now, it is a difficult process, particularly getting to the actual level of costs that are involved with the airport. I note in the draft report that there is a table there of the various regional airports in particular and their costs and revenues and their underlying profits.

I take a lot of that with a grain of salt, because I know that in many cases a lot of the cost numbers are just simply aggregated and then somebody makes a decision to allocate, so there's no true costs involved. I'm actually trying to go through that process with our friends at Wagga at the moment and I must admit I'm getting a bit of push back, but I continue to go down that track.

The other area of the report that we're a little disappointed about – not so much disappointed but concerned the issue was not highlighted and that is

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the cost of security, Security costs and related issues are a major problem for regional airports. In particular at the moment new and increased security requirements are being imposed on many of the regional airports, – effectively taking the size of the aircraft to which the improved security requirements down.

So previously QantasLink, for argument's sake, operate a Dash 8 300 series, which is a 50-seater. They've moved generally to the 70-seater version but they have a number of 50-seaters. Rex in particular operate the 34 seat SAAB 340. Rex is not subject to the security requirements and they will not be under the new arrangements, but the 50 seat Dash 8 will be. And that's going to impose a lot of issues at competitive airports. I know that the QantasLink people are pushing for overall screening, so in other words both Rex and QantasLink would have to be screened.

I think there are some practical issues in that, but again, it's a cost impost on an operator that really doesn't have to comply. So when you move things on the margin like that, those sorts of implications come into effect.

But I think the biggest gripe that we would have at this point with the new security requirements is that whilst the Federal Government has indicated that they will pick up the capital cost of the equipment, there are major issues with getting that equipment and the new process into current terminal facilities. The Federal Government is now saying that funding will not be available for any building works for this purpose..

Now, even in Wagga's case, to actually establish those new security requirements will involve quite a substantial change to the terminal and that's going to be very, very costly. So effectively they're pushing that back onto either local government or through local government onto the airlines and the passengers.

So we think that there is a need for the Government to reconsider that, particularly in the funding area and take some of that burden away, because regional air services are difficult and there's not a lot of margin in it all and it would be very easy for, as a result of some of this, it would be very easy for some of the regional airlines to just walk away.

COMMISSIONER LINDWALL: Shall I start on some of the regional issues and maybe you can cover some of the – now, as you know, a lot of these airports, both the ones that take RPT traffic and the ones that don't, and the ones that could or whatever, they vary in their traffic quite a bit. So many of them do not make money, they are often council owned that have been given by the Federal Airports Corporation many years ago under that regional scheme.

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So the costs that they have are not fully recovered through landing fees, for example; do you think that's a reasonable thing that council's cross-subsidise their asset in that sense?

MR BREUST: I think a lot of the councils, and I think you can split regional airports into two groups; you've got ones that have got RPT services and then you've got a whole bunch of others that don't. The ones that receive RPT services again are, to a very large extent, considered vital to the local economy and the local community and I think a lot of councils believe that on that basis there needs to be a contribution from the local ratepayer.

But on the other hand there is this view that the airports should run on a commercial basis and I don't really think that that is possible. I think , in terms of airport passenger throughput, I think you're going to have to look at airports that have somewhere around 200,000 passengers a year before they could more than cover their operational costs. I'm not saying they'd cover all of their, particularly their infrastructure costs, but certainly cover their operational costs.

One of the issues with RPT services at an airport is that it substantially increases the airport's costs because you've got more requirements to meet, you've got to have more staff, you've got to do all these other things, whereas at a local airport which doesn't have an RPT service, the cost level is much lower. I think if you went to all of the non-RPT communities that have got airports, they would say that that airport is an absolute vital asset for them because it provides access for, you know, medical services, for emergencies, for all of those sorts of community things and on that basis I think the local community is fairly happy with meeting some of the costs. However, it still comes back to the costs of their infrastructure and they all have to go cap in hand to governments, either State or Federal, to get money to either upgrade or to build.

COMMISSIONER LINDWALL: All right. Now, in terms of the security I heard that some of the airports, of course the issue maybe it is Wagga too, it's about the load bearing on the floors of the terminal that requires - - -

MR BREUST: I think there's some of that but it's also the space. I think - and I don't know the security process because there's a whole lot of confidentiality about it, but from what I understand from the local people in Wagga, that the actual square meterage area for the whole process increases quite dramatically and on that basis, because Wagga has been

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pretty good at maintaining the facility the right sort of size for its operations, it's going to have to do extensions.

COMMISSIONER LINDWALL: So you don't think it's unreasonable for the airport to charge on an operating cost basis for the extra security if - - -

MR BREUST: I think that's okay but it's the infrastructure - - -

COMMISSIONER LINDWALL: It's more the infrastructure and the actual building and that type of thing, yes.

MR BREUST: Absolutely, absolutely.

COMMISSIONER LINDWALL: Now some airports, and I can't think of one offhand, have decided they'll screen Rex planes and the 34 seaters and the 50 seaters, at the same level. What do you think of that?

MR BREUST: I think that's a bit discriminatory but again it has to be practical and I'm sure the airlines have got a view on this, but I have heard Qantas group say that they believe in situations where there's themselves and another operator and the screening is required, their view is that all of the outbound passengers should be screened. Now, Rex may well have a different view to that, I can't speak for them but - - -

COMMISSIONER LINDWALL: Well, it does in its submission, yes. Now, the thing about your investment fund, could you talk about the role of the Australian Government versus the State Government for infrastructure provision at airports at regional centres?

MR BREUST: Yes, it's one of those areas that I really don't understand too well because it just depends on what sort of programs the various levels of government are putting in place. From my understanding, the Australian Government, the Federal Government, is more about regional development-type activities and employment and those sorts of things, and if you can work your submission relating to an airport improvement based around some of that, maybe you'll get a tick.

The State is a little different. I think they look a bit more on the infrastructure side of things because I know in a couple of - well, even in Wagga's case, the approving authority or the management authority for the particular grants for the airport go through the Department of Infrastructure in New South Wales and they look at it on a different basis.

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So as an example, I'm aware that an airport received money to do some terminal upgrades as well as some taxiway upgrades - this was before the new security requirements were announced to come in. The terminal upgrade would not suit the new security requirements but their taxiway work that they had some money approved, was not enough to complete that work. They've been fighting now with Infrastructure New South Wales for two years to try and get a transfer of the funds and it's not happening because Infrastructure New South Wales think the terminal is the thing that should be done because they can see it, while a taxiway is not so visible and media presentable.

COMMISSIONER LINDWALL: So - sorry.

MR BREUST: No, no.

COMMISSIONER LINDWALL: I was going to say the national transport or airports infrastructure fund that you propose, what's been spoken about, would you see a benefit if both the Australian Government and the relevant State Government be involved in it together?

MR BREUST: I would see it as a partnership.

COMMISSIONER LINDWALL: Yes.

MR BREUST: Very much as a partnership. And in our initial submission we also suggested, or recommended, there that there be some funding allocated from the major airports as well. They probably won't like that too much but I just thought that on the basis though that they're very much part of the system and they do very well out of non-aeronautical activities, that maybe a small amount of the revenue that they receive from that could go into that fund and overall improve the system.

COMMISSIONER KING: They benefit from the network after all.

MR BREUST: Yes.

COMMISSIONER KING: Actually let me start with the second one but there's just a bit more on security that I wanted to cover up on. I mean, it's often said with the regional airports that, "Oh well they're gold-plated", it's claimed sometimes by the airlines that they're gold-plated. I went through Wagga recently. I must confess I don't think Wagga looks very gold-plated but it may apply to some other regional airports. But to what degree do you believe that's correct? So there's political decision made to fund infrastructure that's just more than is needed for those regional airports. Let me stop there and I've got some follow-on bits.

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MR BREUST: Yes, look it varies and I think you have to look on a case by case basis and I again come back to Wagga. Wagga's got different characteristics because it's an RAAF base as well as an airline airport. The actual main runway facility was originally put in place for the Air Force and has been maintained on that basis. Whereas the terminal facilities and various other facilities there are very much related back to not only the airline operations but general aviation as well. But I think if you go then and look perhaps at Dubbo, Dubbo went through a major terminal expansion a few years ago and it was an overkill and I think Rex, in their submission pointed out a number of airport terminals particularly where they believed it was too much.

Now, a nice airport terminal facility is necessary but it needs to be of the right size and it needs to be practical and I just look at the Dubbo one and say, and I've got direct experience with Dubbo, the Dubbo one to me was an overkill, it was not designed well, it's a huge building, it's very costly to heat and cool, it splits arrivals and departures so much it's not funny, and yes it's just not efficient. The council at the time would not take input, you know, and I'm sure the airlines were saying that at the time - these are the issues with it - but there views were not taken onboard. So they're the sorts of things that have happened and that's why I believe that as part of the funding process, a regional approach to it with input from other - not only the users but the regional community as well, that take a level of the discretion of the local Government away, I think you'll end up with better outcomes.

COMMISSIONER KING: Yes. So, I mean thinking of both the recommended fund approach that you suggested in your original submission and also our draft recommendation 10.6, I mean, do you see it as being as formal as a cost benefit - economic cost benefit analysis of a regional level so trying to, you know, how formal would that process be to try and work out, "Well, is this really value for money?"

MR BREUST: At least some level of cost benefit analysis because I'm not sure anything is done at the moment. Even with Airport Master Plans, you know, – in most cases a local council will bring in a consultant and the consultant will look at it in the context of all the other airport master plan consultancies they have done, bring out their template and away they go.

COMMISSIONER KING: Yes.

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MR BREUST: And nearly all of the master plans that I've seen of late, the projections on into the future, even the projections they did, sort of 10 years ago for now, are just wildly over the top.

COMMISSIONER KING: Yes.

MR BREUST: So in that context if you look at the master plan, and say, well, this is what we need, of course, you're going to get infrastructure which is too great.

COMMISSIONER KING: So widely over the top in terms of passenger number projections or?

MR BREUST: Yes.

COMMISSIONER KING: Yes.

MR BREUST: Passenger number and aircraft size.

COMMISSIONER KING: Yes, okay.

MR BREUST: I think if you look at the master plan for Wagga, I think the future involves 737s and a new terminal and runway and the whole works.

COMMISSIONER KING: Yes.

COMMISSIONER LINDWALL: A lot of regional airports think they're going to international services, too.

COMMISSIONER KING: Yes.

MR BREUST: Yes, yes.

COMMISSIONER KING: They just need to be in a more marginal seat.

COMMISSIONER LINDWALL: Yes.

COMMISSIONER KING: When you do – with the regional airports in particular we've seen some we called it argy-bargy, I guess, in the – in our report. We've seen some interesting discussions and reactions by – for example, REX on King Island, in Mildura, and so on. More broadly, how much countervailing power or generally just power because of – divert to the airlines have at the regional airports in particular and to what degree

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does that really mean that there's an effective cap on the degree for owner's local councils to pass through any excessive costs.

MR BREUST: It's a fairly difficult area. I think just looking at it from a regional airlines point of view and obviously you can talk to them as well, but my experience has been that you've really only got two ways of exercising countervailing power. That is to go through the media and the political process and stir it up locally and lobby hard at the political level. The other bit of power that you've got is walking away. Or reducing services. And that's basically it.

The political and media process is not a good one. It just stirs up a lot of noise and a lot of activity. And I'd think, at the end of the day, it doesn't do anybody any good. That's why coming back to having effective advisory committees and good relationships being developed can lead to a lot of that noise just simply going away, because everybody ends up on the same page and I think that that's a very necessary part of what the future should be.

COMMISSIONER KING: Yes. Can I come back briefly to the major airports, because I'm really interested in your experience at Kendell. Did Kendell have any countervailing power with the major airports? So, let me (indistinct) again, I'll do a follow up afterwards.

MR BREUST: Yes. Not very much at all, really. If you go back into the history of it, post the Ansett close – sorry, pre-the Ansett collapse at the major airports, Kendell operated out of the Ansett-owned terminals. So our negotiations were with our partner in effect. So that was pretty straightforward. Following the collapse of Ansett of course, those terminals reverted back to the airport owner and so forth and I guess – and at that stage, of course, Kendell had gone. When I came into REX which was about a year or so later after they got up, Sydney Airport was our big issue. And there's a very significant case where REX and Sydney Airport had a – quite a major stoush over access to gate facilities – and I was heavily involved in that. And I can speak on the basis of my experience in relation to that and I'm certainly not speaking on REX's behalf.

The only real opportunity we had there was to go political and to go to the media. And we did try to negotiate and it was very much: this is what you're getting. If you don't like it, go away. And we started a campaign based on the fact that Sydney Airport were pushing REX out to Bankstown Airport. Of course, that probably wasn't necessarily the case but it was the means by which we had to take it to get the right sort of support. And at the end of the day, REX ended up getting its proper gate facilities and lounge, I mean, a VIP lounge for which we paid quite dearly

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in terms of the monetary side of it. But at the end of the day it was a political decision made at high level..

We believed at that stage, that was the only means by which we could have some sort of countervailing power in relation to Sydney's approach

COMMISSIONER KING: Any similar issues that the other airports you mentioned Melbourne and Adelaide for example - - -

MR BREUST: Well, not to the same degree, but it required a lot of time and effort to go through the process because – and I – in some respects, I think that's starting to change at some of those other airports, but at the time it was – you'll get what you get, basically. And then when we kept pushing back and working hard on it, eventually we ended up getting what we needed. I think in Adelaide's case, I think we had to run our passengers through the old international baggage area or something like that. You know, it was pretty terrible stuff. But eventually, after a long time, it came through. But it's a difficult process. It takes a lot of time and effort and, yeah, it just uses up so many resources.

COMMISSIONER KING: Resources.

MR BREUST: and I think REX has made the comment, you know, that in a couple of cases where they're not prepared to put any further resources into the negotiations, they say – we'll just walk away.

COMMISSIONER KING: When you're talking about that it took a long time, just for our benefit, you're talking months? Years?

MR BREUST: Yeah, months. In Sydney's case, it was a good six months or more.

COMMISSIONER KING: All right. Thank you very much for that, by the way, because it's sort of taking you a bit away from your submissions. Can I come back to just the security issues for a second? I guess – I'm sorry about jumping a bit between topics, but to come back to the earlier discussions you had on security at the regional airports, I guess at the end of the day, there's three parties who can pay for – for capital, the operating costs. It's going to be the passengers or the rate payers or the broader tax payers.

Your view or at least your submission says that the government level, so the broader tax payer level, they should be funding the installation - - -

MR BREUST: Certainly the infrastructure.

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COMMISSIONER KING: Yes. Why – given that presumably the benefits of the better security actually fall to the passengers using the airport or to the local community because not having an incident at your local airport's presumably a (indistinct) thing.

MR BREUST: I think it's – I think it's even wider than that.

COMMISSIONER KING: Okay.

MR BREUST: You know, I think the airport security and other security issues now relating to terrorism and all the rest of it, is a national issue. And I think that in terms of that infrastructure, to me it's almost just like funding the AFP or the army or the defence forces in that sense. It is a much wider issue. So – and I think what's happened is that because it's been aviation and it's been fairly specialised and it's easy to look at and it's easy, relatively easy to put things in place to be seen to be doing something. That's how it's being channelled.

But I think it's gone beyond that. I think it's a much wider issue. I think certainly operationally, the passengers should effectively pay for the provision of that day to day security. But the infrastructure, there's a lot of money involved in that and it's up front type expenditure and I think that should be funded more broadly.

COMMISSIONER KING: No, thank you. That's a good perspective on it. Sorry, there was one other thing. Sorry. Paul, if you've got something? Because there was one other thing and I've now completely lost it.

COMMISSIONER LINDWALL: Well, I'll go back on that – well, while you're thinking about that I'll go back to the infrastructure fund. Now, at the moment, you've been saying a lot of it's been a bit ad hoc with Federal Government and the State Government – allocate money by having a fund with a defined amount of money, good processes for costs benefit analysis and directing the money to the size of the infrastructure that's appropriate for that particular area. Could you conceive in fact, that it might actually be cost effective for the tax payer, then? You might actually get a lower cost?

MR BREUST: I actually believe it would be, because it - it takes the guesswork out of it, and I think a lot of it is, you know, that the decisions are almost, dare I say, made on whim, rather than good assessment and analysis. So I think - it sounds a bit socialist, I guess, but by the same token, it's - to me, it's good allocation of resources, an good use of funds'.

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And I think the funds would then go to where they're needed, and done in the right sort of way, particularly if there is a proper assessment process after the event. So, in other words, it's reviewed in, sort of, 12 months' time, or 2 years' time, or 5 years' time, that it's actually - - -

COMMISSIONER LINDWALL: Would the funds be a predetermined amount that's announced and then done - and monitored, I guess - - -

MR BREUST: Yes.

COMMISSIONER LINDWALL: And would it be managed by something like the future fund, is that how you see it?

MR BREUST: It could be. It could be. But again, I think, at the end of the day, it would probably go back to either the local government area, or - or something like that, to actually do the job. But I think there needs to be a management of that funding on top of that to make sure that it's actually been done properly.

COMMISSIONER LINDWALL: Sorry, have you decided what you?

COMMISSIONER KING: Yes, I have remembered what I - and apologies again, because it's to jump back to security.

MR BREUST: No, that's all right.

COMMISSIONER KING: So, in your submission, you mention, you know, that maybe QANTAS group is pushing regional airports to adopt screening for all RPT, and unnecessary costs on its competitors. Do you view that that leaves some of the airlines, maybe, involved in a bit of game playing with security at regional airports?

MR BREUST: I don't know, you'd have to ask them. I really can't comment on that. But - but, I think, you know, if I was an airline that didn't require screening, I - and you know, that's a substantial increase in costs, to me, I would be pushing back.

COMMISSIONER KING: Yes.

MR BREUST: And therefore I'd be trying to do everything I could to - to not have to be the subject of it. But at the end of the day, you need to have a practical outcome. And I would say that if, at a regional airport in particular, if you had the process of advisory committees, and a good relationship build along the way, I think you can overcome the issues. Because at the end of the day, we've got to approach things fairly

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rationally, and I think if you've got people in a room, with that sort of an approach in mind - we've all gone to Wagga with that in mind and we're actually starting to kick some goals, as an example.

I think the big issue Wagga has to face now, is this security requirement because there needs to be a lot of work done on the terminal to facilitate the new requirements.

On top of that, actually drilling down, so that we know exactly what the costs are for the airport, because at the moment we really don't know. We can't get into the detail. There's a few areas where we can, like direct staffing costs, but other costs that are pushed onto the airport from the council – such as last year's budget had $50,000 allocated to the airport in costs for IT.

Now, that just doesn't make sense. All of the plant and equipment used on the airport is managed under a total pool for the council, and we're saying, well, "How much did you spend on fuel for the airport last year?" "Oh, it's all part of the big pool." And we're saying, well, you know, if you're going to allocate $100,000 for plant and equipment for the airport, we need to know what those costs are. And at the moment, they can't tell us.

COMMISSIONER KING: Okay. Do you see - I mean, there sort of seems to be a natural coalition that I would expect to have formed between, say, Wagga, perhaps the local council, REX, sort of, pushing back a bit on this idea that you should have upgraded security for - for the planes that REX use. I mean, are you seeing that, do you - or is it just for relations, you know, that sort of - - -

MR BREUST: I don't know what's going on behind the scenes, in terms of all of that.

COMMISSIONER KING: Okay.

MR BREUST: And I'm really not in a position to comment, and I really - - -

COMMISSIONER KING: Okay, that's fine.

MR BREUST: I don't think I'd really like to.

COMMISSIONER KING: Yes.

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MR BREUST: Because that's a matter for them. And in terms of REX, you know, I'm a has-been. I was there a few years ago.

COMMISSIONER KING: That's all right. That's all right. I think that's all I have, actually.

COMMISSIONER LINDWALL: Okay. Well, there's a couple of issues we should touch upon. One's the Sydney regional access, of course.

MR BREUST: Yes.

COMMISSIONER LINDWALL: What can you say about that, and does it work, and would you improve it in any way?

MR BREUST: I think what you're suggesting in terms of the change is appropriate, but I think, you know, again, I'm just speaking as myself. Obviously QantasLink and REX and others will have views in relation to that, particularly in terms of the change that you're suggesting. Definitely the access requirements for regional services are necessary, otherwise the regions will miss out, and if it's just left to operate purely on economic rationality, folks, the regions won't have service. It's as simple as that. And you can't blame the airport, in that sense, because they've got a physical asset they need to maximise utilisation.

COMMISSIONER LINDWALL: (Indistinct) capacity - - -

MR BREUST: (Indistinct) get the best out of it as, you know, A380s every day, you know, every flight. But, to accommodate the smaller aircraft, you need to have some sort of an arrangement. So, unfortunately, that's the way it is.

COMMISSIONER LINDWALL: And the way the creation of the Western Sydney airport, how do you see that effecting - - -

MR BREUST: I think that's going to have a huge impact in Sydney. I can see regionally that Wagga, for argument sake, will end up with services to both - both KSA and to Western Sydney, and I half suspect both the airlines will do them, and I think that's going to open up Sydney tremendously, and I think that's going to benefit, you know, Canberra, and Brisbane and Melbourne and all the rest of them as well, because it enables services to be generated into western Sydney, which is a huge catchment area.

COMMISSIONER LINDWALL: Could I finally ask then about jet fuel, or even, in your case with GA, outgas, in regional airports. Is there

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anything you could comment about both the provision of it, the pricing of it, the quantity that's available et cetera?

MR BREUST: We all - from the general aviation side of things, we all just say, well, "We have to pay what they want, otherwise we won't get it." And it's $2.33 a litre at Wagga at the moment, and you can get some discounts, but it's fairly difficult. But you can pay as much in the more remote areas - I think I paid, last September in Birdsville, about $3.20, $3.50 a litre. But again, understandable, it's a long way from nowhere. (Indistinct).

COMMISSIONER LINDWALL: I heard in the forest (indistinct) it's about $4 a litre.

MR BREUST: It could well be, yes. Yes. But most of the more remote Queensland and New South Wales places it's up in that $2.50 plus. Wagga's a little better - Wagga's not so bad, because there are two operators there, and also they've got the REX Pilot Academy, which increases the throughput quite considerably. So, we sort of - - -

COMMISSIONER LINDWALL: Yes. So, who are the two operators you've got (indistinct).

MR BREUST: We've got World Fuel and BP.

COMMISSIONER LINDWALL: Okay, so having two operators does provide a little bit of competition?

MR BREUST: It does, absolutely.

COMMISSIONER LINDWALL: All right, I think - - -

MR BREUST: In fact, they've just changed World Fuel has now taken the contract for the Pilot Academy off BP, so, BP might become a little cheaper again, I don't know.

COMMISSIONER LINDWALL: Okay, well thank you very much (indistinct).

MR BREUST: Thank you. My pleasure, thank you.

COMMISSIONER LINDWALL: What type of plane do you fly?

MR BREUST: Beechcraft Bonanza. (Indistinct).

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COMMISSIONER LINDWALL: (Indistinct). All right, well let's take a break for morning tea, and resume with Canberra Airport at quarter past 11.

SHORT ADJOURNMENT **[10.58am]**

RESUMED **[11.18 am]**

COMMISSIONER LINDWALL: Well I'd like everyone, could we welcome Stephen Byron and Stephen Carson. Now gentlemen, if you could address – say your names and jobs, and then perhaps a brief introductory statement, that would be perfect.

MR BYRON: Sure. Stephen Byron, I'm the managing director of Canberra Airport.

MR CARSON: And Stephen Carson. I'm the chief financial officer of Canberra airport.

COMMISSIONER LINDWALL: Welcome.

MR BYRON: Thank you. And as you say, we will make a brief introductory statement, and happy to sort of return to a number of issues as you choose and take you through. But I did by way of introduction want to acknowledge the interim report and the rigor that has gone into that and the work that's been done.

One issue that we did want to pick up by way of introductory comment was in relation to Canberra Airport's market power. And in part, it might just be a little bit of slight weighting of the words and that, but I do think it's worth teasing out somewhat. In the draft report, I think you single out Canberra Airport as being closer to the threshold for market power and regulation than others. And that could imply we're super close, or not very close or what have you, and that's probably one of our reasons for bringing it up.

But for us in part, we turn back to your 2012 report, where it was acknowledged that Adelaide and "to a lesser extent", Darwin and Canberra had moderate market power, so I suppose that pitches where it is and puts us relative to Adelaide. The conclusion made by the PC in this draft report was significantly drawn upon the high proportion of business versus leisure traffic at Canberra Airport, and that's probably what we

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wanted to flush out. Our view is that there's been no significant change in market power or dynamics since the 2012 report, where we were lesser than Adelaide.

There are the same mitigants in place, although in reality, given the growth of Adelaide being substantially more than Canberra, we are a smaller airport proportionally to them. Probably the differences are that now there are more formally two airlines domestically: there's no independent, low cost carrier, and we think that has and is playing itself out in the Australian domestic market, but particularly in Canberra in terms of the capacity control that those two airlines exert on Canberra airport. That control of the market by them, not us, is greater.

And secondly, to examine this issue of modal competition and to put that in the context for discussion of the proportion of business versus leisure traffic. The airlines who control the market don't service Canberra Airport, really with a low cost carrier. We have a tiny taste of Tiger and we're grateful for it to Melbourne and a couple of services a week to Brisbane, but we don't have Jetstar. And by comparison, a place like Tasmania, which has the same number of domestic tourists, 2.7 million domestic tourists per annum, they have over 230 weekly services versus our 11. And similarly, Adelaide, which has I think 50,000 more domestic tourists than us, 2.8 million versus our 2.75, they have – I think it's 150 – 135 weekly LCC services.

The point about that is (a) it shows who's got the market power in controlling the market, but secondly, it shows that if we had those services, we would have probably 1.5 to 1.8 million more leisure traffic, and therefore you'd be able to make a different assessment of Canberra Airport. So the fact that something that we have no control over, the share of business v leisure is counting against us, is something we'd like you to have a little look at.

The other aspect of it is particularly the modal shift when we look at the Canberra/Sydney market, and that's always been a case where we've had significant competition with three aspects: the road, the bus service, but then also Sydney Airport as an alternate airport to us for international services and access to LCC services like Gold Coast and Hobart. So it's been our competition, but the mode of road (indistinct) on Canberra/Sydney is the now competition.

Again the evidence where you don't have a low cost carrier on that route, is that passenger numbers have come down. They've come down from 2010 where they were 1.1 million passengers, to now in 2018, 950,000

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passengers. There used to be 35 per cent of our passengers on that route, and now it's 29 per cent.

So that's very significant. And it's something we don't have any control of, that shift to particularly the Murrays bus, – the hourly services that go from 4 am to 7 pm. And again, the context we say in terms of your assessment of market power for airports is not only to acknowledge the competition we face and the modal shift where we've substantially lost the battle; secondly, that it's not in our control, it's in the airlines' control, not ours; and thirdly, that if you took into account about 1 million, maybe 1.5 million passengers that are on the Canberra/Sydney route on the route via private car or a bus, they're leisure travellers. And if you added them into the assessment of our market - we think you should include them in the assessment of our market size and competition – you'd see that the market is such-Canberra is a market with the leisure traffic; it's just they're not flying, for forces outside our control.

Lastly on that point about market power, whilst I've said we don't set the airfares it's the airlines who fly here, we instead, our charges are flat. They are fixed, and they are not distinguished between leisure and business, in fact we essentially have no pricing control over the structure of our charges. But if we were to be a profit maximiser seeking to capitalise on this high business share that we end up with, we would have yield-based pricing that would differentiate between the types of passengers, the routes on which they fly, and indeed the charges that the airlines charge. We don't have the power to do any of those things, and our charges are the same for leisure and business, the same for every flight, and so on, so forth. So that's probably the opening discussion point that we wanted to put forward and - - -

COMMISSIONER LINDWALL: Thank you very much.

COMMISSIONER KING: Can I just do one clarification?

COMMISSIONER LINDWALL: Yes, yes.

COMMISSIONER KING: Just on that last bit. Sorry, Stephen. Just to clarify that bit on price discrimination, so you said something along the lines of, you aren't able to set differential charges. The pricing is beyond – outside your control. Do you mind just expanding on that more, the restrictions are on Canberra Airport's ability if they wanted to set different prices? Is it a legislative constraint, or - - -

MR BYRON: Yes. I mean do you want to respond to it?

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MR CARSON: Yes, I think the key point to make there is that we have long term pricing agreements with the Qantas Group and with the Virgin Group. And so within that horizon, the prices are largely fixed for and set for the two mainline carriers, but also the two low cost subsidiaries of those airlines.

MR BYRON: And the thing is, the structure of those prices is determined by them. So if we had an idea and canvassed it in different ways of changing the nature of the relationship, so maybe it wasn't a per pax charge. We've at different times talked about for the landing component going back to an MTOW based charge. That's dismissed out of hand summarily, and you know, it's not one thing that we as an airport get to discuss very much. It's not possible for us to embark on a discussion with the airlines to say maybe our airport charge should be different for Perth than say, for Sydney.

Maybe it should be a proportion of the airfare in line with if you're charging business passengers more, then the airport charge could be different. That's not within our control to really have those discussions, and - - -

COMMISSIONER KING: Sorry, I just want to - - -

COMMISSIONER LINDWALL: Yes.

COMMISSIONER KING: So have you had those discussions or raised these potential issues with the airlines in the past, and if so, what has been – you know, when you say it's not really within your control, you can raise them with the airlines.

MR BYRON: I mean, at different times we've had a long, four or five hour discussion over a whole range of issues in the last six months with some airlines, and we spent a couple of minutes on the idea of a differential charging mechanism to change the relationship between the airport and the airline. Part of that would require them to share their data on their fares and revenues, and it was not something that was attractive to them. They certainly feel that they get the lowest charges from an airport such as ourselves by having it fixed in this way.

They also strongly want them to be passenger-based charges so that they can pass them onto the passenger outside the – you know, as a ticket tax and lump it in with taxes, not – you can never understand that, but they have tried to move a lot of the costs of an airport, including their own costs, in the airport/airline relationship to be the airport's responsibility, and secondly, to be expressed as a per passenger charge.

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MR CARSON: The other thing that I would add too is that when we've reached a long term pricing agreement with the airlines, we've taken – the airport has taken the volume risk, so we sort of, with the airline, have agreed a price path, and we're projecting a certain growth which would result in a certain revenue stream to the airport. And if that passenger growth doesn't arise, which it hasn't in our case, then you know, as an overall – the overall commercial outcome is worse for us under that approach.

But once the prices are set, it continues to be the airlines – or the airlines have the capability to determine the product, the frequency, the airfares, et cetera, and they've got a fixed price so they can take that into account when they're setting their fares and determining the yields that they're going to generate from the market.

COMMISSIONER KING: Sorry, just one last thing on price discrimination.

MR BYRON: Yes.

COMMISSIONER KING: Just again, this is more clarification really. Has Canberra Airport ever raised differential time of day pricing, so higher charges if you're landing at a desirable – you know, let's say 8, 8.30, I want to get to a 9 o'clock meeting. Have they been thought of, raised, what's occurred?

MR BYRON: Not really, and I can't see an easy way for us to make the argument, and it's certainly not something – we haven't had in discussions with them, you know, maybe over 20 years of doing this job, I've thought about it once or twice, sometimes in relation to a question like that. But it's not something that's yet necessary given the pressure – the availability of infrastructure, and particularly on the runway side there's no – you need to manage it in that way.

COMMISSIONER KING: Okay.

COMMISSIONER LINDWALL: Now you use a building block methodology to negotiate with the airport, airlines. Why?

MR BYRON: I mean, certainly that's a methodology that the airlines are accepting of and supportive of. So that's been the basis for all of the negotiations bar one that I'll come to. And I think that's a function of the evolution of coming out of the price cap mechanism and the negotiations

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that were done in those first few years, and then you know, where do you go to from there?

It's something that the airlines have been very comfortable with, something they feel delivers them the lowest result, and certainly for us, particularly on the airfield side, we have always over that first 15 to 18 years had a price that has been lower than the building block methodology, so a lot of the negotiation has been, you know, how does one get to a pathway to get up to price, as it were.

In terms of, whilst that's been the framework around all of our negotiation, and particularly the more regular airport services agreement pricing, when we did the terminal agreement with Qantas, it was not structured in such a way. It was, in fact, a much more commercial deal, and it was in 2005, December 2005, that we signed a commercial agreement that set the charge for the new terminal at $5.50 per passenger, and that wasn't set off a building block methodology. It was an agreed commercial price.

Probably in the background we had a bit of a sense, both of us, that it was fair, given the infrastructure we would build, and it had a set of expectations and service level requirements to be delivered. That was formalised in a development deed at November 2007, and we were able to then build a terminal, but we could have built something a lot less. We could have built something, perhaps, like what Gold Coast is now, and if we'd have done that the charge would have been the same.

So the fact that we built something better did not cost Qantas or Virgin anything more. That was a position that we took. So certainly it's been a bit ironic along this process to see some aspects of the airlines running a gold plating argument.

COMMISSIONER LINDWALL: Yes, I was going to ask you that question, that they have been saying that it's been gold plated, Canberra Airport, and that therefore is, by both implication plus statement, has led to higher prices for customers at Canberra Airport, but you don't agree with that.

MR BYRON: Well, it's about as factually incorrect as you can get. There is no relationship between the quality of what we have there and the charge that was set and they know that. It was set by commercial agreement, not set on what we built, number one. Number two, you know, at its opening, the Qantas CEO significantly praised the facility and welcomed it, and I remember then another walk-round with him two months later where he said we should get the Emirates CEO here to look

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at the quality, enormously welcoming, and every Qantas executive has been pleased about that.

At the time of the start of this PC discussion, and possible elements of gold plating being alleged generally, I wrote to the airlines, both of them, to ask if they had any concerns about the pricing arrangements we had which were pursuant to written, contractual agreements and the issue of gold plating. Got no response. On the day Qantas media ran it against us last year in August, we were in a five hour meeting with Qantas and we had specifically written to them ahead of the meeting asking them to articulate any issues of gold plating. There was no concern. The issue was not raised. So you're getting this divorce in this gaming world of the hearings, of the rhetoric, from the commercial reality.

COMMISSIONER LINDWALL: So what about the other claim that Qantas put in its submission that Canberra Airport charges are 200 per cent more than Adelaide Airport which they say is a similar type of airport?

MR BYRON: Well, we're not aware of it, but I mean, they're not 200 per cent above, but they're above. You know, there's a volume-based issue here, and for example, Air Services Australia, air traffic control tower and fire services are approximately double of Adelaide because of the - sorry, double at Canberra versus Adelaide because they have more volume for the same level of infrastructure.

I haven't seen the details of the claim, but again, you know, if you go through and work through whether Qantas are happy with our charges or not happy, what we've worked through is that every element of every charge they've entered into willingly, particularly, for example, the terminal charge. They gave up a terminal lease and that infrastructure. They gave up an engineering lease and they did it because they wanted the terminal we were going to build and they wanted the commerce on that. It was entirely willing.

Every price that Qantas has paid they've accepted. When you look at the air field services charge pricing, they make the final offer to us of what they're willing to pay. When you then have written contracts and some price increases that they don't agree with in the pricing contract they will not pay that charge down to the level of 4 to 8 cents. They'll refuse to pay it. So if there's a little bit of skirmish it's at the edges. It's in the cents, and it's not a function of saying Canberra Airport's charges are massively higher than another airport. They're the charges that we've worked through together commercially to deliver the infrastructure we have.

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COMMISSIONER LINDWALL: A former hearing participant earlier today, Harry Bush, said that he was surprised, and he comes from the United Kingdom, that Australia, which has what he thinks is a fairly sound regulatory framework, doesn't - hasn't moved away from the building block methodology, more to the commercial type of approach that you mentioned. To what do you attribute that and is there a scope for more of a traditional commercial negotiation rather than a building block methodology to be used.

MR CARSON: Yes, I mean, it will come down to the negotiation, I guess, and the appetite, I guess. There is a conditioning in the market that the airlines are familiar with a building block approach, and, you know, there's elements to review and discuss. The four monitored airports are almost monitored against that. Their prices against them on volumes and theoretical returns versus the, you know, a building block concept. So I think in general it's embedded into our industry a little bit. But at the end of the day, the agreements that we have reached have moved away from, even though you've started a discussion using potentially a building block approach, that gets moved away from in the end when agreement is reached.

MR BYRON: The other comment I'd make is I think, I think if it stays into the final report, your comments about the parity pricing clauses, or the terms no less favourable clauses that airlines have insisted on airports, I think if they are removed there is more scope for commercial negotiation and deals in a broader bundle kind of way to the advantage of all participants. I think the rigour with which those clauses have been applied on smaller airports have locked in the structures of the way you deal and negotiate, and I think they're very anti-competitive. Our board took a decision before the 2012 inquiry that we wouldn't accept signing agreements with them any more, and we would always start every negotiation with that point, and then at the very end it would be insisted that it be put in.

So we don't have a lot of market power on the non-price terms such as that or bank guarantees and the like, but I think the removal of that and that being clear in the pricing principles, and it should apply from when the report or when it gets enacted. It shouldn't wait until those things just expire over the next decade.

COMMISSIONER LINDWALL: Do you think that, Stephen, that the pricing principles are sufficient for that? We did recommend that would be included in there in the local pricing principles, but they're optional, they're not mandatory, so could it still be even if we - even if the

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government - if we put that in our final report and the government had accepted it, would it be that you might fear that they still exist?

MR BYRON: I think it would probably be enough. It's not guaranteed, but I think it would allow us to stand our ground and not - and try to argue for the point that it not be in a final concluded agreement because it's contrary to the pricing principles. It's not certain, but, you know, today we got no chance- - -

COMMISSIONER LINDWALL: Given what you've said about the absence, the general absence of low cost carriers at Canberra, what do you attribute that to, given the potential demand, as you say, with tourists, et cetera, coming to Canberra?

MR BYRON: I mean, it's difficult, but you know, the airlines are, quite rightly, allowed to choose to profit maximise and , you know, let's also be clear that it's very important for the airlines in this country, domestically and internationally, to be profitable businesses. You know, what's a fair return is always up for grabs, but that's not completely part of this inquiry.

COMMISSIONER LINDWALL: Yes.

MR BYRON: But the airlines have decided that they maximise their profit by servicing only a segment of this market, and if you don't provide the cheaper product, you don't cannibalise your yield, we're hopeful that through direct engagement and articulation of the size of that market that we might be able to attract Jetstar and we'd like to see that and we'd like to see Tiger ramp up their services here as well to service the growing tourism market.

COMMISSIONER LINDWALL: But to be clear, in your current contract you are unable to offer a lower price to Jetstar which might potentially attract them to come to Canberra which at the moment is too expensive perhaps.

MR BYRON: There are carve-outs for the introduction of services and particularly the introduction of new routes, but they only last for 12 to 24 months. But, you know, on the other hand, I mean, Tiger Airlines has shown that low cost carriers can and do operate very profitably, and the ability to access this market is not – and service the leisure market isn't a function of the airport charges at Canberra Airport. That's a misnomer.

COMMISSIONER LINDWALL: I assume, but can you clarify, Canberra Airport has entered into discussions with Jetstar or approached them in the past about operating services out of Canberra?

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MR BYRON: Yes.

COMMISSIONER LINDWALL: Yes. You said the airlines and the airlines' approach. Just to clarify, your comment could be let's guess that when you're approaching Jetstar but it's really the decisions about Jetstar are based on what's good for Qantas and Jetstar together rather than Jetstar as an independent company, so is that what you meant or is that a misinterpretation of what you said when you were talking about the airlines?

MR BYRON: I don't know that's what I meant or what I said, but it's absolutely correct, and I don't – I'm just checking myself to see is it commercially fair to say that, but, you know, Qantas in all of their announcements, publicly say that they have a dual brand strategy domestically and that gives them a very strong powerful market position and it allows them to maximise profits across markets. So they are quite publicly clear that the decisions about, you know, how much Jetstar and how much Qantas in a particular market, even if it's 0/100 per cent or 100/0, those decisions are made by the Qantas Group as a whole in the interests of maximising its Group profitability.

COMMISSIONER LINDWALL: Okay, so Jetstar's not operating out of Canberra. Your view is one of the reasons behind that is that the Qantas group does not believe it will maximise profits for that group.

MR CARSON: That's right.

COMMISSIONER LINDWALL: Yes. Is it a similar situation with Virgin and Tiger?

MR BYRON: So yes, and I think that's why you have 11 services a week from Tiger, not, you know 45 or 55, and why you don't have 70 or 80 services from Jetstar. But, you know - and I don't know that we'll get to there, but we can get to a better place. You know, maybe if I'm a bit more clear, in 2016 we ran a process with Jetstar and Tiger and we said that we're working in partnership with the state government and the state tourism authorities to get a low cost carrier and we will put out an offer to you that will have the commercial terms to attract the commencement of low cost services into Canberra, and we did that and we said it would be available only to one of you on a first come, first served basis, and within twenty – we said you must respond within 28 days, but in any case it's first come, first served.

Jetstar responded to accept the commercial terms and the charges that we'd offered together with the support commercial framework and marketing support from ourselves and the government, and they just had a

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couple of queries to work through. But in parallel, Tiger had also accepted and they moved more quickly to accept and publicly announce those services.

So Jetstar – we got very close to getting Jetstar. In the end we got Tiger, and who knows what will happen down the track. I think ultimately there is a big leisure market and it's big enough for both of them, and my feeling is that the Qantas Group is missing out on some profitability by not yet having Jetstar. But that's up to us to deliver and work collaboratively with them.

COMMISSIONER KING: Sorry, Paul, just one last one before passing back to you.

COMMISSIONER LINDWALL: That's all right.

COMMISSIONER KING: In your introductory comments and just then you mentioned the size of the leisure market and in your earlier submission you talked about Canberra Airport, private vehicle being the main competition on the Sydney/Canberra route. Do you have data behind that that you'd be able to provide to the commission?

MR BYRON: Yes, we can go back to some of that data, but, you know, on the road there's about 5,000,000 passengers. On the bus, there's now over a million passengers, so there's more on the bus than in the air, so we can do a bit more work on that.

COMMISSIONER KING: Just understanding what the data is and also the source of the data is useful from our perspective.

MR BYRON: Yes, yes. Apart from the infrastructure.

COMMISSIONER KING: Can I ask the other data question, which is can you make publicly available your I guess rack rate charges for aeronautical services?

MR BYRON: Yes, we can do that. Why don't we do that through – with you.

COMMISSIONER KING: How much – Sydney airport has had a number of cancellations – sorry, not Sydney airport. A lot of cancellations of flights between Sydney and Canberra have occurred, and I think you mentioned this in your submission, and delays due to basic – also the way Sydney airport has got its constraints in operations – operational constraints to Sydney. Does that bear on the market for people driving as well, I presume, that people would drive rather than use a plane because they're worried about reliability of the service to Sydney?

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MR BYRON: Yes, I mean, most certainly that plays into it because you do have the modal choice and when – you know, these things are about reliability. When you see the level of airfares on Canberra/Sydney, you know, the reality is that it is business people substantially using it, so they are time-poor and reliability and time precision is critically important to them.

We certainly had a situation where the cancellation rates blew out above 8 per cent and as a number of different senior airline executives of different airlines made it clear to me, is that if you're above 2 per cent, you're losing confidence of the market and you're going backward and you've got a, you know, trust and confidence issue that needs to be addressed. Canberra airport – sorry, Canberra/Sydney has had a rate of cancellation above the national average for too long, and so in April of last year we put a challenge to both airlines that we would reward them with a $100,000 reward to the best airline so long as its result was as good as or better than the national average.

You know, all we are asking for on Canberra/Sydney is a result that is on average as good as the national average. We're not asking for special treatment. And it hadn't happened – it hadn't occurred for how long? About seven years before then. There hadn't been a month where Canberra/Sydney was better than the national average. Well, in April, on Canberra/Sydney, both airlines were better than the national average and over the next five months there were three months where both airlines were better and four months where at least one airline was better than the national average.

So it was an outstanding success and shows what can be done. And I think it's critically important to the consumer and the traveller on that route.

COMMISSIONER LINDWALL: Did you pay the reward?

MR BYRON: They didn't want us to.

COMMISSIONER LINDWALL: No?

MR BYRON: So it's interesting in the context of debates about airline charges where, as I said, airlines will not pay you to the tune of 4 or 8 cents for 18 or 24 months or longer. When it came to that, what was equivalent of a dollar per passenger or $100,000 per month, neither of the airlines wanted to be rewarded with that.

COMMISSIONER LINDWALL: You've now got two international services, Singapore and Qatar, and I understand you haven't used

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negotiations with them through BARA. How have you found the negotiations with the international carriers, and where do you see that heading for Canberra?

MR CARSON: I think in relation to the internationals, those negotiations have been good and collaborative, and probably more time has been spent negotiating and discussing the operations and the operational aspects rather than the commercial aspects.

COMMISSIONER LINDWALL: Now, you know that some participants are the ACCC, A4NZ and some airlines have argued for a negotiate-arbitrate approach for airport and eight ASAs and they have – obviously if you're to follow our model it would be something for all those airports with market power and we've already said that you didn't have in our draft report, but hypothetically what do you see – negotiate-arbitrate having an implication for Canberra if Canberra did have market power and was exercising it?

MR BYRON: So we'll just get all the assumptions clear.

COMMISSIONER LINDWALL: Yes.

MR BYRON: So if we had market power, if we were exercising it in an improper way, and if we weren't then the airlines would pass on the savings - - -

COMMISSIONER LINDWALL: Well, actually the second part is not relevant because the argument is that you have market power therefore they have negotiate-arbitrate, you don't have to be exercising it. That's what the ACCC have said, A4ANZ has not said that. So what implications would that have?

MR BYRON: So we will return to the point later about whether they'd pass on the savings because ultimately they'd pitch this as an argument to the benefits of consumers. My view is that every engagement on a commercial matter would be seen through the prism of how you position yourself and get ready for the negotiate-arbitrate, so you'd know you were never negotiating and I'm sure we would fall into that line of behaviour necessarily as well. So you'd never get anything done. You'd be always postulating and setting yourselves up for that.

My view is that the airlines with the biggest market volume would use it to control capacity and try and prohibit investment, and so ultimately that would be pretty detrimental to competition, to airfares and to the consumer.

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COMMISSIONER LINDWALL: So you're basically saying that it could lead to higher fares, rather than lower fares?

MR BYRON: Yes, and lesser investment too. I mean, you know, I think this negotiate-arbitrate locks in gaming behaviour. And I think we've seen very significant gaming behaviour in the lead up to this inquiry and through the inquiry. You know, I've articulated the fact that, you know, the airlines have made public arguments on particular aspects about Canberra Airport in the same hours we've been in the meeting room where that's not been an issue of contention to be even raised or discussed.

So you get this divorced behaviour. You get behaviours for two years coming onto this inquiry. In my mind, a desire to prove that agreements can't be made or that airlines will not standby already existing written agreements that are binding. And then I think you see when you see the writing on the wall of detailed credible economic analysis and an acknowledgement even by the political media classes that this is – the arguments are not being properly made by the other side, without integrity and without the reality of the savings being passed on to the consumers, I think the political classes are not seeing the appetite for the change.

So I think you are seeing the strategic change play itself out very quickly with the airlines in terms of the willingness to enter into deals and to move away from their more recent behaviour.

So if that happens every five years or seven years when we have these inquiries, goodness me, what happens if every commercial negotiation can go to a negotiate-arbitrate. The gaming behaviour's locked in as a permanent state of being.

COMMISSIONER LINDWALL: Did you have anything you want to talk about in negotiate-arbitrate or gaming?

COMMISSIONER KING: Not so much on that, but come back to international just very briefly. I am just aware of the time, yes. Just on the international services, BARA has in its submission since draft, notes – I am paraphrasing them, but the issue is service quality, service measures, rather than so much price per se, at least at the airports that have market power.

In your negotiations, how have you dealt with that? Has that been the major part of a negotiation? Where have the negotiations to international airlines really focused?

MR BYRON: I mean, it is interesting in documentation terms, it hasn't focused on that. In realty terms there's been a lot of focus on that, and you

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know, our desire to make them as operationally successful as possible. Clearly we're in competition with Sydney Airport internationally when we were having the service Sydney, Canberra, Wellington we were very much in competition with Wellington, Auckland, Singapore or Wellington, Melbourne or Sydney, Singapore.

So there's a lot of focus operationally and collegially on the product and so we've got a high class transit – you know, it is a transit lounge but it is a high class product for all passengers. So that's true. In the commercial negotiations, I don't know that we've got heaps in those agreements. I know in the domestic airline agreements we have significant service level standards particularly in the terminal agreement around all of the elements of the service that have, as I said, service level standards and penalties for not meeting them. So it is all in the documentation.

MR CARSON: We haven't actually negotiated with BARA or discussed with BARA - - -

COMMISSIONER KING: No, I understand it wasn't with BARA but yes, I was just wondering because this had been put to us and I was just interested in a practical example because you are not negotiating with BARA.

MR CARSON: Well, we think and we also stand behind the quality of our product and the service that we provide and the international experience is pretty seamless for travellers, for departing and arriving passengers. It's a very efficient process from check-in through both levels of screening and with Border agencies. So you can be from the aircraft to your car in ten minutes getting off an international flight in Canberra.

COMMISSIONER LINDWALL: I don't think you can do that anywhere else in Australia.

COMMISSIONER KING: I can tell you, you can't at Melbourne.

COMMISSIONER LINDWALL: Did you have any - - -

COMMISSIONER KING: No, that's – resolving disputes with your customers, how are they normally handed both when there's a contract in place versus when one had expired and there was a bit of argy-bargy for want of a better term, like publically in the newspapers and on the television and so on, about you know, Qantas has made a bit of a song about that. So what would you say?

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MR BYRON: Yes, I mean, our agreements, the airfield services agreement and the terminal services agreement have dispute resolution clauses. They've occasionally been used, enacted through the notice provisions and of course, there is the ability under those contracts to go to the more formal dispute resolution thing called the courtroom. You know, they're written contracts in place.

The reality is, we are bound by way of our connection forever together, and they are our major customers. Our business depends on them and, you know, I reflect back on the fact that we've done some of the most fantastic things in the domestic aviation industry with Virgin and with Qantas, and we've delivered them and we've been great partners, and I think particularly with Qantas, I think for 18 of the last 20 years, we've probably been the pin-up model airport that they pointed to, and you know, we fell into a way of not being in agreement in the last more recent time and I think that's matured now and we're back onto an even footing.

It's interesting that the dispute resolution clauses didn't particularly provide the framework to resolve the commercial disputes. It took the goodwill of the parties to meet at the highest level and to commit to the relationship before then the detail was worked through, and you know, I think sometimes we're a very small airport that doesn't get a lot of time at the high levels in the airline businesses for understandable reasons, and so sometimes some things can manifest themselves and get further out of the best kilter.

COMMISSIONER LINDWALL: So disproportionately, you basically - - -

MR BYRON : Yes. And anyway, we're in good shape now with our airline customers and looking forward to, as we said, the challenge of growing their business, leisure and business in the town.

COMMISSIONER LINDWALL: Do you think that your contracts and your arrangements and your positioning with your customers is such that you can capture innovations and technology which mutually benefit both sides?

MR BYRON: Yes, I do. I think so. I mean, we're cutting edge in terms of the deployment of facial recognition technology for staff security control as a two-factor authorisation process. You know, when you arrive at Canberra airport you go down from the upper level to the baggage level and you go through from the sterile of the secure area into the non-sterile, and there's no security guards there. That's made an enormous saving because of the deployment of world first technology through a Sydney-based

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Australian company and Qantas and other airports now deploy that detection, pass-back detection technology.

When we were building the airport we realised as the security issues were moving forward and there was debate about the screening of vehicles, so we decided to put a tunnel from our loading dock through into the airside for all vehicles that need to go, so that we could use the common security screening point for staff and goods going into the terminal because investment of capital substantial as it was, very substantial, was net cost saving versus the labour cost of additional security points just for vehicles.

So you know, I think our contracts enable and encourage that and they require us, particularly in security, to deliver security efficiently and cost effectively for the passengers and the airline.

COMMISSIONER LINDWALL: Okay. Thank you very much for appearing today. Stephen and Stephen, thank you.

MR BYRON: Thank you.

COMMISSIONER LINDWALL: Now, we do always offer an opportunity for anyone to come up and have a say, either to agree or rebut or anything else for that matter. Does anyone want to take that opportunity today? No. In which case, I will adjourn the proceedings until tomorrow in Sydney. Thank you all for being here. A short day today.

MATTER ADJOURNED AT 1.01 pm
UNTIL TUESDAY, 26 MARCH 2019

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Australian Government
Productivity Commission

PRODUCTIVITY COMMISSION

ECONOMIC REGULATION OF AIRPORTS

MR P LINDWALL Commissioner
DR S KING, Commissioner

TRANSCRIPT OF PROCEEDINGS

AT GRACE HOTEL, SYDNEY
ON TUESDAY 26 MARCH 2019 AT 9.29 AM

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COMMISSIONER LINDWALL: Okay, everyone, we might get started shortly in 30 seconds or so because I like an on time departure. Welcome everyone and good morning, and welcome to the public hearings for the Productivity Commission inquiry into the economic regulation of airports. I'm Paul Lindwall the presiding commissioner of this inquiry and I have got Stephen King with me, my fellow commissioner, and we would like to obviously acknowledge the traditional custodians, the Gadigal people.

The inquiry started with a reference from the Australian Government in June 2018. The purpose of the inquiry is to investigate whether the economic regulation of airport services promotes the efficient operation of airports and related industries.

We released an issues paper in July 2018 and talked to a range of organisations and individuals with an interest in the economic regulation of airports. This has included representatives from the Australian State/Territory governments, airports, airlines, industry representative bodies, academics, researchers and individuals - that pretty much covers everyone on the planet I guess - with an interest in the issues throughout the inquiry. We held focus public hearings on competition in the market for jet fuel in Sydney and Melbourne in late November 2018.

Following the release of the draft report in February the Commission has called for further submissions and is undertaking consultations along with these public hearings. I think we have so far received 88 submissions prior to the draft report and 16, but they're coming in still, since the release of the draft report. We are grateful to all organisations and individuals who have taken the time to prepare submissions and appear at these hearings.

This is the second public hearing for this inquiry post release of the draft report. Following this hearing there will also be a hearing in Melbourne and then we will be working towards completing the final report having considered all the evidence presented at the hearings and submissions and informal discussions.

The final report will be submitted to the Australian Government in June, and participants and those who have registered their interest in the inquiry will be advised when the final report is released by the government, which may be up to 25 sitting days after the revision after its completion.

The purpose of these hearings is to provide an opportunity for interested parties to provide comments and feedback on the draft report and to facilitate public scrutiny of the Commission's work. We would like to conduct all hearings in a reasonably informal manner, but I remind

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participants that a full transcript is being taken. For this reason comments from the floor cannot be taken, but at the end of today's proceedings we will provide an opportunity for anyone who wishes to do so to make a brief presentation.

You are not required to take an oath, but are required under the Productivity Commission Act to be truthful in your remarks. Participants are welcome to comment on the issues raised in other submissions or by other participants at hearings. The transcripts will be made available on our website following the hearings. Submissions are available also on the website obviously.

For any media representatives, and I understand there may be one today attending, there are some general rules. Please see one of our staff, either Anna or Rebecca, who - there's a handout to explain those rules. To comply with the requirements of the Commonwealth Occupational Health & Safety legislation you are advised that in the unlikely event of an emergency requiring evacuation please listen for instructions over the PA and the meet up point is at the corner of Clarence and Market Streets here. So I think that's it for the introduction, so I would like to welcome our first participants today, they are Sydney Airport Corporation and for the record if you would give your name and position and perhaps make a brief introduction.

MR CULBERT: Thank you very much. My name is Geoff Culbert, I'm the CEO of Sydney Airport. I am joined today by Hugh Wehby who is the COO of Sydney Airport.

First of all thank you for the opportunity to appear today, we do appreciate it. This is my first experience with the Productivity Commission review into airports, and for the record I have found it to be extremely professional, open and fair. We have been given the opportunity to meet on numerous occasions, and the discussion and analysis has always been fact-based and evidence-based, and we thank you for that.

This has been an interesting experience for me. I am relatively new to the industry having joined about 12 months ago. I had previous experience in a range of industries, including financial services and energy. So the comparisons have been very interesting. What I see here is an industry that is working very efficiently. Everyone is doing well. Airports are doing well, airlines are doing well, and most importantly the end customer is benefitting.

The current system has allowed us to grow, but we are also incentivised to invest, to attract competition to the market and to improve customer

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service. Since privatisation we have invested over $4.7b and grown the number of airlines flying into Sydney Airport from 37 to 47, thus increasing competition and providing more choice for consumers. At the same time our customer satisfaction scores have continued to improve and now stand at all-time highs.

In addition airlines are doing well. Qantas's most recent results demonstrate this. They are posting record profits. We don't begrudge this. In fact we are happy for their success as it contributes to the overall success of the aviation sector. A healthy vibrant aviation sector is essential to deliver improved outcomes for passengers and to grow the economy, but most importantly as I said before the current system is working in the interests of passengers. Customer satisfaction has never been higher and international prices have never been lower. By way of an example in 1994 an economy airfare from Sydney to Singapore would have cost you about $2,100 in today's terms. That was equivalent to around two and a half weeks of the average income at that time. Today in 2019 a ticket from Sydney to Singapore will cost you about $350 on a low cost carrier, or $850 full fare, which is less than a week's average income.

So when Australians sit down to plan the next family holiday they're seeing more choice and they're seeing more value than ever before. So airports are profitable, airlines are profitable, and passengers are enjoying more choice, lower prices and better quality of service. It does beg the question what's wrong with the current system. The short answer is nothing. The light-handed regulatory regime is working.

We agree with the Commission's conclusion that the current regulatory regime is fit for purpose. The market is working efficiently and everyone is benefitting. There is nothing with the current regime that is broken that needs to be fixed. We also agree with the Commission's conclusion that commercial negotiations between airports and airlines give little cause for concern. The role of regulation is to protect consumers and to guard against market failures. The role of regulation is not to readjust the bargaining position of sophisticated commercial entities that are capable of looking after themselves.

Perhaps most importantly we were pleased with the conclusion that there is no evidence that we as an airport are exercising market power. We take our obligations seriously. We're constantly seeking to improve the airport for the benefit of both airlines and passengers. We are currently investing over $1m a day to improve facilities, balancing the needs of all 47 airlines who fly into Sydney Airport and numerous other stakeholders.

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We constantly take feedback from customers and we use that feedback to invest in areas that matter the most to them. This has been reflected in our customer satisfaction scores and through the ACCC monitoring reports where we were rated good for the first time in a decade. Having said that we recognise that we can improve and will continue to do that. We will continue to do it because it's the right thing to do, but it is worth noting that the current regulatory regime provides a real and effective deterrent to any inappropriate exercise of market power. The potential threat of price notification and declaration is tangible and credible. The current regime's effectiveness should not be underestimated.

Finally I will say the PC made a number of recommendations in the report and we largely agree with them. This is reflected in our most recent submission. This review has been a valuable exercise in assessing where the industry stands, our own performance as Australia's largest airport, and as a means to identify areas where we can all improve. The review makes the industry better, and that's good for customers, and with that Hugh and I are happy to take any questions you may have.

COMMISSIONER LINDWALL: Thank you very much, Geoff. I might start with - could we talk about the negotiate-arbitrate, which is a proposal that airlines and some other participants have made, and they would point to the fact that the (indistinct) in the case of the east coast gas pipelines that have been around (indistinct) negotiate-arbitrate for about 18 months and then have been (indistinct) arbitration since then, and that therefore it wouldn't make any difference to negotiation, but it might help balance what they perceive as an imbalance in bargaining power. Would you like to comment on whether the relevance of the east coast gas market and the fact that perhaps you wouldn't (indistinct) with arbitration terribly much. At least we would have such (indistinct) for airports.

MR CULBERT: Yes, I think it's a good question. The aviation industry is very different from the gas industry, and we believe that the concept of negotiate-arbitrate will not be effective in relation to the aviation industry, and we say that for two reasons; number 1, we think it's open to gaming and it removes the incentive to negotiate, and by that I mean there is an incentive for parties just to put a low ball offer in, claim the negotiations have broken down and then take your chances with the arbitrator in the negotiation-arbitration process, but perhaps more importantly a bigger concern detailed in our submissions is the fact that we believe that negotiate-arbitrate will lead to outcomes very difficult for us to reconcile.

So we currently, as I said before, have 47 different airlines that operate out of Sydney Airport. If we were to enter into negotiate-arbitrate arrangements we would potentially end up with 47 different outcomes

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which are very difficult to then reconcile. We have common use infrastructure, we have common use assets, and each airline at the airport is looking for a preferred position. So if we were to end up with outcomes from an arbitration process that we then have to try and reconcile amongst those 47 airlines, we think that would be extremely difficult to manage and really not realistic. So we believe that negotiate-arbitrate process has its flaws and wouldn't work.

COMMISSIONER LINDWALL: One way of the negotiate-arbitrate working I would perceive will be for an airport such as Sydney and a single airline working on to an arbitrator. Another way would be the airport having all 47 on the one arbitration which (indistinct) single merits one way or the other.

MR CULBERT: I think it would be difficult for all 47 airlines to enter into a single agreement. What we see is a very complex environment where you have very strong incumbent airlines, remembering of course that between Qantas and Virgin they currently occupy around three-quarters of all the slots at Sydney Airport. So they have a very strong and entrenched position, and we see competition between the airlines in relation to that aspect. So I think it would be very difficult to get all 47 airlines to agree to a negotiate-arbitrate position holistically, but that's something I think you have to ask the individual airlines as to whether or not they are prepared to do that.

COMMISSIONER LINDWALL: And in terms of the investment strategy at Sydney Airport if you did have negotiate-arbitrate what would you expect would be the impact on your investment plans going forward and what do you think an arbitrator would end up (indistinct words)?

MR CULBERT: It's a really important point, because we can only invest to grow the airport, to grow capacity, to bring more airlines in, to provide more choice for the end customers if we have got certainty of investment, and the only way we get certainty of investment is if we have agreement with the airlines. So if we're caught up in a negotiate-arbitrate process that is being gamed, that is resulting in outcomes that are very difficult for us to reconcile, it does actually operate as an inhibitor to our ability to invest in the airport, and this is a really important point.

The other point I would make is throughout our history we have never failed to reach an agreement with the airlines. These are robust commercial discussions between two very sophisticated commercial entities who know how to look after themselves, and there's a lot that's actually discussed in these arrangements. Arrangements are complex, they're detailed, there are multiple trade-offs, and ultimately we get to

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commercial outcomes. It would be very difficult for an arbitrator who doesn't understand the aviation industry to really appreciate all of those complexities and come up with an outcome that would be suitable for both parties. My view is that it would delay investment, it would delay our ability to grow capacity at the airport, which would be harmful for the end consumer because ultimately that reduces competition and reduces quality of service.

COMMISSIONER LINDWALL: So to be clear negotiate-arbitrate from your perspective will almost immeasurably lead to less investment or a slower path of investment (indistinct) status quo and couldn't lead to (indistinct).

MR CULBERT: That is our concern, yes.

COMMISSIONER KING: Just to clarify one thing. You said you never fail to reach agreement. Can I just confirm you've got active agreements with all 47 airlines at the moment?

MR CULBERT: Yes, we do.

MR WEHBY: The only exception is that due to the regulated nature of regionals, it's not possible to have agreements with regional operators - outside of the regional pricing we have commercial agreements for airlines.

MR CULBERT: And individual - - -

COMMISSIONER KING: When was the most recent (indistinct) agreement concluded?

MR WEHBY: We did an agreement with the domestic Tiger business at the end of 2017. We did all our international agreements, Qantas Terminal 3 Agreement and Qantas Domestic Runway Agreement in mid 2015.

COMMISSIONER KING: Actually just on the background on those, the negotiation process, did it take a long time, a short time? Were you looking at months for these agreements overall, years, what sort of background can we have?

MR WEHBY: Sure. I will provide it separately because it's quite a different story for the International and Qantas Agreement. The Qantas agreement was a voluntary agreement on taking control of T3, in 2015. It was a bring forward of the lease expiring over the terminal from June

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2019 to June 2015. So it wasn't an agreement we had to do, and therefore it took some years actually to get to a position where everyone was comfortable with the outcome. It was still four years ahead of its schedule and drove a half a billion dollar cheque for Qantas and ongoing aeronautical charges for Sydney Airport, but actually because there was no expiring agreement, I think we spent a lot of time getting that exactly right for all parties and bringing in the International and Domestic Runway Agreement into a pool of compromises. So that was it.

On the international side it was probably around a year and it was primarily negotiated with BARA, the representative for most of our international airlines. They are not a counterparty to the agreements, we then go and contract with each of the airlines, but that would have been close to a year where we were talking everything from a building block model through to an investment profile, a charges profile, and ultimately even beyond the agreement the setting up of a KPI framework which we are measured against. So closer to a year in total.

MR CULBERT: The thing I've noticed as well as I have come into this role is it's not as though you talk three months out from the expiry of the agreement and then start negotiating. We have daily interactions with all of the airlines where we are constantly talking about what's going on in the precincts, the capacity that we need to build to create more opportunity for airlines to fly into the airport, to improve customer service, and so these conversations are ongoing and it tends to coalesce around an agreement to be closer to the expiry of an existing agreement. So the conversations are very detailed, complex, and are happening the whole time.

COMMISSIONER KING: Let's take some of those negotiations. Presumably some of them hit road blocks at various stages. Surely at some of those stages access to an arbiter who would have been able to deal with some of those specific road blocks would that have sped up the negotiation process?

MR WEHBY: We actually did bring a party in between us on the terminal 3 negotiations. We outlined that in our first submission. They provided a recommendation for the deal which was rejected, and the terms on which they proposed it were rejected by both parties. So it was an unsuccessful use of a, I think more like a conciliator rather than arbitrator to be perfectly fair, but trying to seek that middle ground. So we have used voluntary third parties from time to time. They have not been successful, and it was really for a voluntary single airline agreement. It really doesn't reflect the ordinary course of business.

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We have done two terminal transactions; terminal 2 from the Ansett administrator in 2002, and terminal 3 from Qantas in 2015. We now own all three of the terminals. So it's quite a unique set of circumstances, and it didn't actually end up capturing the detail that we needed to bring in the international charges, the domestic runway charges. The reason we got an agreement in my opinion is it was a multifaceted agreement where we could have compromises on both sides.

COMMISSIONER KING: You mentioned the airlines gaming negotiator or a negotiate-arbitrate system. We have heard that from a number of parties, but we haven't actually heard any details about what that means. I mean what is meant by gaming the system; can you give us any examples of what you think they would be doing?

MR CULBERT: Our concern is that - is that you would be incentivised just to put a low ball offer in, on the table, and then maintain the negotiations have broken down, and then you'd put it to the arbitrator. So, just to use some examples, if you were say negotiating an airline agreement, and an airline might come in and say, well, "We'll pay 50 per cent of the current charges. That's our offer," and then you go into negotiations, it's very difficult to even perceive that kind of discount, and so the negotiations immediately break down, you go to the arbitrator, the arbitrator comes in, if they were picking the midpoint, say 25 per cent, the airlines are still substantially better off than they otherwise would have been if you started from the base principle that you negotiate from the previous price. That is our concern.

MR WEHBY: I would also add, on the investment side, each airline has actually very different requirements. We're going through a process of consultation now, when you get to the international terminal. For the same project, we're getting criticised for gold plating our terminal, and for under investing in our terminal. So, I think you've got to be very careful about the background to each area. What capacity there is for what products, and reconciling between regional, domestic, international, or between low cost and full service international airlines is incredibly complex.

We actually rely heavily on groups like BARA to help us navigate that process, and to develop a set of compromises even on the investment plan, let alone the pricing. So there is potential for gaming on the investment plan as well.

COMMISSIONER KING: Can I just - can I just follow that up. Concerns that you've got about gaming, and arbitrator or a negotiate arbitrate solution, which would be a regulatory (indistinct), the arbitrator

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would presumably have a set of guidelines, and have his guidelines, for example, in (indistinct). Could those guidelines, in your opinion, deal with the sort of gaming that you've raised? Would you - would you be able to set up an arbitration system that had appropriate guidelines to be able to get to a mutually beneficial outcome for the airport and the airline?

MR WEHBY: I think when you're entering 47 agreements at different times, noting that all our expiries are different, it would be incredibly complex. I think you could achieve that on a single airline agreement. I think balancing the needs of 47 different airlines, with different products, different services, different passengers, and different growth profiles – it would be almost impossible to even structure around.

MR CULBERT: And that's our bigger point. I don't want to overstate the gaming point. It is a point. But our bigger point is the inability, or difficulty, to reconcile outcomes, amongst the 47 airlines all looking for different outcomes at the airport. And as Hugh said, we have arguments from airlines that we're gold plating, on the same assets that our other airlines are arguing that we're under-investing. So the difficulty of reconciling outcomes between all those airlines is the bigger point. It's a bigger point than the gaming point.

So even if you had guidelines in place to try to manage the - the gaming issue, you're still asking an arbitrator, who's not an expert in operating airports, doesn't understand the history and the complexity of these arrangements, and doesn't understand the complexity of the common use infrastructure, the common use assets, to try to come up with outcomes that can be reconciled amongst all 47 airlines, and those arbitrations would be taking place at different times in the calendar. It makes life extremely difficult and complex.

COMMISSIONER LINDWALL: When we - unless you have any (indistinct) negotiate-arbitrates, I mean I just want a quick question before I move on to some other topic, it seems like you think there's a significant advantage of having individualised agreements with different airports as - airlines, as opposed to, say, New Zealand, where it's a common agreement for all the airlines?

MR WEHBY: There's certainly some advantage for both parties. I think sometimes there's specific product requirements that you could never provide, or contract, with all airlines. Sometimes, people are looking for bespoke legal changes, that might not work in the jurisdiction. More importantly, though, people are generally looking for different products. Whether that be because they're serving different markets like regional, domestic or international or whether they actually want different standards

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of product within it, a boiler plate agreement certainly is facilitated by BARA, including things like KPIs and that's an incredibly useful document.

But then it is our requirement to go and contract individually to make sure the individual requirements are overlayed, and we think there's value to that, for both the airport and also the airlines.

COMMISSIONER LINDWALL: Can I mention, while we're on that topic then, about negotiating, there have been some thoughts that we should provide some guidelines, either the government should or the Productivity Commission, or the ACCC or some other body, provide guidelines or whether (indistinct) of BARA already does, obviously, (indistinct) and structure of contracts, do you see advantages or disadvantages of that?

MR CULBERT: In our second submission, we actually put that forward as - as a potential proposal. We said some negotiating principles may help. And we thought that would be useful in two respects: (1), from the airports perspective, it could create a set of guidelines that would create a standard around which airports operate, when it comes to their discussions with the airlines. And what we were talking about there in our submission was the willingness to decide about SLAs, and KPIs, commitments around customer service levels, and infrastructure development.

That's something that we've done at Sydney Airport in our most recent agreements, and we feel like that's actually been a really positive step forward. We are now committed, there are objective measurements in place, and they really drive our behaviours. And that was consistently applied across airports in Australia, we think that would be beneficial. But we also thought negotiating principles would operate effectively in relation to the way that the airlines approach negotiation, and we were arguing, or asking, that they come to the negotiating table with a fair and reasonable position, because we do see evidence of things like short paying, non-paying, infrastructure blocking that actually gets in the way of constructive negotiations.

And so, the negotiation principles are not just to tie airports to a set of outcomes, but also to ensure that the airlines themselves come to the negotiations with a fair and reasonable position.

COMMISSIONER LINDWALL: The risk, I guess, and I do see some (indistinct) in the principles (indistinct), spoken there as parties, but is there not a risk that you could end up with the (indistinct) if the government decided you were (indistinct) principles and so on?

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MR CULBERT: There's no doubt about that. And it kind of goes back to my original comment that we seem to be grasping for a new regime, when the existing regime is working really well. And you only have to look at the industry as a whole to see that, you've got airports are doing well, and we're incentivised to invest, and we are investing, customer service levels are going up, competition's increasing, we're attracting more competition in the market from an international perspective. Airlines are doing well. Qantas is posting record profits.

But most importantly, the end customer is doing well. They've got more choice. They're enjoying the better quality of service. The prices are lower than they've ever been before, on the international side. So, we're grasping for a view as to what needs to change, and the answer, as I said in my opening, is actually nothing. This is a really efficient market, with a light-handed regulation that's doing its job. So, any changes to the system are unnecessary and threaten that. There's no doubt that the negotiation processes are robust, and challenging, and time-consuming and drawn out.

That's the nature of any complex, difficult, commercial negotiation, between two sophisticated counter parties who are capable of looking after themselves, and who have a very clear view of what they're trying to seek out of the negotiation. But we always reach agreement. We've always been able to reach agreement, and the end beneficiary of that has been the customer.

COMMISSIONER LINDWALL: Now, can we move on to another - - -

COMMISSIONER KING: Sorry, before we move on. Just to clarify, because you did support the -the AAA and BARA proposal on the overarching principles, I still don't understand the argument as to why it needs government's involvement. So, everything that you've talked about having (indistinct) to discuss issues, why is there a view that government, some part of government, needs to be sitting at that table?

MR CULBERT: I'm not sure we were suggesting that in our report - I'll have to take that on notice, as to whether or not we were actually, in our submission, suggesting that the government would have to be involved in that process. I think where we were going on this is that as you come to the ACCC monitoring report, every year, and as you come to the PC every five years, you can assess whether or not the airlines and the airports have been behaving in a consistent fashion with the negotiation principles, as a way of determining when the parties are acting appropriately.

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Asking a government agency to come in and assess performance against these negotiating principles on a deal by deal basis, I think would be challenging for the reasons that you're pointing out.

COMMISSIONER LINDWALL: Now, could we move to a different direction, (indistinct). When we looked at exercising market power, and analysed the benchmarks at major airports of Australia against those and overseas, comparatively, we found that we had a bit of a concern about potentially, the international services at Sydney Airport seeming to be somewhat high. Could you explain perhaps is that true, and if so why they might be higher than the international comparators?

MR CULBERT: Yes. So our international charges were set by the ACCC when we were privatised back in the early 2000s, and as we pointed out in our most recent submission, our prices were higher, substantially higher, than all of the other capital city airports. The ACCC set those prices substantially higher than all the other capital city airports at that time which is a consequence of a number of factors. It was the cost of land, we're in Sydney where land prices are high, we're 8 kilometres from the CBD, we have three runways, two terminals separated by the runways, a high percentage of international long haul flights and then significant investment in the airport in the lead-up to the Sydney Olympics, so the prices were set at that level for that reason.

If you look at how the prices have increased since then you see that they actually have increased at a very moderate level, they've increased at less than one per cent per annum in real terms over the past 17 years. The ACCC, in their own report, stated that the revenue for a passenger at Sydney Airport has increased at the lowest level of all of the monitored airports over the past decade. So the international charges are a product of the initial setting by the ACCC and we don't believe there's been any evidence of exercise of market power since then that's reflected in the moderate increase in prices since then.

COMMISSIONER LINDWALL: In the way the ACCC assesses Sydney Airport's asset base for the long-term report affects reporting good terms on aeronautical services, or assets I guess, what are the (indistinct words)?

MR WEHBY: The magnitude grows over time and it's reasonably complex. We have an indexed asset base with a real vanilla WACC at privatisation which was the opposite of all the other major privatised airports. We estimate that the ACCC overstates our returns by between one-and-a-half to two per cent relative to the other airports today. It's very hard to determine that without the background detail for the calculation the

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ACCC does, that's our estimate, we've provided some follow-up data to the PC to support that but we also note that it will be exacerbated over time.

COMMISSIONER LINDWALL: So, what should be done about that if you think that's wrong?

MR WEHBY: We think we should be measured relative to the way we were privatised and relative to the way the regulation applied when the ACCC initially set charges, which is how we've continued to operate, as Geoff said.

COMMISSIONER LINDWALL: Now, obviously Sydney is a unique asset, Sydney Airport is a unique asset in terms of its location as you were saying, with the land values and so on, the returns can be also affected by congestion and regulations which make it difficult to expand the general capacity (indistinct), how much do you think that has an effect on price and cost?

MR WEHBY: I think when you look at the InterVISTAS report (that's part of the AAA submission), it looked at the average asset base per passenger and Sydney is, by global standards, at the top. There's really two reasons for that in my opinion. One is that we sit on reclaimed land in a very constrained environment close to the city, the second is we've had to build to a super peak, we have a very busy period from 7 till 11 each morning and a reasonably modest busyness in the international terminal in the afternoon.

You actually, generally, in infrastructure, have to develop close to your peak infrastructure and it might not be utilised as effectively throughout the day. That's a product of geographic location and our own choice but, practically, it has resulted in a higher asset base, so the peak and the location and the congestion certainly drive higher pricing. Over time we have managed to grow the off-peak, we have managed to stretch the peak and that has ameliorated those impacts somewhat. But we are still, at the end of the day, a very peaky airport with a 7 to 11 period, particularly in the international terminal, that drives a huge amount of investment.

COMMISSIONER LINDWALL: How do you expect the effect of Sydney Airport from the opening of Western Sydney Airport (indistinct)?

MR CULBERT: We think it's definitely going to provide competition. If you look at our Master Plan that we submitted last year which we're in the process of now finalising, we estimated that in 2039 we would have 66 million passengers passing through Sydney Airport. In the master plan 2034, the previous master plan, we estimated that that would be 74 million

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passengers, and the material difference going from 74 to 66 is the introduction of WSA. For the first time in our master plan we factored in WSA being an operating airport.

COMMISSIONER LINDWALL: Now, could we move on to some of the movement capping issues, in particular how often do you think aircraft are delayed due to the cap, what is the length or extent of the delays (indistinct words)?

MR WEHBY: Sure. I guess without being specific, because I'd have to take that on notice, it's very regular, particular in cases of disruption for either weather events or east coast general airport airspace issues, so there are generally daily delays in relation to the operation of the cap. One of the issues there is we are measured on both the scheduled movement cap and an actual movement cap, in particular the use of that actual movement cap does tend to create ongoing issues.

That primarily, again, occurs at the morning peak and the evening peak, but we have shown in our most recent submission, I don't think that's published yet, that the time to recovery can actually stretch beyond the day of operation, even from morning disruption. So, flexibility in the operation of those operating restrictions, without any extra aircraft, would actually allow recovery and minimise the economic impact, make the asset more efficient, make the east coast airspace more efficient in general.

MR CULBERT: Our biggest challenge is the lack of flexibility. We're not asking or arguing for a change to the curfew, we're not asking for an increase in the overall envelope in respect of flights, what we are saying is that a lack of flexibility is providing us with real operational challenges. Recognising that these regulations were set in the 1990s when we were handling 21 million passengers a year and we're now handling 44 million passengers, so the whole nature of the airport has changed and the lack of flexibility is what is really providing the change.

So we asked Airbiz to do some analysis, which is actually in our latest submission. Their analysis concluded that a three hour disruption starting at 3 pm in the afternoon, based on the current operating restrictions, doesn't get cleared until 11 am the next day. If we were to even measure the movements on a daily basis then we would be able to clear that disruption before curfew, before 11 pm. So going over into the next day creates 90,000 hours of passenger delays and gives rise to 8000 overnight stays for people who are trying to get home that night, so that's a sense of the impact in relation to flexibility.

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COMMISSIONER LINDWALL: Now, I should say that PC wasn't able to and on no occasion have we ever said that the curfew was to change, nor have we proposed any changes to the removal of cap with minus any possible options for that to be spread out or changed in some way that might be actually levelled. If you were to change the movements in peak periods to other parts of the airport to off-peak periods within that, or shifted somehow, what effect would that have on other operations of the airport such as baggage handling, car parking, et cetera?

MR WEHBY: If we were to take movements from the peak to the off-peak it would alleviate some of the congestion issues we see, particularly probably around the roads, somewhat in the check-in hall. Our biggest criticisms currently from BARA relate to baggage and to bussing, so it would potentially reduce the bussing and maybe reduce the number of gates you would need to deliver. In terms of baggage, it would hopefully make our baggage system more efficient, it is at peak loads at the moment and we are actually looking at developing a new bag room to accommodate those loads. So, once again, it may reduce the need for that investment or, at the very least, improve the operational performance of our current baggage system.

COMMISSIONER LINDWALL: Now, if we look at the other way where there was some flexibility and you increased it in some of the peak hours say, what's the maximum number of movements that you could handle given the current infrastructure do you think?

MR WEHBY: Current infrastructure would need to be expanded. We don't, at the behest of airlines and from economic practicality, we don't build beyond the peak. So we would need to build gates, we would need to be build aircraft stands for parking areas and we would need to extend the baggage system probably more aggressively. We could practically accommodate a number, more than 80, on the airfield in terms of air space, air services estimates with the current mix of aircraft that's probably closer to 90 an hour but it does depend on the mix of aircraft as well, and that may change over time, but we would absolutely need to invest immediately to accommodate the aircraft. And it's worth noting that when slots are allocated, they're not just allocated on whether a movement is available according to the operating restrictions, they're allocated on whether the infrastructure is available. So those slots could not be allocated until we develop the infrastructure that was required to accommodate those services.

COMMISSIONER KING: There are a number of alternatives suggested in regards to allowing more flexibility in the movement cap. Has Sydney Airport done any work on which of those would be the most appropriate (indistinct) in the short term where investment in other infrastructure

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would be in issue? And also, does Sydney Airport look to any of the effects on the noise that may be generated to the local residents from (indistinct) those movements?

MR CULBERT: The answer is – is yes. When we've looked at this, we've tried to balance the operational needs of the airport with the needs of the local community and that's why, in our submissions, you'll see that we're not –arguing in favour of a change to the curfew. We're not suggesting a change to the overall envelope. We're just suggesting that more flexibility is required because of the fact that under the current regime, we're limited to 80 flights an hour and it's measured on a rolling hour basis every 15 minutes. So 20 flights every 15 minutes. It makes it really challenging to try to catch up in the event of disruption.

So if you look at global benchmarks, Heathrow Airport also have an envelope that they work against. But they're measured on an annual basis. So they have around about 500,000 movements a year and they're measured on an annual basis. They get to the end of the year. If they've exceeded that envelope, then their envelope next year goes down by the amount that they exceeded times two. So if they go down by 20, then they have 40 less movements in the following year.

Obviously any period of time that provides for the greatest amount of flexibility would be beneficial. Heathrow are a yearly measurement, a monthly measurement, a weekly measurement, a daily measurement. Anything would be helpful for us to be able to manage the restrictions that we have and the inflexibility that prevents us from recovering from disruptions. Anything less than a day, we think, would be less beneficial, particularly as you get towards the end of the day.

If you have a storm occurring at 8, 9 o'clock at night, naturally, you're going to go into the next day. And therefore, greater flexibility is beneficial. And the next morning, you start with the morning peak, where we're pretty full and it's hard to recover until you're getting to around about 11 am the next day.

COMMISSIONER KING: Sorry, because I'm aware of time, but just briefly, it has been put to us in some of our discussions with groups representing residents that increasing the flexibility even on, say, an 80 per hour over a day type of approach, so that would simply mean that it would be gamed to use a word you've used earlier on in this discussion. It would end up with more airlines and more flights being put in the peak periods, because they're effectively the most valuable, so yes, the total number of flights may not change, but you start getting more concentrated noise and more loss of amenity for local residents in the peak periods

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which also of course overlap with times when the residents tend to be home.

So the idea there is that it would be an undesirable thing. So what's your comment to that?

MR WEHBY: I mean, one of the issues that we would have to look at with any change is the slot allocation procedures as well. Whether you allow airlines that are not operating the peak to move into the peak or whether they're preserved for new airlines, for instance. We saw precedent in something like that when Ansett collapsed. Whether slots were actually preserved for new carriers to come in and utilise those. So you didn't see a mass shift of an incumbent airline into an existing peak slot for instance.

So actually, any changes to flexibility around the operating restrictions, must be accompanied with a review of how the slots are the allocated. And that could lead to the addressing of some of those issues that the communities rightly bring out. We understand those issues. We're concerned about those issues as well. And we'd need to look at the slot allocation procedures, along with the operating restrictions to get a holistic view of noise.

COMMISSIONER LINDWALL: Now, we've got not much time, so I'll just ask about landside access. Do you use take it or leave it contracts and how do you set the price for landside access?

MR CULBERT: So the short answer is no we don't make take it or leave it offers. The landside access that we have at the airport covers a range of different modes of transport but firstly, 37 per cent of all trips that are made to the airport are made in private vehicles where the consumer doesn't pay a cent, so we have free drop off and pick up, so 37 per cent of trips are completely free on drop off and pick up.

Train is now at 24 per cent of total trips to the airport. Sydney Airport has no economic interest in the train that's owned and run by a private operator and run together with the government. And then you have two other categories. You have rental cars and you have what we call ground transport operators. The rental car agreements are negotiated between once again, sophisticated commercial counterparties. We're talking the likes of Avis and Hertz, who are global companies. They operate in airports around the world. And we enter into negotiated agreements with them.

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We have agreements at the moment which average seven year terms. And those agreements have agreed price escalations in them that are agreed upfront. We have consultation with the rental car companies. We have a bi-annual industry association consultation process but we also have daily and weekly bilaterals with our relationship managers on the airport.

So no take it or leave it offers being made there at all. In relation to the ground transport, we have two categories. We have those who require access agreements and those who don't. So access agreements are required by the likes of buses, limousines and shuttles. We have over 3000 of those. And so, the way it works with that category is that if someone wants to get access to the airport, then they'll sign up to an access agreement. And that's to ensure that they actually are a reputable operator, that they've got the right insurances in place. There's a due diligence process that happens there. And then they'll sign up to a schedule of fees which are published on our website and are available to everyone.

And the fees that they pay vary depending on which category you're talking about. Limousines have, at their own request, a site very close to the front of the terminal and therefore, they'll pay a higher access fee than say, cars that are further back from the terminal. And we also set those prices to motivate the parties to reduce congestion. So the longer you stay, the higher the charge is because we're trying to get people through and reduce congestion around the airport.

I should say the biggest single complaint we have at the airport is road congestion. And so we're very conscious of trying to manage that. We have quarterly industry association catch-ups with that category of ground transport operators. We have regular ad hoc meetings and those conversations are ongoing.

The second category of ground transport operators are taxis and rideshare where no access agreement is required. Taxis pay an access fee to get to the airport. Rideshare are able to use our priority pick up which is behind the taxi. So taxis have a preferred position over the rideshare, given their incumbency. And once again, we have regular industry association catch-ups with them and we have relationship managers at the airport who are available to speak to the likes of taxis and rideshare on a regular basis.

COMMISSIONER LINDWALL: Well, in the interests of time and I – we can talk about other things like jet fuel, car parking, yes, regional access and so on, so I think we'll have to call it quits there. But one quick final question. Why do you use the building block technology in air service agreements?

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MR WEHBY: Primarily because of precedent. The airlines generally like us to share a building block model to start their negotiations. What we don't go and do is agree the elements of the building block as part of the pricing arrangements. So we generally share a financial model. It sets the basis for the negotiation from the airport side. The airlines get access to that and can use that as the basis for their discussions as well. So I'd say it's a springboard, but we pretty much agree a price, a price path and an investment profile. Outside of that, there's no agreement on the elements of the building block.

COMMISSIONER LINDWALL: Yes. Well, thank you, Gentlemen. Thank you (indistinct).

MR WEHBY: Thank you.

COMMISSIONER LINDWALL: We'll go straight in now to Brisbane Airport. So I invite our Brisbane participants to appear. Then we'll have one more participant and then we'll have a little morning tea break. We do have another slot at 2 o'clock if anyone wants to use it, by the way. We may as well use it efficiently. So once again welcome and if you could state your names and positions and then you give us an introductory statement as you see fit.

MR DE GRAAFF: My name is Gert-Jan De Graaff. I'm the Brisbane Airport Corporation CEO and I'm joined by David Malek who's CFO of Brisbane Airport Corporation.

COMMISSIONER LINDWALL: Thank you. Yes. Do you want to give an introductory statement?

MR DE GRAAFF: Yes, please. I'd like to thank the Commission for the opportunity to appear at this hearing. These regular reviews by the Productivity Commission is an important process that recognises the significance of the Howard Government's decision to privatise Australia's major airports in the mid-90s. That privatisation has been a resounding success. Obviously that's our view and I daresay it's even the view of the majority of our customers, both airlines as well as the travelling public.

The evidence is clear that privatisation and the light-handed regulatory regime, has delivered to the Australian people and to the airlines significant benefits and a more stable aviation industry than is enjoyed in many other countries. The ultimate success of privatisation which was motivated by the government's desire to see our industry grow, our airports improve and the public benefit, can be seen in the fact that

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Australia's major airports are regularly ranked in the top 100 airports in the world, many of them in the top 50 and at least one or two in the top 20.

Brisbane Airport has been considered Australia's best in all manner of global rankings, and later this week at the annual world airports' awards in London, I hope to see us again crowned the best in the country and one of the best in the world. That Australia's airports achieve these rankings despite their relatively small size compared to the other international ports, and in the absence of government subsidy, which in some countries have seen investment, utterly unrelated to any need for a financial return, is a testament to the system as it stands today.

The system contains within it the necessary checks and balances, including these regular reviews by the PC to ensure that private ownership recognises its responsibilities to the consumer and to the nation, whilst also allowing the profitability to encourage and ensure investment in the growth that drives economic benefit across the country. In the years since 1987 when Brisbane Airport Corporation took control of Brisbane Airport, the number of travellers using the airport has grown 167 per cent to more than 23 million. The number of airlines accommodated has grown 20 per cent to 35.

The number of businesses on site has nearly quadrupled to 420, and the number of people employed on site has grown around 260 per cent to around 24,000, or one in every 100 jobs in Queensland, and importantly this growth has also facilitated the growth and profitability of our partners in the aviation industry, and in Australia's and the world's airlines.

Over the past three reviews by the PC of the economic regulations of Australia's airports, the analysis has been consistent and the conclusions have been consistent. This consistency has provided confidence to our investors, enabling them to sink more than three and a half billion in capital into Brisbane Airport in the last 21 years, and another 2.2 billion in the coming years. Without this level of confidence we would not be building our new runway, a piece of infrastructure of national importance.

We are grateful to the Commission for its fidelity to the original principles of its reviews and for the thoroughness of its analysis. We recognise, too, that whilst a draft report of this review is largely favourable to the positions we have taken in our submission, there are always areas for improvement. We have in our written supplementary submission provided additional information to the commission in response to a variety of information requests. I won't detail those in this statement, but we're happy to discuss this request further this morning.

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Whilst the Commission has rightly concluded that Brisbane Airport Corporation has not misused any market power it holds, it has highlighted a couple of potential areas for attention, notably our international charges and our quality of service agreements with our airline pilots. I'm happy to address these now, though further details are also included in our supplementary submissions.

International charges. The quantum of the international charges at Brisbane Airport primarily reflect the significant investment in the expansion of the international terminal building itself in 2007 and 2008, and more recently in 2015 and 2018. It also reflects major investment in the associated aprons in the international terminal, and the runway system. The capacity investments we have made reflect the peaky-ness of the international demand at Brisbane Airport with most international services landing during the morning peak. Whilst it is certainly our desire and intention to encourage growth into the shoulder periods, the reality is that Brisbane is an O and D (origin and destination) airport and arrivals into Brisbane are overwhelmingly dictated by departure slots at origin airports, particularly in Asia and the Middle East.

In contrast, our domestic terminal has had relatively low investment over the same period as more than two-thirds of the building was, until the beginning of this year, subject to leases to Qantas Airlines and Virgin Australia, and of course domestic demand is more evenly spread across the day. Our published international charges for both the runway and the terminals are based on the building block models and reflect the forecast capital expenditure for the respective services.

The building block models which were shared with our airline customers as part of the negotiation process provide visibility of the proposed capital expenditure projects, operating costs and demand forecasts. It is important to note that the investment side was also reflected in the price path for the international terminal. These charges are remaining flat or falling in real terms over the next few years. As noted by the Commission, the level of charges in itself will not necessarily reflect abuse of market power and the level of the charges should be considered in the context of the investment cycle, service quality and the overall returns to BAC.

In summary. The international terminal has been subject to significant investment in the past 10 years. Service quality remains good and overall returns are moderate and the lowest of the monitored airports. Taking all these factors into consideration, it is clear that the level of charges for

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international passengers does not reflect the use of market power. Rather, it reflects the relative investment in the international terminal.

With regard to service quality, the Commission also flagged service quality at Brisbane Airport as being a potential indicator of the use of market power at BAC. We are unsure of the rationale behind this and note that it would appear to be at odds with the subsequent observations and comments in the draft report. Specifically the Commission notes that Brisbane Airport performs better on other indicators other than the high international charges discussed of, and then noted the consistently high service quality ratings at Brisbane Airport relative to other airports.

The presentation of service quality at Brisbane Airport as amber on the traffic light chart is also at odds with the subsequent statement that there is not a problem with service quality at monitored airports. As detailed in our earlier submission to the commission, Brisbane Airport has consistently ranked highly on the quality of aeronautical car parking and landside access services provided at the airport.

This is reflected in the monitoring reports published by the Australian Competition Consumer Commission as well as external rankings such as those produced by Skytrax and ACI. The quality of service at Brisbane Airport has been consistently good without being excessive and does not reflect a potential abuse of market power. Commissioners, we are more than happy to explore these questions through you now.

COMMISSIONER LINDWALL: Thank you very much. Could I just start, you've said there are 35 airlines. How many of the airlines do you have agreements with?

MR MALEK: Currently there are some airlines which are represented as non-signatories, so of the 35 airlines, there are 29 which are signatories, and of those, we currently have 28 airlines who have either signed commercial agreements, commercially agreed terms or are currently paying the new charges. There's one airline that we have not been able to agree commercial terms with.

COMMISSIONER LINDWALL: One still outstanding?

MR MALEK: Yes.

COMMISSIONER LINDWALL: Would you care to say which one?

MR MALEK: Qantas.

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COMMISSIONER LINDWALL: Yes. Okay. Now, what was the most recently signed agreement apart from - which is the most recently signed agreement?

MR MALEK: So we currently have two agreements, one is a runway agreement which spans 11 years. The price was reset in 2017 and another price reset is coming in 2021, with expiry in 2023. The terminals agreement actually expired in December 2018, so that's the most recently agreed.

COMMISSIONER LINDWALL: All right. Now, you did touch on obviously international charges and quality of service, so I'll the latter first. You do rate very highly on quality of service from – as measured by passengers, but less so the airlines. We've been told by other participants that the Quality of Service Rebate Scheme covers a narrow range of issues and the airports that place commercial accountability because the rebates are factored into the higher prices to airlines.

How do you try to meet the demands and wants of the airlines and improve the service for airlines, in other words?

MR DE GRAAFF: Well, to be really honest, I don't recognise the comments made about quality of service for airlines, because we have continuous discussions with airlines about quality of service through our airline operators' committee. I think for airlines as well as passengers, because we have before us a very good service, well, excellent service. So we were a little bit surprised about those comments made.

The fact of the matter is that we have a very peaky demand for the use of our facility, so in the morning peaks there is quite some activity, there's a little bit of congestion, especially in the government-managed areas of the airport, and there we're working together with the airlines to improve throughput and the quality of service.

MR MALEK: I'll also elaborate on that. As part of the most recent negotiations for the terminals agreements we've worked quite closely with BARA, who represents the international carriers, on adopting a service level agreement and KPI framework. That again will draw to the fore - a baseline of certain service levels, that airlines and airports can work collaboratively together on to ensure and agree where capacity is required, but also keep to account not only the airport operator but also the airlines. So that certain behaviours are enforced - to ensure check-in desks are clean, on time performance is maintained, and if the – and of course, if one carrier is late, the challenge of course is then getting that airline off the gate to provide access for the incoming one as well.

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COMMISSIONER LINDWALL: So in other words, the agreements have some incentives, or this is your desire, that you perform to a certain standards and that the standard is agreed with the airlines and measured against that standard.

MR MALEK: That's correct. At this stage there are no monetary incentives, or penalties, so to speak. We have a 12 to 18 month transition period to determine whether or not it is working. Currently at this stage airline operators have not raised major concerns, so therefore we'd like to see a transitory period of testing this KPI and SLA framework and therefore agreed to revisit penalties at a later date.

COMMISSIONER LINDWALL: And therefore quality servicing. How about we move on to what we started with in Sydney Airport about negotiate arbitrate. Could you – I won't go through the same type of questions, but it's more about what would you see the impact of it, how would you see it operating, what would it do to your investment strategies, do you agree with what Sydney said about it leading to gaming and, if so, how would that be manifested, that type of thing?

MR DE GRAAFF: Yes, I think we're very much looking at this topic in the same way as Sydney Airport Corporation is doing. We don't see a need for arbitration and especially negotiate – arbitrate regulation, because we've always been able to reach agreement with the airlines. The 21 years of history by the organisation proves that in the end airlines and the airports are able to work it out and come up with an agreement that works well for all parties involved.

COMMISSIONER LINDWALL: Is that one that you mentioned before?

MR DE GRAAFF: Well, that's still a work in progress. These negotiations, and there was an earlier question from yourself, these negotiations are very complex and very difficult. To give two examples of that, in this particular contract we're talking about right now, one of the most complicated pieces is that our domestic terminal lease has expired at the end of last year, so we are taking back those parts of the domestic terminal that were managed before by Qantas and Virgin, and there is quite a bit of work to do to get them up to the standard we require, as we call the Brisbane Airport standard.

While we're negotiating with those airlines who's going to pay for what and the break in the trend we had over the years. So we need to understand the airport capacity, the quality of service, but also the issue of the building and the quality of the facilities, to be able to decide what the appropriate

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level of investment is. So that's what we're working for, and as David already indicated, with one of those airlines, we leased agreement, and with the other airline discussions are still happening, but it requires a little bit more time.

COMMISSIONER LINDWALL: Anyway, go back to negotiate arbitrate then, yes.

MR DE GRAAFF: Yes, so I think we've always been able to reach agreements and I agree with Sydney Airport Corporation that there's currently an incentive to reach agreement, that won't be the case with arbitration in place. And there's risk for gaming, as I agree with Sydney Airport Corporation. And once more, I think especially the knowledge and expertise required to make a decision is incredibly important because you need to understand the history, complexity and in-depth knowledge of the capacity and operation of the airport to do so.

So that requires time and I'm saying the current negotiations take a bit of time as well, but if it's third parties going to – to be part of that, it will even extend that timing. So we believe that the current system is working and will resume should it be necessary to again reach agreement with airlines.

COMMISSIONER LINDWALL: So do you agree with Sydney that there would be likely to be gaming of the - - -

MR DE GRAAFF: Well, there could potentially be gaming involved in having an arbiter, but I'm not saying that it's going to happen. But there's potentially that risk.

COMMISSIONER LINDWALL: But what about the other side which says that there's been interest for the east coast gas market and after 18 months there hasn't been any arbitration, it hasn't gone to arbitration, that in the end they've all settled, the agreements have been made, and each party have been satisfied.

MR MALEK: Commissioner, that's a good question, but our view is similar to the thoughts shared with Sydney Airport. The challenge is these are very different markets. I mean, for us the complexity of having 29 carriers in agreement, some of them who are low cost carriers, some are international, some have a much larger presence at the airport. So therefore the complexity of that is quite challenging.

But also in terms of the gaming element, I think for us it's – given the different needs of the airlines, whilst they are common user facilities, there are some things that airports do for specific airlines and commercial

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agreements are reached with them specific for certain developments regarding gates, facilities, operating procedures and the like. Having overlaying that an arbitration and negotiation framework potentially defuses the negotiation tension, whilst it is over a protracted period, by having something at the end of it potentially leapfrogs that process, and if the arbitrator makes a call for a particular airline, that potentially has a flow-on impact to other airlines who of course have different needs.

COMMISSIONER LINDWALL: How do you visualise or consider the National Access Regime of Part IIIA as a restraint or a threat or a - - -

MR MALEK: Well, we believe it's a very credible threat, that framework has been in place really since inception, since privatisation of airports, so we see it as a very credible threat. As is the price monitoring regime looking at whether or not airports are making excessive profits.

COMMISSIONER LINDWALL: But isn't the A4ANZ proposal simply just skipping the declaration phase of the Part IIIA? Is there anything else that's different from what you – how it panned over the Part IIIA do you think?

MR MALEK: We'll take it on notice, but I know there's a fair amount of substantial input from the AAA industry body of the airports and the submission.

COMMISSIONER LINDWALL: No, that's all right. Shall we move on to the international?

COMMISSIONER KING: Sorry. Yes, just before we do that, Sydney Airport mentioned that they had on occasion used outside conciliation or arbitration during contract negotiations. Has Brisbane Airport, to your knowledge, ever used similar conciliation or arbitration during your contract discussions?

MR MALEK: So I can speak to this. Thus far and as agreed on our lines, we've actually reached the negotiated outcomes with all of our agreements, however, in that price reset in 2017 runway agreement, we actually have a dispute resolution clause, which states there is a list of key experts or specialists for both parties to exchange and agree. Now, we actually went through the process and we actually found commercial resolution prior to actually engaging an arbiter, or a mediator, to go through the prescribed process. So yes, we have sought extra assistance through a process.

COMMISSIONER KING: Because it does lead very much - - -

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COMMISSIONER LINDWALL: I just want to very briefly then look at the AAA BARA approach of having boilerplate clauses and having Government in there. Again, can I put to you the same questions I put to Sydney Airport, I can see potential benefits of that approach, except I don't understand why the AAA and the BARA approach seems to feel that they need to have a Government department or some other Government representation when establishing those boilerplate agreements.

Are you able to enlighten me on that?

MR MALEK: Yes. As far as the most recent negotiations for the terminals agreement, we have worked extensively with the airlines, and in particular BARA, on standardising our contracts. Again, across the network we understand the agreements are quite different, so we're very supportive on doing that, and believe that could progressively happen over the course of a number of negotiations or price resets.

We would have to take it on notice, I don't recall the recommendations for a Government intervention, I think more so oversight from the perspective of price monitoring and - - -

MR DE GRAAFF: Yes, and I'm going a little bit further with your answer, I think we appreciate standardisation of contracts, and I think that's in the benefit for all parties involved, provides transparency. I don't think this industry needs the Government to be part of that, I think we're perfectly capable of working that out ourselves and, what David already indicated, that we're trying to standardise clauses as much as possible.

But although we're providing common user facilities, it's not one size fits all, there's always differences in what certain airlines require and others don't, so we need some flexibility in our contracts as well.

COMMISSIONER LINDWALL: Which is why you're reluctant to (indistinct).

MR DE GRAAFF: Yes, but they're not significantly or substantially different but with the clauses that - - -

COMMISSIONER LINDWALL: They basically have a number of common clauses and then you have targeted things.

MR DE GRAAFF: Absolutely.

COMMISSIONER LINDWALL: Now, could we move on to the international again and gold plating, claims that the airport might be gold

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plating some of the infrastructure. Of course, you've also got the pre-finance thing of your new runway. Now, we go across to some regulated industries, such as electricity in New South Wales has been gold plating of transmission (indistinct). Would you accept the claim that there's been some gold plating of investment at Brisbane, and if there hasn't been, how could you justify that there hasn't been any?

MR DE GRAAFF: Well, I strongly disagree with the fact that there's gold plating happening in Brisbane. Yes, we provide a high quality operation, high quality service and high quality products to airlines and passenger customers, and that's how we like it to be. But everything that's been provided in terms of infrastructure and all the products and services are based on consultation with the airlines, and there's a very thorough process defining what investment levels are and what products – what infrastructure would be delivered throughout our investment plan.

So that's not gold plating, that's an agreement between airport and airline.

COMMISSIONER LINDWALL: So given you actually did, hypothetically, gold plate it, you're saying that you wouldn't be able to pass that cost to your customers, they would have to bear it themselves.

MR DE GRAAFF: Well, I think ultimately our investment program is something that is based on thorough consultation and negotiation with airlines. So I disagree with whether we're gold plating it. I think we both agreed that a high level of service is essential for a customer at Brisbane Airport, especially because we compete with airports all over the world, nationally, we complete with airlines in the nation, but also locally and, as you know, we share some customers with a few other airports.

So there's no incentive to gold plate or to drive costs up, because I believe that would lose customers to those other airports.

COMMISSIONER KING: Can I just clarify? So the upgrades that you did to the international terminal and the other investments for international carriers, they were made with the agreement of the relevant carriers or how did that work?

MR MALEK: So, Commissioner, actually the process that we've gone through to give you an outline - is through consultation. The final agreement reflects the agreed projects that actually do go into the underlying asset base. The price path that's generated from those reflects the capital program of existing assets but also a prospective new investments in particular for the international terminal and associated infrastructure.

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COMMISSIONER KING: Can I just follow up one of the things you actually said on the domestic side of it, which I'd just like some more details on. You said you've taken back the relevant domestic terminals, but they were not up to standard and you mentioned, I think, the Brisbane Airport standard. Presumably those terminals were satisfactory for the carriers before they handed them back to you, so how do I interpret your statement there, other than being that you're about to gold plate the domestic terminal?

MR DE GRAAFF: Well, that's a bit of a trick question, I have to say.

COMMISSIONER KING: I need to understand your points.

MR DE GRAAFF: There was no incentive for the two major airlines operating in the domestic terminal to invest in the last few years of their lease agreement, so we believe that they've waited until we took over and that means that together with the airlines and in consultation with the airlines we're investing currently in very basic things like redevelopment of one of the areas for about $40 million, we're fixing up the bathrooms, carpet, seating, those kind of things.

So although perhaps the airline thought it was acceptable, we both agree there's room for improvement.

COMMISSIONER KING: So just to clarify, so it was that end of terminal lease you think that led to them running down the asset?

MR DE GRAAFF: Well, I can't talk for the airlines, but I think, reading between the lines, you could read what my personal opinion about that is.

COMMISSIONER LINDWALL: On the international charges being relatively high, your explanation is that there's been a significant amount of investment and it's all lumpy. Does that mean that in five or so years' time if you were to repeat this analysis your – the international charges are more likely to be in line with the other airports?

MR DE GRAAFF: Yes and no. When you look at our international charges, the terminal share of those international charges is actually more or less flat over the years, for the last eight years it has been flat, and that means that the terminal investments were absorbed in that charge by the increase in volumes. The increase in our international charges are driven by the new runway, and as you know we started the development of that runway in 2013, and we're still investing. So that part of the international charge, the runway share of that is still increasing.

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COMMISSIONER LINDWALL: That will go up.

MR DE GRAAFF: And there's no better example of one view of investment in the runway, because from the day we're opening, it's not going to be fully used, and that's pretty obvious that it will take us 25, 30 years. So that's one of the examples that we've seen.

COMMISSIONER LINDWALL: And your new runway is particularly expensive given the geology of the area.

MR DE GRAAFF: Yes, well the land where the runway is being built has the consistency of toothpaste, so we needed I think 12 million cubic metres of sand, initially this had to settle for three years, and this was financed by Brisbane Airport Corporation. We only started the real construction of – we started the project in 2012, with only starting the real construction of the runway about 18 months ago. We still have about a year to go before we can use it. So all in all, it's almost a cattle prod project that's 10 years in the making from the first dollar spent to the last dollar spent.

COMMISSIONER LINDWALL: Shall we move onto a different topic. Landside access. Now, as you know car parking, access to your terminal by taxis and off airport car parking and so on, how did you determine those agreements and what kind of price? Some people would say they might be too hard and parking's too expensive, that type of thing. How would you justify it?

MR MALEK: Sure, I can talk to that. Just in terms of landside access at Brisbane Airport, I might just speak to the composition of it - they are different across all airports. Given the vast road network that we've invested in over the past decade, we have a much higher percentage of drop off, there is lack of congestion, so its closer to 60 per cent at Brisbane Airport.

In terms of ground transport operators, we have close to 17 per cent. Air Train, which is our train operator, is actually a much smaller percentage than some of our southern airport peers - at 8 per cent. With the balance of course being parking and other operators in the airport.

In terms of how we determine pricing for access - in 2013 Brisbane Airport went through a process of changing our access charging regime, which went from a charge – an access charge for operators irrespective of volume. Given the vast road network and, our obligation to ensure that we provide all people that access to the airport from transfers, pickup and drop off area at the terminal face for passengers, we changed our charging regime to

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focus on the number of the vehicles, vehicle type, as well as length of stay. The pricing regime that was rolled out in 2013 and has escalated predominantly by CPI. All of our operators have signed up to and agreed to the charging regime.

In 2018, we actually did have a slight increase - really to then standardise the charging framework to be in line with where taxis are. The operators on airport do have standard forums, which meet on a quarterly basis or annual basis, to raise any concerns. In the contracts, they do have – sorry, whilst there's actually no dispute resolution within contracts, we do formally engage with operators to escalate issues internally and, of course, they go externally if and when required.

COMMISSIONER LINDWALL: Did you have anything on landside access?

COMMISSIONER KING: No, I think at the time I wouldn't mind changing the schedule.

COMMISSIONER LINDWALL: Yes, go ahead. Well, I think we'll move onto jet fuel given the time.

COMMISSIONER KING: So just to clarifying background a bit, Brisbane Airport, your fuel throughput levy; that's no longer in existence?

MR MALEK: That's correct, Commissioner. That ceased in 2011, I believe, as the throughput levy.

COMMISSIONER KING: Why?

MR MALEK: That predates both Gert-Jan and I so I won't - - -

MR DE GRAAFF: No, I was there.

MR MALEK: He was there, yes, sorry.

MR DE GRAAFF: No, we came to another commercial arrangement with JUHI and so that's the one and only reason to simplify things.

COMMISSIONER KING: So from the airport's perspective was the fuel throughput levy was part of a – was it JUHI charge or was it - - -

MR DE GRAAFF: It was, yes, it was a JUHI charge. It was not significant in the scheme of things so we tried to simplify the relationship

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between the airport, the JUHI operator and the oil companies that are part of the JUHI. So that's the reason why we decided to get rid of this charge.

COMMISSIONER KING: On the JUHI structure you have the jet fuel companies obviously owning or controlling I should say some critical airport infrastructure. We've had complaints from the airlines that this is leading to overpricing for jet fuel in Australia and you'd be aware of BARA's information that they've provided to us and it was in our draft report. What's Brisbane airport's view on the JUHI arrangements that you have? Do you feel that that's leading to be an appropriate level of pricing of fuel for the airlines or do you think other action is needed in that space?

MR DE GRAAFF: Yes, well, BAC understands that the JUHI arrangements are effective at Brisbane Airport. So we're not aware of any issues regarding the access to the supply chain, nor the cost of the JUHI operation. We've got several leases and licences in place to allow JUHI to operate and provide services at the airports and it's a commercial agreement we have with them. We don't own any of the infrastructure. That's all owned by the JUHI organisation. But if JUHI wouldn't invest in the infrastructure based on our contracts, we could step in at any time and do that ourselves and so that's what we have in place.

But at Brisbane Airport, historically we never had real issues. Well, there's enough fuel storage capacity which is usually critical issue at airports. JUHI is actually investing based on their contract in more fuel storage capacity and, again, we are not aware of any issues with regards to pricing at Brisbane. We've got a pretty good arrangement with multiple oil companies being part of JUHI and with access to the JUHI infrastructure.

COMMISSIONER KING: So just a follow up on that last point. So you're happy with access to the JUHI infrastructure; do you mean third parties getting access just to provide jet fuel?

MR DE GRAAFF: As far as I know that's possible. We recently had a biofuel pilot and it's a good indication that a complete alien partner by the way supported by Virgin and Brisbane Airport Corporation had access to JUHI installation to use the infrastructure for biofuel capacity.

COMMISSIONER KING: We have heard that there were a few hiccups, if I can put it that way, in that access arrangement and getting that fuel.

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MR DE GRAAFF: Yes, well, and that's a fair point and biofuel's an innovation; it's new. So the concerns were predominantly about safety. When you put biofuel in your hydrant system it mixes with everything else, so you cannot say, "Well, this one single aircraft, I prefer had biofuel (indistinct) all the others." So we had to convince all the users of the hydrant installation that it would be a very, very tiny point of the fuel that would be tanked would be biofuel.

COMMISSIONER LINDWALL: But my understanding was that Virgin Airlines was quite satisfied. Since they're the ones operating the planes, one would think they had a better idea and, in fact, a greater desire to ensure the security and safety of the fuel than even a fuel company since they're the ones actually very exposed if something happens.

MR DE GRAAFF: That's correct. Yes, no, that's correct.

COMMISSIONER KING: Well, to put Paul's point the other way around, we know in other infrastructure such as gas pipelines, which seems to be coming up a bit today, that claims about substandard quality can and have been used to prevent access. It's an easy way for incumbents to say, "Ah, well, we can't give you access," substandard product and it comingles with the existing product safety problems. Does Brisbane Airport have any concerns that, whilst obviously safety is a pre-eminent issue that it can be used by JUHI incumbents by the fuel companies to prevent competitors in?

MR DE GRAAFF: No, as I said before, I'm not aware of any issues with regard to the JUHI operation at Brisbane Airport, nor did I receive any claims or remarks about it from our airlines.

COMMISSIONER LINDWALL: Okay, well, given the time, we've got a couple of things quickly. To what extent do Sydney Airport's regulatory constraints affect travellers to and from Brisbane Airport?

MR DE GRAAFF: Well, Brisbane Airport on-time performance has been traditionally very high, except in the year 2013 when we dropped below the 80 per cent on-time performance. But on average, on-time performance at Brisbane Airport is between the 82 and 85, 86 per cent over the last few years. In February of this year we were close to 90 per cent on-time performance. So that's a very good result.

The most important reasons that we're not closer to the 100 per cent is weather. But the second one is the knock-on effects of capacity constraints at Sydney and Melbourne Airport. If their on-time performance has been hit by either weather and any other reasons, we see

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knock-on effects at Brisbane. So the lack of service recovery opportunities at Sydney Airport will have an effect on Brisbane as well.

COMMISSIONER LINDWALL: Going back to the commercial negotiations, you used the building block method. Why?

MR MALEK: The building block methodology is, in essence, something that's been known by airports and airlines since privatisation. It really is something that is used for the basis of pricing discussions. It starts with the capital plan, the operating costs and all other variables that are actually put into it. However, that is only the basis for pricing discussions as there's a lot more that all leads to - - -

COMMISSIONER LINDWALL: But let's say that you decided, "Well, we're going to move away from the building block methodology and we're going to set prices a different way, with different quality standards," how do you think your airline customers would think about that?

MR MALEK: Commissioner, the - - -

MR DE GRAAFF: I think the airlines are predominantly interested in what it means for the outcomes of the other calculation. I think the methodology as such might be less important. I think the good thing about the building blocks methodology is that there's history, there's trends, there's knowledge being built up, there's like for like comparison with before. So I think that's a strength of the system.

COMMISSIONER LINDWALL: Anything else you want? Yes, one other question, just a final question about car parking. We did say in our draft report that the underutilisation of the car parking might be indicative of the exercise of market power, since it'd be high prices. Do you want to comment on that in particular?

MR DE GRAAFF: Yes, well, we have included quite some space in our supplementary submission on car parking utilisation because you raise the low utilisation and relate it to possible use of market power and what we believe is that the average occupancy of our car parks is not a very good indicator of the actual use because of the increase, for example, the night and we don't do that much short term parks at night.

So we think the peak utilisation is a better indicator of how well the car parks are used. We included an overview of those peak users in our submission and you will see that we actually, for all of our car parks, have peak utilisation of well over 50 per cent and fewer car parks are reaching

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or actually exceeding 100 per cent. And that means, for example, that from our international car park we're actually actively, during peak seasons, move cars. So our valet operation remove cars from that car park into another car park to make sure we've got enough capacity in our international precinct.

So I think they indicate that peak use is much more important and our peak use of the car park is very high.

COMMISSIONER LINDWALL: All right.

COMMISSIONER KING: Sorry, just to clarify on that. So you actually use -valet car parking enables you to have more flexible use in peak periods of the car parks?

MR DE GRAAFF: Yes. We use our valet operation to relocate cars and park them in other car parking precincts.

COMMISSIONER LINDWALL: Well, yes, David, thank you very much for seeing us.

MR DE GRAAFF: Thank you.

COMMISSIONER LINDWALL: Thank you. Now, could I invite John Clarke to appear, if he's here, for the Sydney Airport Community Forum? Hello, John.

MR CLARKE: Hello. So I'm not actually appearing of the Sydney Airport Community Forum.

COMMISSIONER LINDWALL: Yes, that's fine.

MR CLARKE: I'm a long-standing member of the Sydney Airport Community Forum.

COMMISSIONER LINDWALL: Well, if you could identify yourself for the record and perhaps give an introductory statement that would be fantastic.

MR CLARKE: So I'm John Clarke. I'm here appearing as an individual, not as a member of the Sydney Airport Community Forum. But I have been a member of the Sydney Airport Community Forum since its inception in 1996. So I'm here to talk to you about the regulation Sydney Airport as it relates to aircraft operations and in particular about aircraft noise pollution on the residents of Sydney.

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To borrow a real estate saying, in Sydney it's all about noise, noise and noise. You only have to look at the press that followed the release of your draft report and the view of that in Sydney. It was all about the impact of those operations and what that was going to have on people.

Now, I'm not going to rehash my written submission; I assume you've read it. But I do want to just run through a couple of the, sort of, key points. So the first one is that you need to consider the impact on people. The Commission's draft report in my opinion was grossly inadequate. It showed little understanding and little knowledge of the background of the regulations or indeed any regard for the impact of aircraft noise on the residents of Sydney.

It really just regurgitated the views of Sydney Airport and the industry which seek to benefit from the relaxation of any regulations. You need to understand that this is not an academic exercise. That aircraft noise has a very real and personal impact on people. It affects their physical and psychological health, their amenity, their ability to productively go about their day and their general well-being.

To understand the impact of aircraft noise in Sydney on the people, you need to read the 1995 Senate Select Committee on Aircraft Noise report which is called 'Falling on Deaf Ears'. I have provided a copy of that. So basically following the huge public outcry with the opening of the third runway and the operational changes, there was a regulatory regime that put into place three things. And those were: the Long Term Operating Plan for Sydney, in order to share the noise; the Sydney Airport Demand Management Act of 1997, which was to put a definite limit on the number of aircraft that could cause aircraft noise in any one hour; and, the Sydney Airport Curfew Act, which was to protect the ability of people to sleep free from aircraft noise. Now, these regulations are a necessary consequence of the airport's location 8 km from the centre of the city and the impact that aircraft have flying over tens of kilometres of suburban Sydney, impacting hundreds of thousands of residents, some of whom experience in excess of 400 aircraft a day.

Now, the question is, are the regulations working as intended? The Productivity Commission makes the point in its report that it assesses regulations as to whether they're fit for purpose. And it says, "Any regulatory regime should achieve its intended objectives and do so in a way that is targeted and proportionate to the policy problem.

Well, the policy problem is aircraft noise pollution. The Demand Management Act, in particular, is intended to draw a line in the sand to

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recognise that a major determinate in annoyance is the number of noise events and it seeks to put a limit on that. In fact, you only have to read the Act itself to understand that, because it actually states its purpose. It says, "This act is to provide for the limitation of aircraft movements of Sydney Airport, otherwise than during curfew periods." I mean, that is its purpose.

Similarly, the curfew is intended to allow people to sleep. It provides very strict limits on the number of aircraft and the type of aircraft that can operate during the curfew period. So it's quite wrong for the Commission to suggest that the existing movement cap and curfew are not targeted at noise outcomes directly. They are.

It's similarly quite wrong to suggest that the balance has not been considered when these regulations were put together. They certainly were. In fact, the cap and the curfew regulations are working as intended. And I think it's a bit rich for the airport and the industry, who until recently have lobbied very strongly that we didn't need a second airport in Sydney, to now start complaining about capacity problems at Sydney.

If anything I think I would argue that the cap indeed allows for too much capacity at Sydney Airport, such that the third leg of the regulatory regime, The Long Term Operating Plan, is failing to meet its noise objectives -fairly sharing aircraft noise. Because basically the demand is such now, being close on 350,000 movements, that it's resulting in the noise sharing modes as they're known being used much less, and an over-reliance on the parallel runway operations.

So in fact, the balance of regulation in my opinion, and in fact in the opinion of many others, is far too heavily weighted in favour of the airport and the airlines.

Now, of course, one of the reasons we have economic regulation is due to market failure. And the problem here is that there's no cost to the airport or the airlines for the aircraft noise pollution they cause.

Aircraft noise is a 'free good' to be consumed at will. There's no cost to the airport or airlines. The people impacted are not compensated in any way. So the proposals put forward in the Productivity Commission's draft report are all about creating more airplanes, which equals more profit, but it also equals more noise. So it's not surprising that the airport and the airlines are arguing to increase the number of airplanes.

So there are a number of proposals in the Productivity Commission's draft report, such as: making the cap apply to scheduled not actual movements,

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spreading the measurement of the cap over a longer period, creating extra slots for regional airlines, and a curfew noise budget. But let's be very clear about all of those. They're not targeted at achieving noise outcomes. They have one purpose only and that's to increase the number of airplanes able to use the airport at a time when they want to use it. That's the sole purpose of those proposals.

The Productivity Commission puts arguments to change the cap to allow more aircraft to take off and land based on efficiency. But this ignores entirely the economic, social and health costs of the aircraft noise pollution on the community. And until these economic externalities as they're called, are properly costed, then discussions about the efficiency and the costs to the industry of meeting the current noise objectives are simply not valid. The cap and curfew are a cost of doing business in Sydney.

So, just in conclusion, the current movement cap and curfew are working as intended. They put limits on the numbers, types and times that aircraft can operate at Sydney Airport in order to provide some balance between the aviation industry and the community's health, welfare and amenity.

The airport and the airlines asking for more movements is not Oliver Twist asking to supplement his meagre rations by saying, "Please sir, I want some more." It is more like Augustus Gloop. Now, he's the obese kid in Charlie and the Chocolate Factory who wants to gorge himself on ever more free chocolate despite the protestations of those around him that tell him that he's had enough. That's the consequence of asking for more movements.

COMMISSIONER LINDWALL: Thank you, John. I mean, I think it's indicative of problems with noise, the fact that there's been considerable resistance over decades to the creation of other airports. I mean, by the people who live around where Badgerys Creek, the councils there for example, the – have been – had resistant (indistinct words) that airport.

MR CLARKE: Yes, of course.

COMMISSIONER LINDWALL: So I mean, that supports your case, but I mean, you did say that there's been no compensation. I thought there was a Sydney Airport noise insulation program.

MR CLARKE: There was. The Sydney Airport noise insulation project insulated a small number of houses, I can't remember – about 1000 or something and some churches and other public facilities under the 30ANEF zone. So only under the most extremely impacted zone at the

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end of the runways. There were also some houses that were bulldozed and knocked down. In fact, there's a complete suburb that no longer exists in Sydney. I can't recall its name – now, that's now been overtaken by the airport. But in essence, it was only limited and it was actually done as a levy that was put on top of the ticket price collected by the airlines and went into essentially a pool to pay for that insulation. And indeed, there was actually money left over and this just went back into consolidated revenue.

COMMISSIONER LINDWALL: What about, you know, you said that it's all about benefiting airlines and airports. What about the 69 million people who visit and travel to Sydney Airport? I think it's 66 million each year. Don't they count when the designers count as well? Shouldn't there be a balance that the fact that (indistinct) - - -

MR CLARKE: But isn't there a balance? Isn't there a balance? Isn't the fact that there's already 80 movements an hour a balance? I mean, that was way back in, you know, 1997, or '96, when the regulations came out. I mean, that balance was considered and allowed up to 80 movements per hour, needed in 15 minute - rolling 15 minute increments. It allowed for that, in order for that balance. The problem here - and it drew that line in the sand. It says "That's enough. There ain't no more." But of course, what's happened is in the absence of any action around the second airport, we've got closer and closer and closer to that figure, to the extent that, I understand, it's causing some inconvenience to the airlines, and potentially to the travelling public.

But you know, you've got to remember, every single aircraft flies over hundreds of thousands of people. As I said, there are some people, impacted in excess of 400 times a day.

COMMISSIONER KING: Can I just follow up on the 80 movements an hour.

MR CLARKE: Yes.

COMMISSIONER KING: I'm not aware of any cost-benefit analysis, or noise-based work that was done leading up to work out that it was 80, rather than say, 85 or 75, and in fact, as an outsider - I'm not an airport expert, but it almost seems like 80 was a fairly arbitrary number. Are you able to help me understand where that 80 came from. I mean, is it just arbitrary?

MR CLARKE: It's sort of arbitrary. But it's not. So, as I understand it, amongst other things, when the long term operating plan was done, they

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modelled the capacity and concluded that the parallel runways could operate, if I recollect correctly, 87 movements per hour. Now, the Sydney Airport will argue that it can actually operate more than that. There were people arguing that the cap should be less than - well, less than that. One of the problems is that the noise sharing modes, as they are called - so those modes that are the combination of the north-south, and east-west runways, in different combinations have a lower capacity.

But, probably of those - 14A, in fact, is probably the highest capacity, which is at about 75. The others max out at - at a lower capacity than that. So, I suppose 80 was chosen insofar as it wasn't 87, it was less than that, so it provided for a little bit of flex there, but indeed it was actually more than the noise sharing modes. So, there was a lot of discussion at the time about what that should be, the government concluded, for a number of reasons, 80.

COMMISSIONER KING: Was there any noise evaluation work that we can go back to look at, to understand better the 80 number from a noise perspective?

MR CLARKE: Not that I am aware.

COMMISSIONER LINDWALL: Are you aware - - -

MR CLARKE: (Indistinct) was a regulatory thing done by the - by the department, in support of - of the politicians that first was put forward as a private member's bill by Anthony Albanese, that then got picked up by the Coalition and was put forward by the Coalition at the time.

COMMISSIONER KING: Has anyone actually - as far as you're aware, has a government body or any other body actually done what I'd call the hard yards, for want of a better word, on actually measuring that. As heard you correctly say, it's an economic externality. Is anyone actually measuring the externality?

MR CLARKE: The 80 movements and the aircraft noise that is caused by that?

COMMISSIONER LINDWALL: And the cost of that to local residents?

MR CLARKE: Well, no. No one has ever thought to cost that for the local residents. There's no - no one has ever done the economic analysis for that. Associate Professor Ernestine Gross, who was at the Macquarie Graduate School of Management did write a paper, in the, mid-90s. I

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know Ernestine Gross, but I haven't seen her for some time. I may be able to get a copy of it. She wrote a paper that did look at - at some costs, and essentially creating a potentially a compensation regime around this. She is an economist.

To be honest, at the time I was opposed, because my view was, we just need to get rid of the problem, not compensate people for it. I think, you know, 20-odd years after the event, I think she was actually, probably right, and I'll - you know, I'll tell her that when I next see her. Because, you know, because it's led to this current situation. If I recall correctly, she basically - her paper essentially looked at the fact that the RMS, or whatever they called themselves at the time, Department of Main Roads and Transport, that they have an economic model for the cost of traffic, you know waiting times for traffic, and they costed essentially what that waiting time was, and she applied that to the duration of noise events, and said, well, you know, here's at least some dollar figure, to be allocated to - to that.

That is, to the best of my knowledge, the only economic analysis that's been done on that. But I mean, you know, if you wanted a cost, you'd need to cost the loss of amenity, property values and health consequences, and all of those other sorts of things that actually result from the impact of aircraft noise on people.

COMMISSIONER LINDWALL: When, obviously since the creation of the runway, there's been an increase in the number of planes.

MR CLARKE: Correct.

COMMISSIONER LINDWALL: But hasn't a lot of planes actually become quieter over time? So, you've had an increase in number, but a reduction in the noise per plane?

MR CLARKE: So, firstly around the increase in number. Around 1995, the number of aircraft operating in Sydney was 262,000. And last year it was, for all intents and purposes, 350,000. So, you've had a very significant increase in the number of aircraft. There is essentially what's called - what's being known as the quiet plane furphy. There's no doubt, planes are getting quieter, and I absolutely endorse that. But they're not that quiet. I mean, there is no such thing as a quiet aeroplane, and so, you know, that an aircraft that is three, four decibels quieter when it's measured in ideal conditions, doesn't actually translate into a great benefit to the community.

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Three decibels is considered about what is just perceptible by the human ear, right? In terms of a change in noise. So, you know, the reality is, if you're getting a three or four decibel reduction, it's barely perceptible. Despite the fact that, you know, from a noise measurement point of view, in terms of measuring noise pressure, that's a very significant change in the noise pressure. It's actually not a very significant change in the perception of noise. The other thing about it, to remember, of course, is that, you know, these aircraft are causing noise just not as a result of their engine noise, there's also air frame noise.

You know, you can hear the change in the noise of an aircraft when it puts down its wheels and the flaps. You know, it's quite distinct.

COMMISSIONER LINDWALL: I think you said that we've been - you didn't liked our recommendations, but we didn't actually make recommendations - - -

MR CLARKE: Your conclusions.

COMMISSIONER KING: We never have argued that the curfew should go. We've not argued that there should be an increase in the cap as far as I remember, but could I - - -

MR CLARKE: But that's a consequence of - I mean I'm not saying you argued - I'm not saying you're saying that the curfew would disappear. I'm saying you'd loosen it. You want to loosen the regulation.

COMMISSIONER KING: Well, let's explore that a little bit, because I mean, some people would say that in Sydney, noise regulations are stricter than any other airport in the world.

MR CLARKE: Yes.

COMMISSIONER LINDWALL: Airports like Heathrow which are surrounded by many more homes than Sydney, and they have a form of restriction, of course, on airport noise, but it's less inflexible. Why shouldn't it be a bit more flexible? Now let me give an example.

MR CLARKE: Yes.

COMMISSIONER LINDWALL: Technically, the period is in curfew where there are, I think, (indistinct) planes, or BAe-146 planes, which I've been told - we've been told are noisier and smaller, and that Australia Post testified in a meeting, or told us in a meeting, that they would prefer to have fewer planes, say a 737, which they say is quieter. So I would have

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thought some mutual gain. You get fewer movements in the curfew period, and it's quieter.

MR CLARKE: So as I - said in my submission, and I know as a member of the Sydney Airport Community Forum, I will be quiet happy to endorse, you know, reviewing the types of aircraft that operate during the curfew more frequently to enable quieter aircraft to be used. I'm not suggesting otherwise. My issue is not - is not the review of the type of aircraft. My issue is, you know, increasing the number, allowing more aircraft to operate in that curfew period. You've got to remember that curfew period only operates for seven hours. The World Health Organisation recommends that you get between seven and nine - an adult, gets between seven and nine hours of sleep.

So, the reality is, you know, even if the last plane flies over at 11 o'clock at night, you know, it's probably 10 or 20 minutes until you get to sleep - you're not getting seven hours' sleep. That ignores, you know, children, the elderly, and teenagers who might actually need more.

COMMISSIONER KING: Well, on another subject then, we've received a submission, and the gentleman's appearing later today on this, from the Australian Business Aviation Association who says that they would like business jets to be able to operate more freely during the curfew period. What would you say to that?

MR CLARKE: I've got a problem with it, because you know I mean the reality is there's a whole lot of people in Kurnell who get woken up several times a night by aircraft flying over them, so the idea of putting another aircraft over people and waking them up for the convenience of some businessman who wants to land in Sydney Airport at 2 o'clock in the morning, I don't think is good policy.

COMMISSIONER LINDWALL: What about in terms of – so we're speaking about during the curfew period for like the Australia Post example. What about increasing the flexibility during the normal operational period. Now, the 80 movement cap, for example.

MR CLARKE: Yes.

COMMISSIONER LINDWALL: Couldn't there be some mutual gain where that shrinks by a little bit and yet you can allow flexibility so some hours might be more than 80 but some a lot less, and wouldn't you get the total noise as less because of fewer movements.

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MR CLARKE: But I mean the problem is that's not going to happen. I mean, the Sydney Airport has been expanded incrementally right? You know, it's death by a thousand cuts.

COMMISSIONER LINDWALL: (indistinct) has been (indistinct).

MR CLARKE: So what are you saying? We should say, "We'll let in 85 here because that's going to mean that at another time it reduces from 75 to 70," or "from 80 to 75" or whatever that number actually is. What will happen is very soon that will be taken up by somebody else.

COMMISSIONER LINDWALL: Why do you suspect that since it hasn't happened in 25 years.

MR CLARKE: But of course it's happened. That's why we've got 350,000 movements.

COMMISSIONER LINDWALL: But that limit has been set in stone for all period so I don't see – - -

MR CLARKE: Because, you know, what's happened is – - -

COMMISSIONER LINDWALL: The government sets a regulation which says, hypothetically, "We're reducing the cap from 80 to 78."

MR CLARKE: Yes.

COMMISSIONER LINDWALL: "But we'll allow a little more flexibility over the hours." Then by definition you've got less than 80.

MR CLARKE: So are you proposing to – so we'll reduce the cap to 75. Is that what you're saying? But we'll allow the measurement over – - -

COMMISSIONER LINDWALL: Well, where would you agree there could be more flexibility? Do you say 80 at the moment, there shouldn't be any flexibility. If you took it down a little bit, how much lower would it have to go before you would allow some flexibility?

MR CLARKE: Well, I'm of the view that the cap – and indeed, you know, you only have to look at the modelling undertaken for the Long Term Operating Plan where they modelled 360,000 movements, that in fact the way to get that is indeed to have a lower cap during the non-peak periods of the day, a cap that is set at a level to allow those noise-sharing modes to be used. Now, you might want to – I'm trying to think what that

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number might be, but, you know, 60, 65 should allow those to be used most of the time.

COMMISSIONER KING: So actually on the – - -

MR CLARKE: As long as there's an incentive that will also create an incentive for the use of the non-parallel modes, because at the moment it's really – there's no carrot and no stick to not use the parallel runways, right, so it's very easy when, you know, things are going on. "Well, I'm not going to actually delay that plane for another, you know, minute flying, you know, 100 kilometres off the coast. What I'm actually going to do is I'm going to change to parallels," right? And that happens today, all the time.

COMMISSIONER KING: So can I just follow up on that, because you say or you mention in your submission that current regulations work as intended, but then when I look at the Long Term Operating Plan, and you also point out that the percentage of movements to the north, the target on that, so the Bennelong funnel was a term sometimes used to the north of the airport. But those percentage movements haven't been met, so why do you think the current regulation is working well when you have targets not being met
for – - -

MR CLARKE: Well, as I say, within the purpose of the current regulation – the current regulation is 80, right? And in that respect it's working well. You know, it's actually putting a limit on the number of aircraft. Is it supporting that third leg of the regulatory regime? No, but, you know, the reality is that it is not required by law that the Long Term Operating Plan achieves targets. So, you know, I mean, regrettably they're aspirational targets. The Long Term Operating Plan was implemented by ministerial directive, but one of the points in there is that capacity isn't to be compromised. So essentially it allows the door to be opened and for those aircraft to be spread throughout, you know, the peak periods to enable, you know, 80 movements per hour, well outside of the peak periods throughout most of the day.

COMMISSIONER KING: So you've said that one way perhaps to help the targets be met would be to have a lower cap outside peak.

MR CLARKE: Correct.

COMMISSIONER KING: The body of course that in a sense runs the LTOP from a practical perspective is Airservices Australia.

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MR CLARKE: Yes.

COMMISSIONER KING: It's not the airport that decides which runways will be used.

MR CLARKE: Of course.

COMMISSIONER KING: So is there an issue with the incentives or the directives provided to Airservices Australia at the moment, and if so how do you think that should be changed?

MR CLARKE: Well, as I say, what I would do is I would provide a directive that said firstly that, you know, you have to use the noise-sharing modes, as they are known, in accordance with the priority as set out in the Long Term Operating Plan. You'll see that reflected every month in the Airservices Monthly operating statistics for Sydney Airport, and you'll see there's a nice table there that shows the hierarchy of modes, and so, you know, the idea would be was that you have to use the non-parallel modes during those times, you know, in that priority. So the only time you'd be allowed to use parallels would be as a consequence of weather, not as a consequence of capacity.

COMMISSIONER KING: Would that raise any safety issues?

MR CLARKE: No. No. Why would it raise a safety issue?

COMMISSIONER KING: I'm just thinking of how there might be pushback against it.

MR CLARKE: Well, I mean, the pushback will be that they want to land more aircraft. They want to take off more aircraft. That's where the pushback would be. So instead of spreading them throughout the day in a manner that allows those noise-sharing modes to be used, instead what you do get is you do get bunching, you get planes showing up or wanting to depart. You've got to take them off those noise-sharing modes into parallel operations. That is in accordance with the way the slots are allocated and the way the airport is regulated to operate today. I'm not suggesting otherwise. But the consequence of that is that those noise-sharing modes are not used and there's an over-reliance on parallels.

COMMISSIONER KING: So it's been suggested to us that the sort of flexibility that we've been talking about, having 80 for the cap spread across the day, will lead to more movements in peak and an associated lower level of movements off peak. So in some ways would that start

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actually achieving your objective? In other words, have we potentially got a win/win here of removing aircraft out of – - -

MR CLARKE: If you want to regulate – if you want to regulate, and I mean, you know, so that it's not optional, you want to regulate that there are less movements during other times of the day to enable those noise-sharing modes to be used, then I'd be all for it. But that's not what's been proposed, right? This is all about incremental growth. This is all about allowing more than 80 movements, at any time throughout the day. None of these proposals that were put forward in the Productivity Commission's draft report said, "Yeah, don't worry, we'll be happy. What we'll do is between 6 and 7 in the morning we'll restrict that to 45 movements an hour so you can use simultaneous opposite directions," which are the ones coming in and out of the Bay that cause really very little noise problem, right? "We're going to do that," right? But meanwhile at 9 o'clock we're going to allow you to do 85. No one is proposing that. What's being proposed is 85 at 9 o'clock in the morning, but we'll just keep 80 available between 6 and 7 as well.

COMMISSIONER KING: And this is your personal view. I understand that, but would you personally favour an approach that said, "Well –" or do you believe it would be desirable to do the sort of thing you just mentioned, which would be to say, "Well, you can have more movements in that peak, but the quid pro quo has to be explicitly less movements off peak," and that would actually – may or may not be desirable from the airport's perspective, I don't know, or the airlines, but that would potentially be a better noise outcome for the residents.

MR CLARKE: I think it would be, so long as it was regulated that there was a, and it's been put forward previously, a 'variable cap', and as long as it was regulated in such a way that the capacity – sorry, the number of movements was no greater than the capacity of the noise-sharing modes.

COMMISSIONER KING: Okay. If you had a variable cap type approach but there were weather events that led to delays.

MR CLARKE: Yes.

COMMISSIONER KING: And again, from your personal perspective, do you think it would be reasonable or desirable to build in some flexibility there? So, yes, if a thunderstorm happens to have come across and prevented movements of planes during the peak, then for that one day, there could be catch ups in the off-peak periods?

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MR CLARKE: To an extent. If you got - if what you - if what you are able to achieve was, you know, fair sharing of aircraft noise throughout other periods, then the idea - that has some merit to it, I can understand why that would want to be achieved.

COMMISSIONER KING: Yes.

MR CLARKE: But again, the point is that it can't be just aspirational. Noise sharing and a variable cap actually has to be regulated. Because at the moment, this is the problem. At the moment, there is neither stick nor carrot. Right?

COMMISSIONER KING: Yes.

MR CLARKE: For it to actually achieve the noise sharing objectives. Now, don't get me wrong, I'm not suggesting that Airservices are out there trying not to today- that is not the case, all right? But I'm just simply saying there is no incentive to achieve noise sharing objectives today, and that's a problem, because you're seeing the consequence in that on the people of Sydney.

COMMISSIONER LINDWALL: So, I do understand now that you're basically saying then, that you can perceive some flexibility, as long as it is regulated flexibility.

MR CLARKE: It's got to be.

COMMISSIONER LINDWALL: And that airports, obviously, as governments have to balance the needs of the people who are affected by the noise, versus other community members who want to travel to Sydney. But how do you see technologies at Airservices as deploying over time, like it's OneSKY, and so forth, with a change in (indistinct) eventually. Is there any (indistinct) to noise outcomes (indistinct) that?

MR CLARKE: Well, as I understand OneSKY, it's really about - and I don't have any particular expertise on this, but as I understand it, it's really about coordinating different air traffic control systems nationally.

COMMISSIONER LINDWALL: But it is also about how players move across the lanes, rather than the formal lanes they used to have.

MR CLARKE: Yes, but once they get - once they get into the, sort of, terminal airspace in Sydney, that's an entirely different issue. It's really that that's the concern there, you know? But they can certainly - aircraft flying at 10,000, 12 - 20,000 feet don't really create much of a

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disturbance. Aircraft flying at 3,000, 2,000, 1,000, you know, 300 feet, they're the ones - they're the ones that create the disturbance. One of those new technologies, Airservices are euphemistically calling "Smart Tracking".

Now, "Smart Tracking" - the real, proper name for Smart Tracking is a collection of technologies that come in under this umbrella, is PBN, Precision Based Navigation. All right, now, precision based navigation is - or, well, could, on the one hand be, very useful, because it allows the aircraft to fly very accurately within a wingspan, right? So, if in fact what it is used for, is keeping those aircraft over water, over non-populated areas, good to go. The problem is, that's not the way it's necessarily used. So, if it's used for example, for landings over the north of Sydney, then what you've got is, is you've got aircraft flying within a wingspan over the same houses every single time.

So, the concept of spreading them is the response to the issues that arose from the opening of the third runway. There were two aspects, one of them was a whole bunch of aeroplanes were put over areas- new areas. But the other one was, was that they made operating changes .They introduced the narrow flight corridors, which are concentrated corridors. And they became known as the Bennelong Funnel. So, instead of aircraft - in the old days, aircraft would basically come in quite close to the airport, they'd land, and were good to go. And what happened was that they - these aircraft were now pushed further and further north, and then came down in very narrow corridors.

Now, one of the consequences of the implementation of PBN to the north of the airport would be just that. You would go back to the concentrated flight corridors that were one of the first things that were disbanded, after the Coalition were elected in 1996.

COMMISSIONER LINDWALL: It could be that, or it could be in a different direction, it spreads it out more evenly?

MR CLARKE: Well, it - what do you mean by that?

COMMISSIONER LINDWALL: Well, I mean - - -

MR CLARKE: So, what do you mean by that? So, yes I mean - so, one of the - - -

COMMISSIONER LINDWALL: It should almost have individualised approaching patterns. Rather than the standard (indistinct).

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MR CLARKE: You could. So, one of the things that the Long Term Operating Plan recommended - well, one of its modes is what's called mode 10, which is landings form the north, and along with that was a procedure, called trident. Trident provides for multiple flight paths to the east and the west of the centreline for aircraft landing from the north. The problem is, trident has never been implemented, and one of the reasons that's constantly been put forward for that is that the technology is not there to enable it to be done, and that technology is probably a couple of things.

One of it is sequencing, and the other one is the ability to accurately direct all aircraft. Now, one of the issues, of course at the moment, is potential conflict with Badgery's Creek. And so, whether trident is ever able to be implemented with the airspace design for Badgery's Creek is an issue which remains to be seen.

COMMISSIONER KING: All right. Did you have any final points?

MR CLARKE: No.

COMMISSIONER LINDWALL: Can I just finally ask then, John, how do you see the community and Sydney Airport in 20 or 15 years? How do you envisage it, in terms of good outcome from - - -

MR CLARKE: Well, you know, I mean, there's sort of two views here. One of them is, you know, in reality is, in a great many first world countries, city airports have basically been moved, because - and, the land has been repurposed to higher and better use. Because the reality is that an airport is not a good use of real estate. That's the reality of it. The airport will bang on about all the money it brings to the economy, and all the rest, but that is not location dependent. You know, people still fly to Narita, in Tokyo, but it's still 67 kilometres from the outside of the city, right?

So, the airport and the city it serves, you know, they don't have to be, you know, close, geographically close, right? So, in, in an ideal world, you'd say, "Really, that land ought to be repurposed, it ought to go, you know to higher and better use," and away you go. Now, the problem is, is that there's a whole bunch of people out here who have a financial interest in its retention where it is. So, is that - is that likely? Probably not. I'd like to think it is. I mean, economically it's a rational thing to do. But politically, I don't know whether you'd get away with it.

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So, you know, the reality is that caps need to be put on and retained on Sydney Airport that enable it to exist in the manner that is not entirely destructive to the community, in fact it serves – (indistinct)

COMMISSIONER LINDWALL: I think that's the time, thank you.

COMMISSIONER KING: Thank you very much, then, John.

COMMISSIONER LINDWALL: Now we've got a little morning tea break, and I believe we're taking off at 11.55 with Qantas.

SHORT ADJOURNMENT **[11.37 am]**

RESUMED **[11.57 am]**

COMMISSIONER LINDWALL: So I'd like to welcome Qantas to speak to us. And I'd invite you all to introduce yourselves.

MR PARKER: I thank you, Commissioners. Commissioners Lindwall and King. My name is Andrew Parker, I am the group executive for government industry international and sustainability. I am joined today by my colleagues, a few of us, Rob De Bella who is the executive manager of finance, Matt Hudson who is the head of commercial airports, Moksha Watts, head of sustainability and industry affairs, Michele Laidlaw, at the end, the head of legal. Jackie Quang, our senior legal counsel and Rick West, our manager of airport commercial relationships.

COMMISSIONER LINDWALL: Before you go on, Andrew, could I say that when you all speak at various times.

MR PARKER: Yes.

COMMISSIONER LINDWALL: It's probably good to just say your name just for the transcript. But please, if you want to give an introductory statement, thanks, Andrew.

MR PARKER: Thank you. Thanks, Commissioner. We are perplexed and disappointed at how easily the draft report has, in our review, dismissed critical independent evidence, accepted airport claims without question and disregarded the everyday realities of air travellers and others who need to use our airports. To Qantas, this process and review has been about fairness. Is $6 for an airport coffee fair? Is $90 for airport parking

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fair? Is $34,000 to land and depart a Qantas A380 fair? And how is it fair that parking at an airport can cost more than the Jetstar flight itself?

And on this question of fairness, we would consider the statement of five years ago to be particularly pertinent. Privatisation without competition risks turning a public monopoly into a private monopoly. The owners may change but the public will get ripped off just the same. What is the second option? If competition is not possible, then the privatised business needs to be regulated so that it cannot exploit its market power. It's a fine sentiment from Commissioner King in 2014.

So it is a genuine mystery to us that the Commission now thinks that regulation in its mildest of forms of a privatised monopoly business is somehow unfair or unreasonable. And it is a shame in our view that the PC has essentially endorsed the exorbitant airport and car parking charges and green lighted monopolistic behaviour to the detriment of our passengers and the Australian community.

The enthusiastic endorsement by the Australian Airports Association in rejecting fair and reasonable reform to airport commercial behaviour for the sixth successive time should also provoke reflection and concern. To this end, Qantas is of the view that future reviews of airports by the Commission should be abandoned given their lack of rigour analysis and unfortunate predictability regardless of evidence or changes in the external environment.

And whilst the Commission states in its draft that it will consider regulation for more extreme examples of a clear abuse of market power in your final report, we remain sceptical. Hence our position that an expert open-minded body should assess this matter in future, in the future, or that parliament given the weight of evidence should directly legislate to government.

We believe also the Commission has ignored the abundance of compelling evidence provided to it by the Australian Competition Regulator, multiple airport users and credible experts, such as Michael O'Brien QC, Margaret Arblaster, Frontier Economics and the National Competition Council. These experts may be dismissed by the Airports Association, but consider their credibility versus that of a lobbying group.

And we believe the facts speak for themselves. The lowest car parking profit is earned by Perth Airport which more than 50 cents out of $1 spent goes in profit and 70 cents at Sydney. Airports earn 25 per cent more revenue per passenger in real terms since a decade ago and their margin is

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double the long-running international average. And meanwhile, airfares, best measured by best discount economy fares have declined 40 per cent.

Seven Australian airports charge hidden fuel throughput levies. A fee for no service extracting over $20 million a year from airlines and their customers. And nine out of 10 of the most expensive airports in the world for car hire are in Australia. And the number of airports, a number of airports are even brazen enough to profit from aviation security. Their public conditions of use assert the right to extract a return on their investment in security. In plain English, that means profit.

And don't just believe us. Consider their investors. Sydney Airport has an unregulated revenue stream in a monopoly environment. That was UBS last year. Ongoing myths, such as effective regulatory oversight exist today, profits by monopoly airports are reasonable and airlines have countervailing power, seem to be swallowed whole by this draft. And opportunities to uncover the truth of super normal profits have, in our view, been passed over. For instance, not determining airports cost of capital or their overall profit margin, is intellectually lazy.

Like drop bears and Lasseter's Reef, airline countervailing power is a myth. A tall story told by airports to distract from their monopolistic behaviour such as denying us the right to fly Johannesburg to Perth or holding our aircraft to ransom at Canberra Airport until a diversion charge eight times higher than other airports was paid by credit card.

In a fiercely competitive Australian market, airlines have almost no countervailing power. Network airlines like Qantas or Virgin cannot credibly threaten to withdraw their services. This can be demonstrated through a simple real life example at Newcastle Airport last year. The Qantas Group was forced to withdraw services from Newcastle due to pilot shortages. Frontier Economics found that Virgin was able to respond almost immediately to backfill this lost capacity.

Frontier Economics also looked at the relative cost faced by the Qantas group and Perth Airport from the threat of a withdrawal of a single daily return flight between Melbourne and Perth. It found that the airline would have more to lose, up to 10 times more than the airport because of Perth's critical importance to our customers, our broader network and operations. Reducing or withdrawing services in response to airport behaviour is simply not feasible and the airports know this. And which market will we give up? Is it Qantas to Perth? Is it Jetstar to the Gold Coast? Is it QantasLink to Tamworth.

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It deeply concerns us that the Commission has chosen to believe this fiction as fact and yet the Commission presents no evidence of countervailing power anywhere in its 367 pages. The Commission's suggestion that airlines can refuse to pay charges at the level determined by an airport when an agreement expires is to us extraordinary, as is the implication that the payment delaying tactics to Australian charges are a normal and adequate bargaining tool. These extreme measures are indicative of a broken system that offers airlines few options to moderate airport charges at reasonable levels.

The fact is, while negotiations were underway with Perth, the Qantas Group agreed to play – pay what we believe in good faith to be a fair and reasonable charge. And we continue to pay it. We ask Perth Airport to resolve the dispute through binding expert determination. They refused and yet our offer still stands. But instead we now face a long retrospective court case that will cost millions of dollars and destabilise that market.

As privately owned monopolies, Australian airports have the economic advantage of falling costs per passenger as output increases. But despite significant increases in passengers and freight from airlines, monopoly airport charges continue to rise well above inflation. And while Australian monopoly airports' revenue has soared 25 per cent over the last decade, airfares continue to decrease as a result of airlines focussing on all aspects of their cost space.

On this point, I'd like to briefly address the false claims perpetuated by the airports about the cost of airfares. The AAA claim there has been an increase in real domestic airfares over the last seven years. This is simply wrong. The reality is that real restricted economy airfares which have been used as the base of its entire argument, make up less than 2 per cent of airfare inventory sold.

In real terms, best discount economy airfares which is what the majority of economy passengers purchase, are 40 per cent lower today than in 2003. It illustrates the AAA's ignorance of competitive airline economics. The Commission and the AAA view that aeronautical charges make up only a small proportion of the total cost of an airline and that is wrong. Airport fees, levies and charges at as much as 20 per cent to the cost of an airfare.

In fact in some regional routes, airport charges are higher than fuel, aircraft costs or flight crew. So in conclusion, we believe the current regime of oversight is ineffective and gives Australia's privately owned monopoly airports carte blanche to increase airport charges and sting air

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travellers as much and as often as they wish. To call it light handed regulation is a misnomer. A more accurate term is non-regulation.

The ACCC has consistently argued price monitoring is not regulation. Monitoring alone is not enough to constrain the behaviour of airports with significant market power. And declaration under the National Access Regime is time consuming, expensive and difficult, if not, impossible. The solution: efficient and timely reform through deemed declaration of major airports and access to independent and binding arbitration are essential in our view to deliver true and effective light-handed regulation. As A4ANZ has pointed out, the advantages of such minimal reform include at least $445 m in net savings and efficiency benefits with a benefit to cost ratio of 14 to one. And like arbitration, the wider economy, parameters can and should be set for efficiency and fairness.

Arbitration is part of the aeronautical pricing principles. The Airports Association also say they can do better and want to talk to us airlines after the PC process has finished. This offer should of course be viewed with cynicism. Instead, while doubtful, we urge the Commission to reconsider its findings in the final report for the benefit of all Australians and not singularly for monopoly airports.

Thank you, Commissioners.

COMMISSIONER LINDWALL: Thank you, Andrew for that comprehensive presentation. Can you hear me now? Sorry. Thank you for that, Andrew. I'd like to just start by saying that the teams and the commissioners for the four now PC inquiries have all been different, and the PC doesn't take a different approach each time to how we analyse the problem. Now, I know that you have suggested that perhaps the ACCC should be involved in that, but there is a very fundamental regulatory system structure that has been long held as a principle in government that a regulator should not, should not be involved in the declaration of their own policy, because there's a major conflict of interest, and that's why there has always been a structure where an independent agency may not think the PC is the right agency, but some agency that doesn't actually implement the regulation. That's where the principle of that comes from. So I wanted to put that out.

Now could I turn to negotiate-arbitrate. If there's a problem with Part IIIA surely the best solution is to make Part IIIA more efficient. Why does there need to be a specific regulatory regime for airports compared to any other types of organisations and sectors of the economy?

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MR PARKER: You're certainly right in the sense that we have very little faith in declaration and Part IIIA of having effectiveness, and that is why we are calling for that to be absolutely part of the solution, but we have tried to be as practical and as pragmatic as we could in finding a solution, and that is why we believe a concept like final offer arbitration is the most light-handed way, and we strongly disagree with a rhetoric of airports that say it will have a significant impost or gaming of the system when it is used efficiently throughout the rest of the Australian economy, and there's examples of energy, of gas and others we can talk to where these are brutally efficient processes, and I would again reference in contrast the counterfactual, which is the Perth court case which we envisage to take many years at huge cost and which will be retrospective.

So we have not looked at models like Heathrow where there are pricing arrangements agreed as regulation, and I would point out despite that Heathrow has had a bountiful assurance of investment capital flow to it. Even under a heavier handed regulatory model we've tried to be pragmatic, we've tried to be reasonable to find a compromise. So I think it's both those options on the table. I don't know if anyone wants to jump in.

MS LAIDLAW: Yes. Michele Laidlaw. The only other point I'd make I guess is that the Part IIIA process also contemplates arbitration within its structure. So arbitration is already there once you cross the threshold of declaration as the commissioners already know.

COMMISSIONER LINDWALL: Yes. Can I just follow up on that. I think the words "deemed declaration" were used by Andrew. So I wonder why given that there is a declaration procedure, the NCC are one of the experts that you have argued we haven't paid appropriate attention to, they manage the declaration process. It has certainly been put to us by the NCC that the declaration process is certainly fit for purpose across a wide range of industries. Given that background why does Qantas say let's ignore the NCC and deem declare the airports?

MS LAIDLAW: I think the principal reasons within a legal perspective is that in our view the declaration process is perhaps a particularly difficult one for non-vertically integrated monopoly infrastructure, and particularly the change to criterion A that was the result of the 2013 Productivity Commission review, in our view has raised the threshold that needs to be clear before declaration can be found. It may be the case that that is the right outcome, but nonetheless if you take the Virgin Blue position, the Federal Court view of criterion A prior to 2013, which had a much lower threshold of access materially promoting competition in the downstream market, and the amendments to Part IIIA now which solidify

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the test of criterion A to be the effective declaration in promoting competition in the downstream market, I think we feel that that has raised the bar that needs to be crossed.

COMMISSIONER KING: Just to clarify my understanding is that the original NCC decision and a tribunal decision on appeal for Virgin Blue in Sydney was on an equivalent test to A, so - - -

MS LAIDLAW: That's correct.

COMMISSIONER KING: - - - so my understanding is the original declaration there occurred on what would now be equivalent law. That's your understanding as well?

MS LAIDLAW: Yes. We certainly don't suggest that it's impossible to clear the threshold of criterion A. What we say is that it has been made materially more difficult, particularly in circumstances where we have a non-vertically integrated piece of infrastructure with perhaps not the incentive to deny access that you might see in a case of vertically integrated monopolies.

COMMISSIONER KING: So Qantas disagrees with the National Competition Council who to the best of my knowledge the NCC has said that the current tests are fine and fit for purpose.

MS LAIDLAW: I think what I would say is that the threshold has been raised and that if the Part IIIA process is designed to provide a credible threat of an effective remedy for the use of market power there may be a question mark as to whether Part IIIA really does that, because by increasing the threshold it has perhaps increased the time, cost and resources involved in pursuing a declaration to its natural conclusion.

COMMISSIONER KING: Despite the fact that there was effectively a declaration at Sydney Airport on the current criteria.

MR PARKER: It's not the current criteria.

COMMISSIONER KING: The Virgin Blue original declaration was under a test that - Part 1 which is the one that I think we're arguing about, or discussing, Part A - - -

MS LAIDLAW: Yes.

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COMMISSIONER KING: - - - which was very similar to the Part A that's currently in place, unless Qantas believes that's an incorrect statement.

MS WATTS: We would argue that it isn't similar given that the criterion A test has changed, and the - - -

COMMISSIONER KING: No, but it's changed twice. The determination of the criteria as put forward by the Full Federal Court in Virgin Blue appeal was a different interpretation than had been given to criterion A up to that time, which included the NCC and tribunal decision to declare Sydney Airport in the Virgin Blue case. The recent change has then been to return the interpretation of criterion A back to the interpretation that was used by the NCC and the tribunal when Virgin Blue was successful in declaring Sydney Airport.

MR PARKER: I think answering your question as directly as we can we are pessimistic on the declaration process in its current form, and I think it is worth reminding that the Virgin Blue process took five years, it cost millions of dollars, and as the ACCC has said we need a more direct and efficient and productive access to a dispute mechanism like final offer arbitration instead of a process that is wholly inefficient and with real ambiguity on its potential for success, would be our summation.

MS LAIDLAW: Sorry, Andrew, and just to add that the NCC - there's been an application to revoke the declaration of the Port of Newcastle as a result of this change in criterion A, or following on from this change in criterion A. Now, whether that revocation process will be successful is still an open question, but it seemed a reasonable conclusion to draw that that process was kicked off post a change in the law, a change to criterion A.

COMMISSIONER KING: Although I would note that the NCC did not recommend declaration Port of Newcastle prior to the change of law either.

MS LAIDLAW: No. The Competition Tribunal did though.

COMMISSIONER KING: I understand, but you put forward the NCC as an expert that we have not paid appropriate attention to. It appears that Qantas's view is they prefer the ACCC as the regulator rather than the NCC. Is that a reasonable approach or a reasonable interpretation of your comments, Andrew?

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MR PARKER: I think we're trying as I said to be as efficient and light-handed in having a commercial practical solution, which is why a model like final offer arbitration is our preference.

COMMISSIONER LINDWALL: Could you contrast final offer arbitration with negotiate-arbitrate, or are they basically the same things?

MR PARKER: I think they're the same things, and I think in Graeme Samuel's testimony he will go through in greater detail, but the fundamentals are the same, and I think that speaks to the fallacy of gaming. There is inherent risk for both parties in such a model, and we accept that and we have stared into that risk profile of what a final offer arbitration could mean for the Qantas Group, and it must by its nature bring parties closer to a more acceptable common commercial position. It will only be used, we believe, in those extreme examples where you are unable to reach a commercial agreement, and again I think Perth is a live example of this of instead we have to go to a retrospective court process that we think is wholly inefficient versus an independent expert arbitration model.

COMMISSIONER LINDWALL: There are 47 airlines at Sydney Airport if I remember from the Sydney Airport testimony this morning. Do you envisage if there was a use in negotiate-arbitrate that let's say Qantas was in dispute with Sydney Airport that the other 46 airlines would want to be part of that too?

MR PARKER: I don't know, but I certainly have some doubts as to the validity of that argument. As I say I think these are extreme examples. Many airports have given testimony today and in their submissions about most negotiations in their view are wholly satisfactory and dealt with in an expedient manner, but we believe an arbitration model will be used infrequently. Most international airlines are collectively represented through BARA, but I think we can only speak to Qantas and our position, which is this would be an outlier in its used, but a really important tool, because we certainly believe the airports don't consider the national access regime as a credible threat to regulatory intervention.

COMMISSIONER LINDWALL: How should an arbitrator view the desires of the travelling public, the community at large, potential new airlines when determining an arbitration process between say Qantas and Sydney Airport or some other airport? I mean you don't know who these potential airlines might be, and they could result in a requirement with the law, the investment then say is currently planned, who knows.

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MS WATTS: A couple of points, Commissioner. Firstly, the arbitration is, as Michele Laidlaw has said, is currently part of the regime, so the national access regime already enables arbitration to be activated, although we believe that it's incredibly difficult, and secondly the arbitration is also envisaged in the aeronautical pricing principles. So it's not - I suppose it's unclear if it's arbitration that's being challenged in this questioning, or if its used in some particular hypothetical scenario. If it's the latter, well we would submit that things such as the gas code have demonstrated that you can set the conditions for arbitration. You can have a pool of arbitrators who are asked to consider a number of issues, including competition from other entrants. So we're not the regulatory experts, but we would say is that in our experience it is possible to construct an arbitration system in such a way that it would not stifle competition, if anything the way that many monopoly airports behave now that would be stifling the competition.

COMMISSIONER LINDWALL: Is it the fact of an airport being a monopoly that's a concern or the market power that it possesses, because I've got a friend who owns a bakery in Braidwood which is a monopoly by definition since there's no other bakery there. Doesn't that mean that it's exercising market power that's the important issue?

MR PARKER: Is the bakery charging $12 for a loaf of bread?

COMMISSIONER LINDWALL: It charges a fair bit, the bakery for its loaf of bread and I'm sure it's making a decent profit actually.

MR PARKER: I think it's a combination of those factors. Monopolies without regulation we concur with many voices on this topic, including one I quoted earlier, but particularly the ACCC, who I think it's worth pointing at from the earlier line of questioning, similarly said they don't believe that arbitration would be used in a large number of negotiations. But I think it is a combination of absolutely our view that there is an exercising of market power and that is evidenced through a range of matrix items including their margin and profitability, the international comparison, and the lack of any competitive threat or countervailing power by an airline like Qantas.

COMMISSIONER LINDWALL: I think you're coming down to the fact there's market power in the exercise of it. If you have a monopoly or if you have an organisation without the exercise of market power, but it has market power, or it is a monopoly, would you agree that it shouldn't be subject to additional regulations, or are you saying that because it's a monopoly or/and because it's got market power ipso facto it should be regulated?

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MS WATTS: Commissioner, again the UK CAA has taken the view that having market power is sufficient to have a regulatory regime that is able to adapt to constrain that market power. We also note that the ACCC has said that regardless of the size of a buyer market power - it's not an effective constraint in and of itself on market power. So we would submit that there's a number of factors that need to be taken into account that come with being a privatised monopoly, and that there is a level of regulation that is required of a privatised monopoly which doesn't exist at the moment.

COMMISSIONER LINDWALL: Does Qantas have market power?

MR PARKER: As we said in the submission we don't believe there's countervailing market power in this debate of a network airline like Qantas, and as - - -

COMMISSIONER LINDWALL: Not countervailing, it doesn't have market power.

MR PARKER: Well, I think there is competition in the Australian market, and we have used many examples to demonstrate what happens in a competitive market when even if we have 60 per cent market share, and there's erroneous information that we have claims of 80 per cent market share in markets, which is completely incorrect using the Canberra example that was quoted, that through the combination of existing competitive entrants there are no barriers to entry in the Australian domestic aviation marketplace, which is almost unique in the world. If you want to start an airline in Australia tomorrow you can. So in its whole we believe there is not market power in definition or in practice by Qantas.

COMMISSIONER LINDWALL: But if there was then by your testimony or Moksha's testimony we should regulate Qantas on that basis. It's the mere possession of market power that should be regulated is what I'm hearing.

MR PARKER: But I haven't agreed to your - - -

COMMISSIONER LINDWALL: No, obviously you don't agree that you do have market power.

MR PARKER: Correct.

COMMISSIONER LINDWALL: I am just saying if it were the case.

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MR PARKER: Yes, well I don't think anyone has called out reasons or given evidence of how or why we have market power, so I'm a little perplexed at - - -

COMMISSIONER LINDWALL: It's an airports inquiry.

MR PARKER: They argue countervailing power.

COMMISSIONER KING: I think what Paul is getting at is perhaps a philosophical difference between regulators. Some regulators believe that if a firm has market power then ipso facto it should be regulated. Other regulators believe that a firm that has market power should only be regulated where there is evidence that that market power has been used or abused against it in their interest. We are simply asking which of those two camps does Qantas fall in.

MR PARKER: Yes, well I would just come back to the philosophy of we are not a monopoly.

COMMISSIONER KING: No, claims that you're a monopoly or you have market power, we are just interested in what is Qantas's view. Regulators that fit in the first camp are correct or the second camp. That's all we're asking.

MR PARKER: Jackie, do you want to comment on that one?

MS QUANG: Jackie Quang from legal. Only that in our submission and in our response to the draft report, we feel we demonstrated that, even putting aside the economic philosophical differences that we've demonstrated, that the airports have misused their market power.

COMMISSIONER KING: I understand that submission. Could I just follow up on understanding Qantas' behaviour and strategy. So, aero prices change all the time, around Australia, different negotiations are entered into and concluded. What strategies does Qantas have when, for example, charges may go up at one airport, they may go down at another airport, there are changes in demand, obviously, by passengers - there's a range of things that effects Qantas' behaviour. How often, or how does Qantas change its strategies, it's route scheduling, networking, its use of its expensive aircraft equipment across Australia?

MR PARKER: Matt, do you want to respond to that?

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MR HUDSON: Hi, it's Matt Hudson here. From a Qantas perspective, obviously, we'll take into account the performance of our - of our network. What we take into account as well, our corporate customers who require us to maintain a network offer, regardless of - of the demand of the day, which is critical for us. We can't just provide part of a network, or most of a network, we have to provide a full network. So then anything we do, we need to -to take that into account, to how we operate our network on a day to day basis.

We also have large, long-term investments in fleets. So, multi-year, 10, 20 year investments in the fleet. So once we've made those decisions, we need to operate those aircrafts, and as any airline we need to fly those aircrafts as far as we can, and get as much utilisation out of those aircraft. So, those two components mean that as a starting point, we do have a strategy around how we, obviously, how we operate out business. But they are two constraints on what we can actually do on a day to day basis, or on a seasonal basis. Those two factors always mean we fly to every airport in the country, we need to provide a network, and we need to fly our aircraft as far as we can.

From time to time we might make adjustments due to market forces, or market conditions, or profitability, but they'll be around the edges, and I think, as an example, I think Jetstar, in any one year, has never changed its network by more than 1 or 2 percent. So anything we do is around the edges. So our strategy is around with those fixed investment, so fixed, long-term investments in aircraft, the real strategy is to get as many, to fly those as hard as we can, and get as many passengers on those aircraft as we can to maximise the work we can get.

COMMISSIONER KING: So, I understand the constraints, and I understand the importance of keeping network, but presumably, Qantas does, for example, change a number of flights on the Melbourne-Canberra route in the morning, because you've done that very recently, as I understand, which is why (indistinct) has disappeared. That would be a response, and maybe a response to demand changes, it may be as a response to price changes, but Qantas does have some flexibility. It's not like the aircraft, you know, it always has to be a 737, or that always has to be a whatever on particular flights.

MR PARKER: I was just going to add, I think there is a misnomer here that somehow an aircraft down gauge could be in a response to a commercial negotiation, or commercial pricing behaviour with an airport. That is a fallacy to us, and a really good example is Townsville. We are in a difficult commercial dispute with them, and yet, there have been claims that, well, as a result, Qantas has reduced market share, and yet if

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you look at the available data, again, some seasonal and some market-based and operational-based reductions were captured fully and more by Jetstar in the group.

So we do not allocate aircraft based on a commercial negotiation. It is based on supply and demand, and it is based on operational requirements, because, as we've given examples of, the Frontier Economics Perth study, the Newcastle airport study, with competitors, if we remove your 7 am Melbourne-Canberra sector, and there's a glaring hole now emerging in the market, we know that Virgin will fill that very quickly, or Tiger.

COMMISSIONER KING: So just to clarify, because it seems to be a very strong statement you're making, so I just want to make sure that I understand it, if I understand you correctly, you're saying that Qantas cannot, does not, has never threatened to withdraw or reduce services at any airport in response to a change in aero charges? Is that your statement?

MR PARKER: No. You have - - -

COMMISSIONER KING: Okay. Please - - -

MR PARKER: I am saying, on a day to day basis, we do not allocate aircraft differently because of a commercial dispute. We will, in the case of Perth, and the court case, we have stated clearly on the public record that the domestic operation will continue as business as usual. But until we have clarity, and because of the complex nature of the litigation involved in terminals, we have no certainty on how to grow the international business out of Perth. So that, for example, is on ice, until we have clarity and resolution on that particular court case. But what I am saying is that on a day to day basis, it is a fallacy to argue that we somehow move our assets around based on commercial negotiations.

COMMISSIONER KING: No, I don't think that's what I'm saying. Let me put it in the positive. Has Qantas ever threatened to withdraw, or reduce services at an airport in response to a change in aeronautical charges?

MR PARKER: There certainly are examples where, in a commercial negotiation, we will look at the economics of a route. And if the economics of the route are impacted, as they often are, by extreme commercial behaviour, of course that is the demand argument we're talking about. Jetstar, for example, is extremely exposed to small, incremental rises in price, and if airport charges, as part of that

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compilation, are going to have a material impact, then absolutely that is going to be part of our consideration on whether the economics are viable.

But all things being equal, we - we don't, and again I use the Townsville example, which has been quoted by some, we don't consider aircraft allegation in and around a commercial negotiation.

COMMISSIONER KING: So I think I take that as a yes.

MR PARKER: If you wish.

COMMISSIONER KING: You will make, in your terms, commercial decisions, but they amount to the potential - maybe I won't use the word "threat", because "threat" sounds like a - making (indistinct). But you've (indistinct) a notice of airline, at the airports, the potential for Qantas to withdraw or reduce services, if aeronautical charges change. And that's a - and that is a real consequence of changes in aeronautical charges.

MR PARKER: Absolutely. That's a fact of life, that we routinely have 40-5- per cent price increases lobbed on us as an airline, and in the evidence we gave, where we talked about, particularly for some routes, how exposed they are to a cost impact like that, we would make it abundantly - abundantly clear the impacts that could have on an operation.

COMMISSIONER KING: Just to clarify, also, in the Townsville example, am I to understand that Qantas' reaction, then, has been to reduce its full service operations and to increase its low-cost carrier operations through Jetstar?

MR PARKER: No, that was a temporary arrangement, when the pilot shortages - we went backwards for a short period of time. Jetstar backfilled the capacity, as did Virgin, and Qantas is now growing again in the Townsville market.

COMMISSIONER KING: I just wanted to understand.

COMMISSIONER LINDWALL: Now, I'm much enjoying this conversation, but time is getting through, so I've got to get through some other questions that we haven't been talking about.

MR PARKER: Yes. Please.

COMMISSIONER LINDWALL: One of our recommendations was that a number of anti-competitive clauses be removed from contracts that have been mentioned in submissions. One of them seems to benefit

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airlines, one of them seems to benefit airports. We recommended that they be put in the aeronautical pricing principles. Would you accept that if that was adopted by the government, or - because pricing principles are voluntary, as far as I understand.

MS WATTS: Sure. We have no objection to such a recommendation, we would simply submit that the problem with the pricing principles are that they are not enforceable, that - that airports, in our experience, don't take them very seriously.

COMMISSIONER LINDWALL: We've also discussed a - well, let's talk about a status quo, because it was spoken about in negotiate-arbitrate enough, and now, I think, we welcome your thoughts on that, obviously. But the building block methodology has been used for a long time in - in working out the costs, and for investment, which of course is a lumpy and quite high cost, in particular, putting new runways in. How do you envisage the use of that in the past? Has it been useful to you to use that type of model?

MR HUDSON: All right, so, it's Matt Hudson here. I think - we would say we think it's essential to use that model. In markets around the world, that model is used in other industries, in Australia that model is used. We think it's a critical statement that we should use as an industry. We would say that we don't think the model has been consistently used over time and that's where the challenge is; that's what we think needs to be addressed.

COMMISSIONER LINDWALL: But wouldn't the fact that airports are using building block methodology suggest that they don't have the market power you might be suggesting? For example, you know, in another industry they just tell you the price and you take it or leave it, and that's the way it is and the fact that you do manage to get a building block methodology might suggest some sort of ability to negotiate.

MR HUDSON: I would say we don't consistently get to use the building block model. So we have some airports when we engage in conversations on the building block model will say to us things such as, "We understand Qantas. That's what you're doing and here's the price," so that's not consistently applied. Indications where it is applied, we think that there's a lack of transparency of information shared between the airports and Qantas which makes it a difficult conversation for us to have without the information available to us.

COMMISSIONER KING: Just on that. Sorry, just to make sure we've got all the information. So the airports that don't use the building block

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approach or give you a "take it or leave it" offer, is that any of Perth, Melbourne, Sydney or Brisbane?

MR HUDSON: Yes, I'd say definitely, in the case of Perth. I'd say definitely; Perth's view is that the building block model does not apply.

COMMISSIONER KING: And Qantas' view is that Perth effectively made it a take it or leave it offer.

MR HUDSON: That's right.

COMMISSIONER KING: I understand that there's a court case going on here and I don't want to - - -

MR HUDSON: Yes, that's right, correct, that's right.

COMMISSIONER KING: No, thank you.

MR HUDSON: Yes.

COMMISSIONER KING: I just wanted that clarified.

COMMISSIONER LINDWALL: Now, another issue that was raised this morning and is by submissions, and we also talked about aircraft noise, is the movement cap at Sydney airport. Have you got any thoughts about that you'd like to share and any of the reform options mentioned, palatable or not?

MR PARKER: Yes, we think obviously there's an enormous – many decades' work has gone into trying to solve the complexity of Sydney Airport. We are big supporters of Western Sydney Airport because we think it will add, we certainly hope, a competitive element to aviation in the Sydney basin.

We don't, in all intents and purpose, have a view that an increase in terms of movements per hour or the curfew is politically realistic. We do like a couple of things; which is flexibility within, particularly the 15 minute windows, so that we can catch up after a weather event and, importantly, we operate a very small number of overnight freight services and there's some legislative arrangements proposed in terms of introducing the ability for us to use quieter aircraft which we would like to do than the law currently allows for. So there's a few areas we are supportive of, but we're not overly confident on the appetite for other more significant changes.

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COMMISSIONER LINDWALL: Now, the other thing of course that you've mentioned in your submission is about what you'd say is "excessive security costs" to a number of airports.

MR PARKER: Yes.

COMMISSIONER LINDWALL: Of course the government determines the amount of security, the minimum security at an airport. I guess, well, to articulate, are you claiming that the airports are deliberately having more security than required or is it that the cost of the security is too much for a given level of security, and why is that so? What would be the incentive for an airport to gold-plate security, if you like?

MR PARKER: Moksha?

MS WATTS: I think – sorry, Moksha Watts. Commissioner, our concern with the security pass through charging model is that the definitions have slipped over time that, as it was originally envisaged, it related to direct costs of security; costs such as passenger and baggage screening, counter terrorist security, and it has, now, expanded to include indirect costs such as administration fees, return on capital investment and a range of other overheads.

So, although there is an umbrella of government mandated charges, the concept has significantly expanded and because it is a pass through charge model, there is, not only very little scrutiny that we're able to apply to what is in those costs, but it fundamentally does not incentivise an airport as a security operator to be efficient. So they simply pass on whatever the cost is to airlines who then pass that onto passengers.

COMMISSIONER LINDWALL: Would you prefer the New Zealand approach where the government provides the security and then charges airlines for the security that the government is actually providing?

MS WATTS: So we're open to considering a number of reform options. There are challenges with the New Zealand model as well. We believe it could be more efficient and cost-effective. The Canadian model is another example; that's slightly different again.

But we believe that there are some simpler more light-handed options that are available for government before it considers something so different as bringing security in-house and some of the ones that we have suggested include introducing efficiency obligations on security operators, introducing appropriate boundaries on the concept of what is a recoverable security cost, amending price monitoring to consider security

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charges so to provide additional information that we currently don't have and also implementing some pricing principles on the infrastructure costs around security. There are some simple things that could be done initially before some of those other options are considered.

MR PARKER: If I could just quickly add.

COMMISSIONER KING: Yes.

MR PARKER: I think it is the pass through charging model that we think acts as a disincentive for efficiency, and if I could just quickly give you the example of Perth Airport. So when we constructed our T3-T4 new international operation, Perth quoted circa $40 million of which security was an essential element of that capital build.

We proposed, and it was ultimately agreed that we would develop and implement the new terminal arrangements, including security, and we did it for almost half and the Commonwealth itself noted how more efficiently, because of incentive, that the airline was able to operate versus an airport that has no real incentive in a pass through model when they simply pass on that cost, or in the case of some airports, seek to be rewarded with a margin on top of the investment.

COMMISSIONER KING: Do you want to do – I'm happy to do jet fuel or you are?

COMMISSIONER LINDWALL: Yes, you do jet fuel.

COMMISSIONER KING: I'll do jet fuel.

COMMISSIONER LINDWALL: We're going to talk about jet fuel, obviously.

COMMISSIONER KING: Jet fuel: Qantas' view on whether there's appropriate competition in jet fuel and do you see significant differences in the prices of jet fuel between either Australia and overseas or between different airports in Australia?

MS WATTS: Jet fuel, as you would have come across in your inquiry, is an area where information is incredibly difficult to find. So there's a number of commercial confidentiality constraints around the supply of jet fuel.

What we would say is one of the issues of concern to us is the application of fuel throughput levies which operate at seven airports, five of which we

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operate to, and to the best of our knowledge we cannot find an additional service that those levies fund.

So if you took the example of the joint user hydrant installation at Sydney, the JUHI pays that a license fee and a leasing fee which (indistinct) should cover all of the costs to the airport of hosting that facility, regardless, the airport charges a 5 cents a litre levy which has increased in – well, it was introduced in 2012 and it's increased since then, to airlines for the passage of that fuel.

We believe that represents a windfall gain of approximately 17 million to that airport and probably of those seven airports nationally, we believe that the gain would be around about 20 million a year. So that's certainly an efficiency that we would suggest is worthy of consideration.

COMMISSIONER KING: Do you see any systematic difference in the total fuel price, in other words, including the throughput levy at airports that have that levy versus not? So in other words where there's a 5 cents per litre throughput levy, do you tend to pay 5 cents per litre more for fuel than you would otherwise be paying?

MS WATTS: So there's two ways to respond to that question. So at Sydney if the 5 cents didn't exist, we would pay 5 cents less and so that would be obvious. The case of Melbourne Airport its, as you know, is an open access arrangement but the infrastructure at Melbourne is incredibly constrained. So the access fee is actually quite high because there is an infrastructure constraint there.

So there can be a number of factors that will, beyond the actual price of the crude, come into the ultimate price we pay. The three most crucial factors would be fuel throughput levies, the access arrangement – the ability to get alternate access where there is a price constraint and an infrastructure provision along the jet fuel supply chain. So that's off and on airport.

COMMISSIONER KING: Qantas is in a slightly unusual position because you are obviously equity holders in the JUHI. It's been put to us that these fuel throughput levies are simply part of a negotiation for JUHIs so they're actually just part of a contractual agreement between the airport and the JUHIs for the JUHI lease. So does Qantas believe that if the 5 cent throughput levy disappeared, then, at the next contract negotiation with the JUHI and the airport that the 5 cents would simply reappear somewhere in there as a direct charge to the JUHI?

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MS WATTS: It's a hypothetical in the sense that the levy was introduced in 2012, you know, the year of the last inquiry. In our experience, we would, through other airport negotiations which my colleagues can enumerate in additional detail, where an input cost is challenged by us, an often equivalent appears elsewhere in the building block methodology or in the OpEx cost.

So the fuel throughput levy is a great example of the way we see some of the gaming behaviour of airports where costs are simply shifted the moment there is some scrutiny. So throughput levies might've been seen as an opportunistic way of raising money. If the Commission were to make a finding against them, it's not possible to say if that cost will not simply disappear and be put into another input that the airlines pay and that's, I suppose, why we're here to argue for more effective light-handed regulation in order to provide greater scrutiny and transparency of the entire airport operation because we believe there is a risk of these things.

COMMISSIONER LINDWALL: Getting to that, and I'm conscious of the time. Do you believe that the profits made by an airport, say from its DFO operation, should be used to cross-subsidise aeronautical services?

MS WATTS: So more broadly there is a range of non-aeronautical revenue that airports earn because of the symbiotic relationship they have with airlines. There's no one to buy a cup of coffee if there isn't someone travelling on your plane, to be really simple about it. So there's a range of aeronautical revenue that is directly linked to the aeronautical revenue of an airport. You know, whether that's a DFO or not is another matter. We would suggest that's more an issue around what's permissible and not permissible under an Airport's Act airport rather than the material of a question.

COMMISSIONER KING: Yes, so just to clarify. I mean, essentially we're only talking about hybrid till or a dual till or some sort of – where should the boundary be? So should it include all airport profits under any sort of regulatory approach of airports, regardless of where the profits have come from, what operations? Should it include those that are only in the terminal and therefore you can say directly related to passengers? Should it include business parks where arguably, you know, some of the rent of those business parks is related to its proximity to the airport, but others are simply a commercial rent? So if there was a broader approach to airport profits, where would be draw the line?

COMMISSIONER LINDWALL: I'll let Jim - - -

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MR HUDSON: Yes, I think from our perspective there's two things we would want, before I get to the question of where we would draw the line. We want airports to earn as the monopoly asset to earn a return that's a reasonable return in accordance with the building block model; a WACC framework. We also want airports to be incentivised to invest efficiently and invest efficiently in the right sort of investments. So whether that's aeronautical or not aeronautical, drive right long term outcomes for the airport and airport community. I don't know what the specific answer is around where you draw the line. What I will say is that hybrid till models, single till models can act as incentives to get the right efficient investment. They can also operate as a right framework to ensure an airport receives an appropriate return on a building block framework.

I would say that the current model where you do have a dual till often ends up where retail or non-aero investment is prioritised over aero investment or even worse, is categorised as aero investment and so I think that's the challenge that we would face.

COMMISSIONER KING: Sorry, I do want to just sort of push this a little bit further because I want to understand Qantas' position. So let's say there is a retail outlet – we won't mention a specific brand – which is built on an airport but completely separate from the terminal; may have a different access road – and if you've got one in your head, it's in Brisbane – maybe highly profitable, perhaps, because of tax rules or, perhaps, because of the original lease conditions meant that the government may not have got as much money as it should've when renting it out and simply a better use of land.

But if there is evidence that there is little, if any connection, between the use of the retail precinct and the aeronautical services, would Qantas say those windfall profits associated with a retail centre, "Yes, no, they're separate. They're not regulated. It's the aeronautical, broadly speaking, relating to passenger transport services that need to come under that single till"?

MR PARKER: We would certainly encourage the Commission to look at this more deeply because I think it warrants a debate to our philosophy that Matt mentioned earlier of the passengers we bring to an airport, and if you reverse engineer it, it is also the extraordinary margin of airports in Australia, compared to their international peers that suggests there is something fundamentally wrong with your making an 80 per cent margin or a 70 per cent margin on car parking.

So the answer to your question is "not perfect", but we do think it warrants serious examination, if not by the Commission, by others and we

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have always said that there is much evidence of a hybrid model elsewhere in the world where it's a more harmonious economic arrangement in how airlines and airports are sharing growth.

COMMISSIONER LINDWALL: I think I've got one final quick question.

COMMISSIONER KING: Sorry, for those of you who are getting hungry.

COMMISSIONER LINDWALL: Yes, well, we'll get going. This'll be the last question and it's a quick question. How many agreements have been agreed since our draft report has been released?

COMMISSIONER KING: By Qantas.

COMMISSIONER LINDWALL: By Qantas I guess, yes.

COMMISSIONER KING: Or Qantas group.

MS WATTS: You take it.

MR PARKER: We might take it on notice but - I don't think any. But we'll take it on notice.

COMMISSIONER LINDWALL: Take it on notice.

MR PARKER: Yes.

COMMISSIONER LINDWALL: All right, well, despite the vigour of our discussion, I would like to say that I've been a regular user of Qantas' services over many years. You provide a perfect air service and I enjoy it very much and I will continue to use it.

MR PARKER: We appreciate that very much.

COMMISSIONER LINDWALL: Thank you, and we'll have a break here for lunch.

COMMISSIONER KING: And thank you for that.

COMMISSIONER LINDWALL: Thank you.

LUNCHEON ADJOURNMENT **[1.00 pm]**

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RESUMED **[1.18 pm]**

COMMISSIONER LINDWALL: Welcome. If you could both introduce yourselves for the record and just make an introductory statement, that'd be great.

COUNCILLOR BYRNE: Yes, I'm Darcy Byrne, I'm the Mayor of the Inner West. Thank you very much for the opportunity to attend the hearing today. In essence, I'm here to present the council's submission to the inquiry which is that, whilst we appreciate the benefits of living in close proximity to Sydney Airport, and unlike some elected representatives in the inner west, I certainly can support it continuing to function as an international airport, we do believe that the cap and the curfew are essential component of the compact that exists between Sydney Airport Corporation and the people of the inner west, which enables us to coexist.

I do want to begin by just elaborating a little bit further on our support for the airport as a driver of economic activity and an important part of our region. So we acknowledge its importance to the economy of Sydney, New South Wales and Australia. We acknowledge that changes may need to be made over time to the operation of the airport to achieve the objectives outlined in your inquiry to make it more efficient and economically viable. We think it's legitimate to maintain the balance of impacts on local residents and businesses against the economic viability of the airport, but that reviewing or lifting the cap and the curfew would put that balance out of whack.

Currently, half of our population in the inner west local government area are already badly affected by aircraft noise, Australian Noise Exposure Forecast, ANEF, of 20 contour or greater. And our contention is that the impacts on those existing households and businesses would be greatly increased, but there would also be a whole new cohort of local residents and property owners who would be impacted were the curfew to be lifted.

The proposal to reduce or review the curfew and the cap for the Sydney airport would have a particularly devastating impact on people in the inner west and those impacts would include that of community wellbeing, property values, general health and wellbeing, and I'd invite anyone who was to propose the lifting of that curfew or cap to visit places like Tempe public school, Tempe high school, any household in Sydenham, St Peters or Tempe. You can come over to my home, just off Norton Street in

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Leichhardt which is one of the flight paths that the planes use to line up their landing and you can meet my seven year old daughter whose first word was plane because she'd spent so much time pointing up at the very loud noise coming out of the sky.

So we're not unused to the impacts of aircraft noise and I think lots of our local residents have made a decision a long time ago when they moved there or chose to remain there, that that was part of existing in the inner west and that that's traded off against the enormous benefits of living in such a fantastic place, but we do want to see that balance maintained.

There are specific, perhaps unintended consequences that we wanted to highlight which you should be wary of. Firstly in relation to zoning and conflicts with residential premises. All of the surrounding council's planning controls reflect aircraft noise within the current legislative framework. Extended noise footprint would place many residential dwellings within unacceptably high ANEF contours. Current land use zoning would need to be altered. In other words, there are lots of existing residences that don't have any protection against aircraft noise but would need some subsequently, and I think it is highly unlikely 20 years on, that there's going to be another round of Federal government funding for the insulation of homes and there would be enormous opposition from residents who would be on the receiving end of that impact.

We do question the need for increased airport movements. The draft report admits that Sydney airport already has best operating cost per passenger of all of the airports examined in the study. The whole of airport operating costs are very low in comparison with many overseas airports, and proposed changes to the cap and curfew would provide only limited economic benefit to the airport, and we do think that it could potentially be the thin end of the wedge, and I know that there are advocates out there who suggest that we shouldn't just lift the cap and the curfew, but we should operate the airport 24-7.

I hazard a guess that none of them live in any of the suburbs that I've outlined to you. Residents were promised a long-term operating plan, introduced in July 1997, the stated target was for there to be no more than 17 per cent of aircraft movements to be going over Sydney's inner west. In reality we're experiencing between 25 per cent and 28 per cent of the air traffic right now.

Sydney Airport Corporation master plan promised the status quo and showed no need for the proposed changes to the cap and the curfew. The master plan was prepared in 2018. The plan guaranteed adherence to the existing curfew and aircraft movement cap, and this indicates that the

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operator believes that Sydney airport operates efficiently with the existing curfew and cap.

The plan indicates the aircraft movements at Sydney airport over the past three years have been relatively stable and currently the cap is only approached during super-peaks, like public holidays and the start and finish of school holidays. And there doesn't appear to be any consideration of how a lift to the capital curfew would affect the future Western Sydney Airport. We've been advocating for the Western Sydney Airport to be built for a very long time now, and as an indication of my credentials as an Anti-NIMBY, I have very publically advocated to some of my colleagues of the same political persuasion in Western Sydney that their objections on the basis of aircraft noise to Western Sydney Airport are unfounded.

There are people in the Blue Mountains who are saying, "Oh, no, we can't have a Western Sydney Airport because it will affect us. The noise will affect us". It is actually quicker to get from the inner west to Parramatta than it is from Western Sydney Airport to the Blue Mountains. So I don't think there's anyone in Australia who has a more intimate understanding of what aircraft noise is or a greater tolerance for aircraft noise than people who live in the southern part of the inner west municipality.

So we are not opposed to airports. We're used to living with one. We're opposed to the agreement that was reached all those years ago and which has been infringed upon in practice, being torn up and the curfew and the cap being permanently undermined. So I might leave it there.

COMMISSIONER LINDWALL: Thank you very much. Do you mind if I call you Darcy?

COUNCILLOR BYRNE: Not at all. My technical title is Your Worship but I've been trying to convince people to go with that for many years and no one will.

COMMISSIONER LINDWALL: Rather good. Could I just clarify the Inner West Council distinct? Where does it extend compared to the airport itself?

COUNCILLOR BYRNE: It is bounded by Balmain and Birchgrove in the north. Ashfield in the west, Ashfield and Croydon in the west. Marrickville, Tempe, St Peters and Sydenham in the south and Newtown in the east. So it is kind of ground zero.

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COMMISSIONER LINDWALL: Yes. There's no other council's area that would - - -

COUNCILLOR BYRNE: No, the three form a constituent councils that make up the inner west council were Marrickville, Leichhardt and Ashfield and they were also the three councils that were most affected by aircraft noise in the past.

COMMISSIONER LINDWALL: And you would acknowledge that we haven't said in our draft report that curfew should be removed or that there should be an increase in traffic, we were just exploring options with some level of flexibility in this.

COUNCILLOR BYRNE: Well, I was first made aware of it when I was contacted by Channel 7 to say that it had been suggested in your draft report that maybe the cap and curfew should go, and so I made my views clear on the television program that night and I've come here today to respectfully engage with you on the issue as well.

COMMISSIONER LINDWALL: Yes, I don't think you'll see us making any such recommendations.

COMMISIONER KING: There certainly aren't any such recommendations in the draft report – I would be extraordinarily surprised if they - - -

COMMISSIONER LINDWALL: I'd be surprised.

COMMISIONER KING: I suspect the current Commissioners would have to walk under a bus.

COUNCILLOR BYRNE: Right. Well, that's very reassuring.

COMMISSIONER LINDWALL: But can I talk about the operations during curfew period.

COUNCILLOR BYRNE: Yes.

COMMISSIONER LINDWALL: We are told that if Australia Post and other freight companies have told us that they'd have to have more movements of noisy aircraft and they're prohibited to use fewer movements of the large area (indistinct) . Is that somewhere that some flexibility could be agreed?

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COUNCILLOR BYRNE: I think we'd want it to be very clearly demonstrated that any change to the cap or the curfew was not going to have any detrimental impact on the quality of life of residents living in the immediate vicinity of the airport, and it seems clear to me that if you increase the number of movements that there will be an increase in noise.

I understand that the technology is changing and that the aircraft that are coming online now operate very differently to those that were built 20 years ago, but people in our community are pretty cynical about any suggestion that we should have to put up with more aircraft noise. We're already dealing with more of it than anyone else in Australia, so I think the onus is really upon Sydney Airport Corporation or any of the operators making use of the airport to demonstrate very clearly that there won't be additional impacts through any change.

COMMISSIONER LINDWALL: So this thin edge of the wedge you mentioned, how would it be demonstrated credibly to you as the Mayor, that this change would be of mutual benefit, if you like or in fact it could reduce noise or lead to a better outcome and also allow greater levels of freights.

COUNCILLOR BYRNE: I think I'd just have to return that question to you. How would you demonstrate it to us? I don't think the onus is upon us to come up with a set of criterion - - -

COMMISSIONER LINDWALL: I am just asking for any suggestion, that's all.

COUNCILLOR BYRNE: Yes. We've got two very important protective measures in place and we're determined to maintain them.

COMMISSIONER LINDWALL: You've got this close association with Sydney Airport in many ways, obviously over many years. And in our inquiry we did look at a bit about the planning and master planning approach and interaction between the roads and rail and so on and the airport - and obviously, the airport does communicate with the state government. How happy are you with the relationships at Sydney Airport, in terms of your day-to-day interactions?

COUNCILLOR BYRNE: Well I think you have to understand the political context of our area, so there's - I am a member of the Labor Party. The Greens political party have significant representation across inner western Sydney and their policy is to close Sydney Airport. They are also opposed to the Western Sydney Airport, so I understand how people would get into Sydney under the Greens administration which is

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by parachute but I just don't understand how they would get back out. So I've always tried to have a very constructive relationship with Sydney Airport Corporation. They undertake a lot of community development work and grants programs, charitable giving, there's lots of good people who work there, we consider them a very significant employer. There's lots of our local residents who work there and so we recognise all of those benefits and have always tried to have a constructive relationship. Obviously, as you'd already be aware from your investigations, accessibility through the local traffic networks, into and out of the airport is very poor.

COMMISSIONER LINDWALL: The congestion must be painful, yes.

COUNCILLOR BYRNE: Yes and the planning around Westconnex hasn't solved that. The original premise would be that it would create a direct link to Port Botany and the airport; it's still not entirely clear how the two - how Westconnex will be connected to the airport. There is this Sydney Gateway project which is proceeding but I think the planning around that entire project, in relation to the airport, has been shambolic. That has created a lot of cynicism and distrust. One of the other factors that you might want to consider is that the existing impacts on places like St Peters, from the Westconnex project and now the construction of the Metro, have been very, very significant in terms of dust, air pollution, noise pollution, traffic disruption. So it's all sort of tied into one sort of tsunami of infrastructure impacts, which local residents are up in arms about.

COMMISSIONER LINDWALL: So this is really a sense that a government, of whichever persuasion, make a promise in some area and it's not fulfilled through noise, through dust and other impacts and that makes the community distrustful of promises or even resistant to change that might be helpful?

COUNCILLOR BYRNE: Yes, the government's inability to ensure that contractors associated with the Westconnex project have complied with their conditions of consent, has engendered a lot of anger and were you to have obviously, disowned any suggestion that you would propose lifting the cap or the curfew but I could certainly attest to the fact that were that to be proposed now, that that would be conflated with the existing impacts that people are experiencing and it would result in very strident opposition.

COMMISSIONER LINDWALL: I should let Stephen ask some questions.

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COMMISSIONER KING: So just to - I guess what we were trying to explore in our draft report was sort of the potential for win/win type of situations, where the local community is better off and the travelling public are potentially better off as well. I am happy for - these are theoretical but I am interested in exploring whether some of our suggestions could potentially do that. So for example, you mentioned LTOP targets not being met. It has been put to us that if we reduced the number of movements off-peak, then that would help achieve the targets in the long-term operational plan. Now obviously, that would be a loss for the airport, so what we were wondering is, if you then had more movements in the peak - and I understand there's a bit of flexibility there from the airport's logistical perspective - would that be overall a benefit? So concentrating the noise, in a sense, in the two peak periods, with perhaps lower noise in line with long-term operational plan in the off-peak periods. Is that something worth considering or not - and I'm happy either way.

COUNCILLOR BYRNE: I might ask our strategic transport planner, Ken Welsh, to address that question.

MR WELSH: The issue with concentrating the noise over the peak periods is that the morning peak, in particular, is still a sensitive period for the residents and for the schools. So you would have a much more intense period for say three hours in the morning, where at the minute the cap is 80, whereas you could push it all the way to 100. That would have the potential of yes, depleting the need for the off-peak period but putting a very intense period of noise from six until nine and that, I consider that quite a sensitive period.

COMMISSIONER KING: Okay. One of the other possibilities then - so I take that as a trade-off and it's not clear. Is that a reasonable summary?

MR WELSH: Yes, you would need to do a full noise analysis on it. The other issues we have is the current method of analysing noise is about 35 years old, so we're not convinced that the system is - - -

COMMISSIONER LINDWALL: Just a quick one. I don't think it was 100, I don't think even think that Sydney Airport has the capacity of managing 100 movements in the tower. I thought maybe 85 might be something - - -

MR WELSH: At the minute you have a cap of 80 but the joint study into the operation of the airports back about five years ago, five to seven years

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ago, estimated that your absolute capacity would be 100. Whether that capacity is achievable or not in terms of operation, I'm not convinced - - -

COMMISSIONER LINDWALL: So to go along with Stephen's point, if you were able to make a significant reduction in the off-peak but also have a limit in the peak period of course, so some increase in the peak - I'm not saying go to 100 - is that something that worth considering?

MR WELSH: I think in terms of the off-peak, the off-peak isn't the really sensitive time. A large proportion of our residents are actually at work during that time, so by softening the blow between ten o'clock and three o'clock, I don't think it would really benefit the residents.

COUNCILLOR BYRNE: If that does come under serious consideration, I'd like to re-extend my invitation to hold a hearing at my place, between 6 am and 9 am and we can get a really good understanding of what the impacts would be.

COMMISSIONER LINDWALL: I bet you.

COMMISSIONER KING: If you could put on a sausage sizzle for breakfast that would be fantastic.

COUNCILLOR BYRNE: Absolutely, the hospitality will be very good.

COMMISSIONER KING: One of the other suggestions or proposals was to allow more flexibility in the cap, so rather than the rolling 15-minute, to say well you can't increase the number of movements - scheduled movements per hour - but that only needs to be met over you know, say a day or a shorter period or as some people put, a longer period. So there wouldn't be a change in the total number of movements but simply allow the airport flexibility; when there's say, a weather event, that they can catch up more easily. The view from the local council, is that something worth considering or again, are there immediate problems with that sort of approach?

COUNCILLOR BYRNE: I can only really restate our position, that we're here to assert the need for the cap and the curfew to remain unamended and that it would be, the onus would be on the proponent of any minor change that you're alluding to, to demonstrate through evidence that there would not be increased impacts on people's amenity via that change. I'm certainly not going to put forward a policy position from the council here, that any suggestion that you put forward that weakens or mediates that as our policy position.

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COMMISSIONER KING: No, I understand that. Just a couple of things on the evidence background. The 80 movements per hour, it is far from clear to us that there was actually any great science behind it when it came in, rather than 85 or 75 or whatever. Is that the case or are we missing something, was there a study done at the time to justify the 80 movements as a reasonable level?

COUNCILLOR BYRNE: I was in Year 10 at the time, so I might defer to our strategic planning officer again.

MR WELSH: I wasn't in Year 10 but I wasn't in the country. I am not aware of any study that definitively said 80 was the point but some of the representatives from organisations like SACF may have the history on that.

COMMISSIONER KING: Okay. Are you aware of any studies since then, which have actually properly evaluated the cost to community around Sydney Airport of the noise pollution, the economic externality, to understand both the direct economic and just the health and other costs associated with the airport noise. Has anyone in a sense popping it back to you, Darcy, you said that evidence would need to be shown to you. Has anyone actually done the evidence in the last whatever, 20, 30 years to actually show the impacts and how those impacts are changing, what the impacts are? Whether the impacts currently are satisfactory or not?

COUNCILLOR BYRNE: Well, I think that's very enlightened to hear the Productivity Commission looking at the issue in that way. It was an enormous political issue at the time that the cap was introduced, but huge in the same way that Westconnex has been now. There was huge community opposition, all of the local councils were involved in arranging protest rallies against the changes that occurred. At Sydney Airport, at one stage (indistinct) council was driving their waste and recycling trucks around the airport blockading it. And the settlement that was reached did not satisfy a significant proportion to population but people have moved on. And so if you're still living in the inner west or you've moved to the inner west since, you've made a decision that you're going to live in a community where there are pockets or extensive areas where there are significant impacts from aircraft noise.

We know from the data that that has certainly not been reduced over time, but people accept that that is the status quo. That's the decision that we've made. So if Sydney Airport Corporation or the Productivity Commission were to come and ask us that – to cooperate with them in a study to quantify the impacts on people's health and well-being of aircraft

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noise, we'd participate, but we'd also just settle for an acceptance that the curfew and cap need to stay and move on with the reality of the situation.

The only other thing I had was on the zoning.

COMMISSIONER LINDWALL: Yes, that's (indistinct). (Indistinct) you do that?

COMMISSIONER KING: All right. So, sorry, slight change of tack, then. The council zoning, as you said, any changes would obviously have zoning implications which is a very good point, so thank you.

Exactly how a zoning decision is made by the council, is it based on the Australian Noise Exposure Forecast corridors or, and if so is that the only tool that's used? Is it the broader group of tools? Are you restricted by some sort of legal constraints on your zoning decision? So just so that we can understand that a bit more?

COUNCILLOR BYRNE: Well, I think the crux of the issue – so we're governed by a range of state and federal regulations and controls and our own local environment plan and development control plan. But the crux of the issue is that any significant change would result in properties that are currently not impacted by aircraft noise being so. And I don't think there's any likelihood at all that a Federal Government or State Government agency is going to provide significant funding for the retrofitting of those properties with glazing or insulation.

There was great dissatisfaction in the late 90s at the insulation program that occurred then. It certainly wasn't perfect and it's been expired for a very long time now. So, we will not be looking at amending our zoning in any way. We're pointing out to you that there would be a significant structural problem with the existing adopted zonings endorsed by both the council and the New South Wales Government if you were to make a significant change to the cap or the curfew.

COMMISSIONER LINDWALL: Now, I think you also said in your submission that there's a case for moving onto land and transport (indistinct) the station access if we put a train to the airport which goes through I think (indistinct) onwards. What would you say to that?

COUNCILLOR BYRNE: Well, if you make public transport more affordable and accessible you'll reduce the necessity for parking at the airport, so like everybody else in Sydney, we would like to see that reviewed. And for public transport to be a more viable option for commuters who are travelling to the airport and to be frank, everyone I

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speak to about the parking fees at the airport thinks that it's exorbitant or wrought and you'd be, I think, well-placed to direct your energies towards that rather than reviewing the capital of the curfew.

COMMISSIONER LINDWALL: And a final question before we move on. It's about the (indistinct) bus, suburban bus, networks, maybe cycle parts and so on. What type of links are happening on – in that space, to the airport or around the airport.

COUNCILLOR BYRNE: Well, that's really tied in with the planning of Westconnex and the Sydney gateway, which as I've stated previously, has been in our view shambolic. Still really unclear to ask exactly what the connectivity will be between Westconnex and the airport and it's been a moving feast. The planning around that seems to change, the route, the ingress and egress, all of that seems to change on a month by month basis.

We would be completely open to sitting down with the government, with RMS, with Sydney Airport Corporation and looking at creative ways that we could pool our money together to create better cycling and pedestrian connectivity between Tempe and Sydney Airport which would be a great thing to do because we do get a lot of people coming and parking sort of long stay parking in and around local residential streets there. So we're open to that, but our experience so far from RMS has been less than collaborative.

COMMISSIONER LINDWALL: I think we might finish on that, thank you, Darcy and thank you, Ken.

MR WELSH: Thank you.

COUNCILLOR BYRNE: Thanks very much for the opportunity.

COMMISSIONER LINDWALL: Could I now invite, I think, John Alexander, Jonathon Ward and Maria Patrinos? If you could go and just introduce yourselves for the record and I'm happy to listen to statements that you want to make and then we can ask some questions. Would you like to introduce yourself first, Jonathon?

MR WARD: Jonathon Ward.

MS PATRINOS: Good afternoon, everyone, I'm Maria Patrinos and I'm a community representative on the Sydney Airport Community Forum that's chaired by John.

MR ALEXANDER: I'm John Alexander.

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COMMISSIONER LINDWALL: You might have to speak up because the microphones are purely for recording the transcript.

MR ALEXANDER: I see, okay.

COMMISSIONER LINDWALL: So yes, they don't amplify.

MR WARD: Sorry. I'm Jonathon Ward.

MS PATRINOS: And I'm Maria Patrinos a community representative for the west on the Sydney Airport Community Forum which the Federal Government committee feedbacks to the Federal Minister for Transport.

MR ALEXANDER: And I'm still John Alexander. And have been for a long while.

COMMISSIONER LINDWALL: Indeed. Welcome. Do you want to make a statement?

MR ALEXANDER: Sure. I'm the Member of Parliament for Bennelong and chair of the Sydney Airport Community Forum, or SACF for short. I'm joined here by Maria Patrinos and Jonathon Ward. Jonathon is a member of my staff. I believe the inquiry will also be hearing from John Clarke who is also a member of SACF, but we'll be presenting his submission separately.

SACF has already provided a written submission to the inquiry and we will speak to this today. Firstly, we should mention a bit about who we are. SACF was set up by the Minister for Infrastructure and Transport in July 1996 to address the impacts from Sydney Airport in the wake of the huge public outcry over aircraft noise with the opening of the third runway.

It includes representatives of the community, local councils, industry, State and Federal Parliaments. The full membership of SACF is available from the website. The role of SACF is to provide advice to the Minister, Sydney Airport Corporation and aviation authorities on the abatement of aircraft noise and related environmental issues at Sydney Airport and provide advice to aviation authorities to facilitate improved consultation and information flows to the community about the airport's operations. We hold quarterly meetings with local residents and their representatives put their concerns particularly about aircraft noise to industry and the department who in turn give regular updates.

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Meetings are fully open to the public. Because SACF's terms are related mostly to noise concerns, we will be limiting our discussion to this element of the inquiry. As Sydney Airport is in the middle of the city and while this is advantageous for access from the CBD, it is disadvantageous to the liveability of the many surrounding suburbs. But this is area of concern in parts of my electorate, in north-western Sydney, demonstrates the wide breadth of Sydney suburbs that are effected by aircraft noise. I would draw the committee's attention to the N70 diagram in our submission, to see the full size of the impact of aircraft noise.

It is impossible for a plane to take off or land in Sydney, without travelling over suburbs. Even to the south, Kurnell lies right under the flight path. Additionally, parallel runways suggest most flights should take off to the north and south of the runway, if one was to simply to consider productivity. But if - but it was the outcry to this concept, back in 1996, that created the need for SACF in the first place. The solution to this problem was the LTOP, the long-term operating plan. To quote from the SACF website:

> *Airservices Australia developed a report setting out options for operating the Airport in a way that shares the noise as fairly as possible. This document effectively put forward the draft Long Term Operating Plan for Sydney Airport and was released for public comment in late 1996.*
>
> *The LTOP has the following noise sharing targets for aircraft movements:*
>
> *17% of movements to the North of the Airport; 13% of movements to the East of the Airport; 15% of movements to the West of the Airport; 55% of movements to the South of the Airport.*
>
> *A key feature of the Plan is the runway rotation system. This system involves different combinations of runways (runway modes) being used at different times of the day to provide, as far as possible, individual areas with periods of respite from aircraft noise. Noise sharing modes must be used at the airport, except when weather or unusual traffic conditions prevent this occurring, during the following hours on weekdays:*
>
> *6am to 7am; 11am to 3pm; and 8pm to curfew.*
>
> *Longer noise sharing hours apply at weekends. Noise sharing modes should be used at other times if the conditions permit.*

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If the Productivity Commission is seeking to change the cap or curfew, it is the LTOP that they are actually looking at. It's also something that SACF is against changing. The LTOP is not a perfect system. It regularly overshoots on its targets, particularly to the north. However, it enshrines, in a transparent method, the aspiration to minimise the effects of aircraft noise over our suburbs. The cap and curfew are key regulations that give some, albeit limited, protection to aircraft noise impacting community of Sydney by creating a ceiling on operations.

In this respect, they are working exactly as intended. Proposed changes to the cap and curfew are nothing more than attempts to increase the number of aircraft allowed to operate at the airport. Cities don't just need to be productive, they also need to liveable. One without the other is not a recipe for a successful, happy or productive city. Discussions around the cost of the airport, and industry, of addressing noise objectives, ignore the cost of aircraft noise pollution on the health, amenity and productivity of the noise impacted community. Until these externalities are properly costed, then discussions about the cost to the industry of current noise objectives lack validity.

Before we move to discussion, we'd also like to dispel a couple of myths that pop up in the draft report. Firstly, it states that planes can be forced to wait in the air because of the cap or curfew, which creates additional noise. On flight management systems can be used to very accurately time the arrival of aircraft. However, occasionally aircraft do arrive before the end of the curfew, or the availability of their slot, and are forced to hold. These holding patterns, by definition, have to happen at a height and distance well removed from the runways for operational reasons.

Airservices has informed us that if aircraft must be held, they are placed in one of seven locations: holding points east of Sydney, over water; holding points north of Sydney, Boree, 85 kilometres from Sydney, Sadlo, 130 kilometres from Sydney, Mehan, 220 kilometres from Sydney; holding points south-west of Sydney, Taral, 139 kilometres from Sydney, Culin/Makka, 185 kilometres from Sydney. Additionally, these planes are held a height which further reduces the noise impact. So to suggest that cap or curfew creates noise, is not right.

Secondly, there is a persistent method about aeroplanes getting quieter. What people forget is that while they may be getting quieter, they are not quiet. The different in decibel output of a so-called "quieter aircraft" is often not large, and often undetectable. Meanwhile, the (indistinct) of the future need for larger planes is likely to offset any benefit. A test in 2008 by Airservices Australia using its noise and flight path monitoring system

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on a Singapore Airlines A380, prior to its introduction as a commercial service demonstrated this.

It showed that on arrival, the A380 was only between 2.1 and 3.7 decibels quieter than a 747-400. Even Sydney Airport admitted, in its recent preliminary draft Master Plan, that a drop of decibels on landing is barely perceptible to humans, let alone when noise events are frequently between 70 and 90 decibels. The fact is, larger planes are generally noisier than smaller ones, and the pdMP predicts that trend to accelerate. Of course, any move to new generation aircraft will require - will take decades to fully replace the current fleet. The reliance on planes becoming quieter, is not going to make the difference the report is suggesting it will.

In concluding, I would like to reiterate the importance of this cap and curfew. The movement cap is a specific measure limiting the maximum number of movements, during a rolling 60 minute period. The cap reflects the recognition that an important aspect of the impact of aircraft noise on humans is the frequency of events even then, the current cap of 80 movements per hour means an aircraft movement over residents, every 90 seconds, resulting in almost constant aircraft noise.

Economic arguments to change the cap to allow more aircraft to take off and land based on efficiency ignore the economic, social and health costs of aircraft noise pollution on the community. Aircraft noise pollution is treated as a free good, to be consumed at will. As far as Sydney Airport and the aviation industry are concerned. Currently it's only through effective regulation that the community is given some protection.

We believe the draft report fails to consider the broader picture of productivity. Increasing the cap and reducing the curfew in particular may increase the productivity of the airport, but would likely be more than offset by the loss of productivity and health impacts, caused by the constant disruption and annoyance of aircraft noise as well as the many thousands of people who would suffer a broken nights' sleep. Existing cap and curfew regulations must remain. Thank you. And we would welcome questions.

COMMISSIONER LINDWALL: Thank you very much for that one. I just wanted to clarify one thing, just from the start. We had not made a recommendation to remove the curfew or increase the cap. What we tried to explore was some flexibility in those, and that's what I'll get to in questions.

Secondly, on the point about orbits, holding patterns at various parts away from population centres at a high altitude, I just note that about three or

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four weeks ago, I was in a dash eight from Canberra, and remember doing at least three left hand orbits around Sydney harbour bridge, and up through to suburbs to the north of there, and around, and while that was very nice and scenic, I don't think it was due to the weather. The weather was nothing inclement or anything, so it must have been due to some restriction in landing I would have thought. Anyway, that's just an observation.

So, can I ask, starting - since we had a testimony from John Clarke earlier, we also had council of Darcy Byrne, the mayor of the inner west council. They had slightly different perspectives on the long term future of the Airport. John Clarke said that he envisioned that the airport would cease to exist at some stage in the future, whereas the Inner West Council said that there should be a long term future for the Sydney Airport. Where does your group think it should - what is the future of the airport?

MR ALEXANDER: Well, I don't think I could speak for the group, I could speak for myself, but it would have a very, very long future, indefinite, we don't know what the future holds, que sera.

COMMISSIONER LINDWALL: Of course. But, yes, you don't have a policy prescription on that obviously?

MR ALEXANDER: No. Our main objective is to be a voice for the community and express the concerns of noise pollution. There are probably others who would be better qualified to answer those questions.

COMMISSIONER LINDWALL: Okay. No, that's good. Now, could I ask about the period during curfew where we received testimony that the types of aircraft that are allowed to land are small and relatively noisy and that there is restrictions, or in fact apart from emergency landings, but illegal to land larger planes like a 737 for freight purposes that would be quieter and result in fewer movements. So is that something you would be willing to consider, that in other words having somewhat larger and less noisy planes at less frequency than what is currently occurring?

MR ALEXANDER: I think our overall view always is to look at the reduction of noise. So I think that we should remain open to any prospect of advancing that cause.

COMMISSIONER LINDWALL: So you're open to changing the parameters around things if it can lead to an outcome which is mutually beneficial if you like?

MR ALEXANDER: I am, but I just chair the place.

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COMMISSIONER LINDWALL: Yes, that's true, that's fair. How about you go, Stephen?

MS PATRINOS: No, no, please, go ahead. All I'm saying is that there are a variety, there's a plethora of views around the committee and so it requires a lot of debate to get to a joint position and to agitate for some change.

COMMISSIONER KING: I understand. But if things haven't been discussed at the committee and the committee hasn't reached a consensus and you can't really give a forum view unless there is a forum. I understand.

MS PATRINOS: We can give individual views, of course.

COMMISSIONER KING: Of course, and we'll take them on that basis.

MS PATRINOS: Okay.

COMMISSIONER KING: You may have heard my questions earlier on to the mayor of the Inner West Council relating to where the 80 movement per hour cap came from, why it was 80 rather than 85 or 75 or anything else, are you aware of why 80 was chosen, was there a study done into the noise and amenity, the cost to the residents, is there something that we can go and look at to say that's why 80 was chosen, there is a science or a rationale behind this?

MR ALEXANDER: We did have a discussion about the origins of this, didn't we.

MR WARD: Yes, I mean it wouldn't have been a random number because we weren't there when it was but I can take that on notice and find out.

COMMISSIONER KING: That would be fantastic.

MR ALEXANDER: It wouldn't have just been plucked out of somewhere, nowhere rather, it must come from somewhere.

MS PATRINOS: Well, it definitely came from somewhere, it would have been predicated, I don't know if it was legislated originally on some basis or whether it was part of the development of the LTOP, but I believe there are physical constraints as to how much an aircraft can use a runway under a defined, a predefined configuration, so it's all configuration specific.

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COMMISSIONER KING: Yes. My understanding though is 80 is under the capacity and was under the capacity at the time that it was brought in, which is why I'm sort of wondering why 80 wasn't set at capacity, it was set less than that.

COMMISSIONER LINDWALL: There might be a (indistinct words) basis but there are many things in public policy that I have observed over time that are based on totally arbitrary numbers.

MS PATRINOS: Yes. But if you could find out the exact source.

MR WARD: Yes. No, I'll definitely do that.

COMMISSIONER KING: If you could, yes. Again, one of the things that you may need to take on notice, and again this is something that I think would be important, if they exist, for our report to highlight, which is studies, if there are any, that have been done in recent years, and I'm happy to go back over the last two decades for recent years, into the effects of noise on the local community.

Again, I'm unaware of any person, I don't claim to be an expert in this area, but for such an important issue to the Sydney community I would have hoped that somewhere, somebody has done the studies on, well, what is the cost of noise to the residents around the airport and even on the north shore with regards to not just the economic cost but the broader cost to their health, to their family life and so on. So are you aware of any of those being done, and if not I'm happy to take it on notice if you can do a quick check?

MR WARD: Well, I mean there's Professor Hede's report, though I can't remember exactly when that was, it's probably pushing the two decade barrier.

MS PATRINOS: That was 20 years I suppose.

MR WARD: But that was about the same time as when all this was being said at LTOP and that sort of thing, so the Professor - - -

MS PATRINOS: Robert.

MR WARD: Robert Hede, H-e-d-e, did a report. We, SACF, actually wrote to him last year, maybe the year before, for looking to see if there had been any way to renew that sort of a study. He put out a scoping document which I can definitely get across, it wasn't - he definitely didn't do the full report but he set up what a new report might look like were the government to commission one, or anyone else for that matter, and sort of the

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frameworks. The report that he did back in the day, I note of interest it was a joint report with another person whose name escapes me. But the report didn't just take in - - -

MS PATRINOS: I want to say Paul.

MR WARD: You think it was Paul?

MS PATRINOS: I think it was Paul, yes, I think it was.

MR WARD: The report took in sort of two aspects of it, because particularly with hearing and noise effects it's not just a – in fact that one person feels that may not be the same way another person feels that, so it's not a truly scientific thing of this aeroplane fits this amount of noise and this aeroplane noise will travel x amount of distance that will stop at this road, this house might affect it, it might have different cladding, that person might have more sensitivity.

So the two people that did it, one was more of the engineering side and plus was more social, behaviour psychologist I believe or much more of that side of the social aspect of it and it was a very interesting report, but it is also fairly dated. So I'll definitely find out.

COMMISSIONER KING: Yes, it's good to know.

MR ALEXANDER: Just I should add that the number one issue regarding the operation of the airport is safety and that figure of 80 movements per hour is probably well within a margin to provide us with probably, the airport, with as good a safety record as anywhere in the world, so the noise is second to safety.

COMMISSIONER LINDWALL: I understand that, yes.

COMMISSIONER KING: I was going to go onto the LTOP, that was the intent.

COMMISSIONER LINDWALL: Yes.

COMMISSIONER KING: All right, thanks. We made a number of suggestions as to possible reforms, Paul ran through one with regards to the post-curfew, whether the planes should be evaluated on a noise basis rather than just a list of this plane and not others that may actually be quieter, so we've discussed that. One of the other ones that we looked at was whether there's ways to provide more flexibility in the cap of potentially have a

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variable cap and one option there would be to have fewer movements off-peak and more movements in the peak.

My understanding is that that would make it more likely that the sort of LTOP targets would be able to be met, but it has been put to us that that may be an undesirable change rather than a desirable change, there seems to be different views. So I'd be interested, again, if the forum has a view I'd be interested in the forum's view, if the forum doesn't have a view we'd be interested in your individual views.

MS PATRINOS: Our view is against it I believe, the forum's view is against it.

COMMISSIONER KING: The forum's view is against it, okay.

MS PATRINOS: I think that it's important that the cap remains where it is, I think there's always pressure whether the maximum of the cap is 80 or it's 90 or it's 100 regardless of the absolute value I think there will always be pressure to increase the cap. So in many ways it's about what

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is acceptable to the community, what is acceptable to their amenity and lifestyle, because we know that the airport can operate at that cap but there's still pressure to increase it.

So I think overall our committee has determined that it is only adding pressure to changing well-entrenched modes of operations and also regulations for not any particular benefit, particularly given that we're building a second airport. You mentioned earlier, Mr Clarke mentioned that he would like to see the airport, the Sydney Airport, closed down at some point. I would like to speak personally and say that my view very early on, was that would have been a wonderful thing for Sydney overall because the airport is so close to the CBD and so close, it's built essentially and has been allowed to be built up, right up until the airport precinct, which makes it very difficult for people to live. They do get benefits but there are major disadvantages.

Not naively, I think many of us thought that the Western Sydney Airport, yes would bring many benefits but also would come with the dovetailing and decreased use of Sydney Airport. But the reality of the situation, to me, is that actually all the business interests are such that both airports will want to be used and will be pushed to be used to their maximum capacity. So I can't realistically see that Sydney Airport will be closed in my lifetime.

MR ALEXANDER: Just to add to this, we've just completed an inquiry into mass transit autonomous vehicles and alternate (indistinct) which followed on from a previous inquiry, entitled: "Building up and moving out" which essentially argued for master planning infrastructure and having the purpose of infrastructure understood and therefore, the master planning of land use.

So if you were to contemplate the closing down of Sydney Airport, you would have to master plan the infrastructure in that we judge commutes not in distance but in time, so the supporting mass transit infrastructure from that airport to those who wish to access it, the possibility of high-speed rail, the Melbourne-Sydney air route is the third busiest in the world in terms of numbers of flights, fourth busiest in terms of the number of passengers and when you look at Sydney to the Gold Coast and Sydney-Brisbane, Sydney-Sunshine Coast, that's one of the most busy airport corridors also. Sydney to Melbourne is the busiest air route over land; that could be very much substantially offset with the advent of high-speed rail. So if and when these other modes of transport come into play, it may well be that Sydney Airport has less of a need - it may well be - it would be dependent on many other things.

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COMMISSIONER LINDWALL: Anyway, that's not part of our inquiry.

COMMISSIONER KING: Is there any more that you want to ask because we are a bit short of time.

COMMISSIONER LINDWALL: That is all from me.

COMMISSIONER KING: We might have to finish it there.

MR WARD: Could I just add one thing really quickly?

COMMISSIONER KING: Please.

MR WARD: You were talking - sorry (indistinct words) but I remember seeing something online earlier. You were talking about judging aeroplanes by their sounds after curfew times. The curfew actually already allows for that. There is a list - it's part of infrastructure page about the curfew, a list of aeroplanes that are allowed to take out simply because they are quieter, so that is somewhat - - -

COMMISSIONER LINDWALL: We have received testimonies, I think it's a 737, 800 (indistinct words) isn't on the list but which was supposedly less noisy than a lot of those that are on the list.

MR WARD: I have no idea how that list is formulated or reviewed but it does seem to be listed by quietness, so whatever anomalies I've no idea but in theory.

COMMISSIONER LINDWALL: Okay, well thank you very much for appearing.

COMMISSIONER LINDWALL: We might firstly start with the Australian Business Aviation Association, then if you're happy, we'll go to Regional Express or REX and then an afternoon tea. How does that sound? Okay, David would you mind introducing yourself and perhaps making a statement?

MR BELL: David Bell, from the Australian Business Aviation Association; I am the CEO, I've been so since 2003. The Association was formed in 1981. We currently have 73 members, who operate 120 business jets in Australia and some turboprops and some helicopters but we are basically a business jet organisation. We are one of 14 business aviation associations in the world, who are members of the International Business Aviation Council in Montreal, Canada. Business aviation plays

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a vital transportation role throughout the world, with in excess of 35,000 jets and turbo props in operation; it's a very large fleet of aircraft.

Our submission to the 2011/12 Productivity Commission Inquiry into Economic Regulation of Airports concentrated on the requirement for larger business jets to operate at primary capital city airports, due to the need for longer runways and other infrastructure. It's very pleasing to note that in general, business jets are now very welcome at these capital city airports. We have worked hard at that and it was supported by the Productivity Commission report in 2012.

Also, the ABAA has achieved improved access to Australian airspace for our members and visiting business jets from overseas. Operations into primary capital city airports improved in 2016, when an amendment to the Airservices Australia Assessment of Priorities aeronautical information publication came out.

Now, if a business jet is off blocks on time and has a landing slot if required, the aircraft will be accommodated in the air traffic flow. This improved safety; this was a major step forward for business aviation and airspace safety in Australia and we've had absolutely no adverse comments, even though the Airports Association was very against it, they said that A380s would be diverted from Sydney to Adelaide, et cetera. It was absolutely wrong. We fit into the system, we slot in very easily and our air traffic controllers really appreciate that now.

We have got two major items for discussion today. One is we request a study be undertaken to compare charges incurred by business jet operations at primary capital city airports. We know they are Sydney, Brisbane, Melbourne, Essendon, Perth, Adelaide, Canberra. These airports are of course owned by the Commonwealth and leased to publicly listed companies and privately owned airport operators. Airport charges include take-off and landing fees, aircraft parking fees, security fees, ground handling fees in some cases - but we are particularly concerned about fees at Canberra Airport and it's in our paper, which has gone up on the website today, I believe.

I will just give you a couple of quick examples of Canberra. Domestic operation, first example. Same day domestic arrival and departure, this is one business jet, a Bombardier Global Express, $3,421 thank you. Aircraft parking for one day, same aircraft, $2,900 thank you very much. Total $6,337 plus GST. I will give you another example of an international operation at Canberra, where we need to be there for two days. Apron development levy, $260 a day, that's 520. Apron access security levy $440 a day; landing fee per visit $3,763; aircraft parking fee

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$3,200 per day; total for a two-day trip, international, Canberra Airport for Bombardier Global Express $11,579, plus GST. I think that would be amongst the most expensive in the world and there must be, in our opinion, an inquiry into Canberra charges and also at the same time, look at other airports.

Now I'll give you an example of Sydney. Sydney International FBO arrival movement fee – that's a fixed based operation charge - $390 for arrival, and $390 for departure; airport landing fee $274.98; airport departure fee the same; airport security fee $21; aircraft parking fee $280; total $1,631. That's at Sydney Airport; for a one day airport visit for Bombardier Global Express.

So who is charging too much? I did get a story from Canberra Airport some years ago. They said, "We have to make these charges because our volume is very low." Well, maybe your volume would increase if you decreased your charges. So that, I really believe we've got to look into capital city airport charges for business jets, particularly Canberra. But look at the rest for a comparison.

Now, I'd like to move onto the recommendation that Curfew Regulations 1995 be amended to allow business jet aircraft which are certified to ICAO Chapter IV noise standards and also certified to carry – and this is very important in our proposal – "a maximum of 19 passengers", because that's the way a business jet is defined in the world. That is the benchmark for a business jet. It might be a Boeing business jet, but they're usually certified for 19 passengers. Our aeroplanes are the biggest, usually Gulfstreams, Bombardiers and Falcon Jets, et cetera.

This recommendation is supported by all of the business aviation associations in the airport who say that the – I'll get onto it shortly – there's a weight limitation, a maximum take-off limitation of 34 tonnes for quiet business jets to be able to operate during the curfew of Sydney Airport.

This was put into motion in 1995 when the Act came out and the largest business jet in general usage then was a Gulfstream G4 which weighed 33.8 tonnes. But aeroplanes have grown much bigger, less noisy and more fuel efficient and they fly further. But those heavier business jets now are penalised. They are discriminated against, even though they are quieter than many business jets currently approved to operate at Sydney during the curfew, but because they're a little bit heavier and they have longer range, they are not permitted to operate.

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So we've got a situation now, where there's several of these aircraft on order by wealthy Australians who are running very successful Australian companies, most of their employees fly on the airlines, but some of them fly with the boss in the business jet. But those people are being discriminated against because they're buying quieter, more fuel efficient, long-range aeroplanes that do weigh more than 34 tonnes. So we're asking for the Act to be amended, come into the 21st Century, please.

Now, business jet operations during the curfew at Sydney have been very important for overseas visitors for many, many years and – I talked about the 34 tonne issue; I'm jumping ahead of myself there. The economic case for change, there has been a world-wide trend in the past decade for business jets to be increasingly capable of long-range international operations; I touched on that as well. We're saying, please, raise the weight.

Now, it should be about noise, not weight. Business jet operations during the curfew should be based on noise, not weight. But the max take-off weight limitation's 34 tonnes. This position was supported by Deputy Prime Minister Warren Truss when he was also Minister for Infrastructure, Transport and Regional Development from 2013 to 16. Noise, not weight is also supported by Sydney Airport Corporation Limited and the aviation industry.

Under the current interpretation of the regulations by government agencies it is permissible to operate a Global Express (with a flight manual supplement) from Nandi to Sydney and land during the curfew, but not from airports of departure further afield, such as Honolulu because it'd be more than 34 tonnes on take-off. Well, that's just illogical, isn't it? This interpretation serves no practical purpose as the low noise footprint on arrival over Botany Bay will be exactly the same.

Now, I want to talk about the most important part of our submission; "Departures and arrivals over Botany Bay". We agree with the requirement that low noise jet aircraft take-off from runway 16Right during the curfew, with the take-off roll commencing south of intersection with taxiway G – that's south, you know, of the main sort of threshold there, going south – and landings be on runway 34Left, which is the same runway in reverse. They are the longest runways at Sydney.

But should a downwind component be present, the flight crew can either elect to carry out the landing or divert to another airport. In fact, you take-off over the Bay and you come back over the Bay. If the downwind's too large you go to somewhere else; Canberra or whatever.

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Now, "Departures": The requirement to take off from runway 16Right results in virtually no noise to surrounding suburbs as the track is over Botany Bay, then, with a slight right-hand turn over the sand dunes and out over the Pacific Ocean. This is known as the KAMPI Standard Instrument Departure – a SID – that's publicised now.

But for arrivals, there's not a standard arrival procedure that doesn't go over Kurnell. So I've spoken to Sydney Air Traffic Control and they've told me the following:

"Presently, the requirement to land on runway 34Left, the long one, currently results in the aircraft approaching from the south, over the Pacific Ocean, parallel to the coast and then over Kurnell before landing. Apart from Kurnell, the noise impact on surrounding airport is" – well, we would say zero, but let's say "close to zero. The ABAA has requested Airservices Australia prepare a Standard Instrument Approach" – "STAR" it's called – "utilising the reverse track of the KAMPI SID. We have been advised this should be feasible, with the new STAR being over the Pacific Ocean, then over sand dunes and then west of Kurnell prior to landing on runway 34L."

So we've resolved the problem. We're also going to look at take-offs with a left-hand turn straight out over Botany Bay or coming in over Botany Bay, Airservices telling us that it might be a little bit tight from the western runway – the longer runway – but we're going to have a look at that. But we can certainly resolve the noise issue with this new STAR, coming into land at Sydney's 34L.

So we're very excited about this. This has gone out to our members; it's gone out to the International Business Aviation community. I will be putting a proposal to the Deputy Prime Minister prior to the budget. I've almost got it ready; it'll be based on this one here. It'll be going to the opposition as well and go to the Trade Minister et cetera.

This is about productivity. That's what the Commission's about. We're about increasing productivity in the business world for Sydney, New South Wales and Australia, and this is going to help your business airplane operators who are the leaders of our community. They set the example, they want to abide by the law.

Now, I've just got one other point to make here; "Aviation Sunsetting". "Senior offices of the Department of Infrastructure, Regional Development and Cities have been reviewing Australian airport-related regulations through the sunset process over the past year or so, with a decision made last year to extend the sunset date of ten Aviation and

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Airport Division instruments." This is very interesting. These ten instruments were due to sunset in April this year. In their wisdom, they've decided, "No, we'll let those sunset in another five years."

Well, we have asked the Department to bring forward at least the Curfew Regulations to sunset as soon as possible so we can get these regulations changed, so we can have these departure and arrival situations and airplanes weighing more than 34 tonnes, but quieter.

Now, it's very interesting that the Department have said that they will try to move the Curfew Regulation sunsetting forward a little bit. It definitely must happen before April 2024 and I'm going to work with them to have this as one of the first of the ten. There's slots; there's other things that are very important there too.

We don't complain about the slot system. We try to fit in with it. I just want to touch on that a little bit and then I'll be quiet. The slot system actually has worked – our members have always worked very well with Airport Coordination Australia on the slot system.

We understand where ACA's coming from. We try to fit in with it and we do. But we've been quite lucky in recent years because the airlines have cancelled quite a few flights. Either the day before or even on that day. So if our guys are willing to go at short notice, they can. And it's very interesting that our members are becoming more flexible. They might say to the boss look, we haven't got a spot at 8.30 now, but you know, if you're ready to go sometime after 7 am, we might get it. And invariably, we do now. Because the airlines are cancelling flights. Anyone who goes to Canberra knows that story. Anyone who goes to Melbourne knows that story. Brisbane. It's the same thing. A lot of flights cancelled every day. And fortunately, Business Aviation can step in if we're ready. And I get quite excited sitting on a Dash 8 going to Canberra at 7.05 or whatever it is. And I see a Global Express behind us, because I know someone has cancelled a flight and our guy was ready to go. So it's great stuff. That's it from me. Thanks very much.

COMMISSIONER LINDWALL: Well, thank you very much, David. Yes, just a couple of things initially. You said that the current limit is 34,000 kilograms.

MR BELL: Kilograms, yes.

COMMISSIONER LINDWALL: Now, what's the – how much – how heavy are the planes we're talking about?

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MR BELL: Okay. The latest aircraft to be certified is the Bombardier Global Express at 52 tonnes. But they're quiet.

COMMISSIONER LINDWALL: So it's still maximum 19 passenger seats.

MR BELL: Yes, certified maximum 19 passenger seats. And those aircraft right now cannot operate during the curfew, which is such a shame because they're long range, they're very quiet. They're quieter than some of the aircraft currently approved.

COMMISSIONER LINDWALL: The Canberra Airport prices which you've alluded to here are – well, they seem, on the face of it, high. Have you spoken to Canberra Airport and - - -

MR BELL: No.

COMMISSIONER LINDWALL: We had a testimony from Canberra yesterday, so.

MR BELL: Not – well, I did have a meeting with Canberra Airport when the first hearing was on back in 2011/12, I got the short shrift. I was rudely treated. He was on the phone, he didn't come back to the meeting. And I thought well, if that's the way we're going to be treated, that's not very good. He didn't want to listen to me, in fact, I think you know who I'm talking about. He actually said, "What is Business Aviation?" And I said, "If you're running an airport and you don't know what Business Aviation is, you should not be running the airport.

We have 35,000 turbine powered airplanes in the world criss-crossing countries every day. "Well, they're not all flying every day but you'd have 25,000 flying every day probably. The gentleman down there was not interested in Business Aviation.

COMMISSIONER LINDWALL: Your point about a standard instrument arrival for runway 34L. The – they could of course, make a standard – so, they could make a visual of (indistinct) if they wanted to in that (indistinct).

MR BELL: They can.

COMMISSIONER LINDWALL: Do they do that?

MR BELL: They do that from time to time but we're taking the worst case where it's – instrument approach here, yes. I'm very pleased that the

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Sydney air-traffic controller said that should be feasible. It's on their list to do now, the staff, the reverse track of the SID and they think they'll have it done by the end of the year. – these are proper IFR approaches and departures.

COMMISSIONER LINDWALL: So what do you say about the government policy announcement that when Western Sydney opens in 2026, there'll be no arrivals during curfew at all except for emergencies?

MR BELL: Yes, it doesn't seem reasonable. We'll have to cross that bridge when it comes. It's – I think that we've proven that our airplanes are very, very quiet and with these new flight procedures we're not going to be flying over built up areas at all. They're very quiet airplanes. In fact I had a group visiting from the Japanese Research Institute, part of ANA Airways. They're interested in Business Aviation movements during the Olympics in Tokyo in 2020 and they had a team come out. We showed them around the airports and talk to airport managers – we went to Sydney Melbourne, and Essendon airports, and we stood outside Kentucky Fried Chicken one day and watched the airplanes coming into land on 16Left, the short runway and there was a couple of 737s with flaps down, pretty noisy.

And then I knew this was going to happen because I had a mate of mine who said I'm going to be arriving in a GIV soon, David, I'm coming from Brisbane. And I said to the Japanese, "Just have a look at this G4 coming in." And they said, "Well, where is it?" I said, "It's just going past now." "Oh."

You could hardly hear it. So that's the proof of the pudding. I know some noise away from airports, but you'll find that Business jets are not noisy away from airports either. They're very quiet.

COMMISSIONER KING: Can I come back to your price examples. So when a business jet arrives, or let's say is flying into Canberra, do – would your members negotiate the prices with Canberra? Or is it sort of like a supermarket. You go in and you either take the price or - - -

MR BELL: No, they don't negotiate. They might tell me that it's too expensive or – I said to them before this hearing now, I said, "Give me some examples that you're really disappointed with." And Canberra came up mostly. But then I got a comparison for Sydney which is in here, so the two examples I've given for Canberra, or it might be three, are actually quite recently.

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The first one was an operator from Melbourne going for a day and he was up for more than $6000 to go to our national capital and park at Fairbairn, that's where they park now, of course. And there's no assistance there and you don't get any assistance from the airport.

You're on your own, organise your own transport or if you want an FBO on the other side to organise a taxi or fuel, you'll do it that way. So the airport doesn't help at all.

COMMISSIONER KING: Yes, are there – so you went to – you've asked your members and they've come back with Canberra. Any other airports that really we should also be looking at here or is it really Canberra that's the standout - - -

MR BELL: Look, I don't get a lot of feedback, they're very private people. They don't like even putting this on the table. I had to squeeze this out of a couple of them. I said, "Look, I'm going to the Productivity Commission hearing give me some examples because otherwise, my case is going to be weakened." And so they're very reluctant to come forward. It's like the curfew. They leave at – these leaders of business don't get on television, they leave it to the association to the best – to do the best for them.

And they're all members. You find – all of the people who operate the bigger business jets in Australia are all members of the ABAA. So we have a very good representation there, but they do leave it up to the ABAA.

COMMISSIONER KING: I assume that one that's the business jet that's used for the Governor General and the Prime Minister are not subject to the same rigorous restrictions as yours?

MR BELL: Well, they are actually. Yes. They do abide by them. The challengers, the three smaller aircraft do operate during the curfew under 34 tonnes and they meet the noise requirements, Chapter 3, ICAO. The Boeings are Chapter 4, but of course, they're heavier than 34 tonnes. So RAAF 34 squadron does comply - I haven't known them to abuse that at all. I think they always comply.

COMMISSIONER KING: Just – and again, your members may not give you feedback on this, but I was wondering if you have had any feedback on the different costs of refuelling at different capital city airports and – and whether that's an issue?

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MR BELL: Not much. Not much really. I know Essendon was a monopoly up until fairly recently and then another fuel company came in to Essendon and that's improved the situation a lot. Essendon, I'll just say this is a very important Business Aviation airport. There are more than 60 Business jets based at Essendon and a lot of turboprops. It is a – it's a hub for Business Aviation in Australia. The other airports, Sydney, Brisbane, Melbourne, Adelaide, Perth, Darwin, Cairns, to some extent, are all now welcoming business jets, which is great. Because it wasn't the case 10 years ago with some of these airports. In fact, Sydney airport when it was owned by Macquarie Bank in entirety wanted to move Business jets off the airport. They said you can go to Bankstown.

I reported this in the last Commission Inquiry. Going to Bankstown, Newcastle or Canberra would be totally inept and they said "By the way, because of downtown real estate prices, we're going to start charging your members $3300 a day to park at Sydney airport. They were currently paying $150 a day. Well, we won that one and since that meeting in 2010, we've had CPI increases at Sydney Airport for parking. And you'll now find that Sydney Airport is amongst the least expensive airports – for aircraft parking. I don't know about car parking charge. They're good for us.

COMMISSIONER LINDWALL: Thank you very much there, David.

MR BELL: Thank you. No more questions?

COMMISSIONER LINDWALL: No, no.

COMMISSIONER KING: That's it.

COMMISSIONER LINDWALL: We're going to hear from REX now. Yes, John how are you? Nice to see you. So John and Warrick, if you would like to introduce yourselves and then perhaps give us a statement.

MR SHARP: Certainly. My name is John Sharp, I'm the deputy chairman of Rex and I'm here with Warrick Lodge.

MR LODGE: Yes, I'm Warrick Lodge and I'm the general manager of network strategy and sales for Rex.

MR SHARP: Thank you very much for giving us a hearing. I have to say at the outset that we very nearly didn't bother to come here today because we are extremely disappointed with your report. We're disappointed on a number of grounds, but one of them which is the reason why we nearly didn't bother to come was because we believe that you

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didn't bother to read our submission. This is our submission. There's over 500 pages of it, and there's very little evidence than anybody in the Productivity Commission actually read it, and if you had read it then you couldn't honestly have declared in your draft report that there was no evidence to conclude, or insufficient evidence to conclude that airports were putting take it or leave it deals to airlines.

Now, that's what you said in your report, your draft report. In this document here there's 400 pages of examples of exactly what you said there wasn't sufficient evidence of, and that is examples of take it or leave it deals that airports put to airlines.

Now, strangely enough in your draft report you refer to one of those take it or leave it deals at Mildura Airport. You recall. You've used that as an example of regional airlines having countervailing power over airports. That was an instance where Mildura Airport proposed to put up their charges by 13 per cent. They went ahead and did it. We threatened at the time, as you know, to withdraw services from that airport if they did.

They put the charges up by 13 per cent. We withdrew the Mildura Sydney service and did it have any effect? None at all. Mildura went ahead and increased the charges to all airline operators, not just Rex, by 13 per cent. Now, that is in your own use of an example is a very good example of a take it or leave it deal put by an airport to an airline. Also you got it wrong, and I will go into that a little bit later on, because you actually argue one thing but actually because you got it wrong it turns out to be an argument for the opposite.

So we were very disappointed with your draft report, and I am going to go into that in a little bit of detail in a little while's time. Having said that there are a couple of things that we do agree with, and those - - -

COMMISSIONER LINDWALL: Sometimes you get it right, I guess.

MR SHARP: Yes, occasionally you've got to get it right, and we agree with your recommendation in regard to the need for governments, State and Federal, to undertake some form of economic analysis prior to providing regional airports with funding for extensions or upgrades of their airport. We think that's a sensible decision.

We also agree with your recommendation where you draw on the West Australian example of their template, if you want to call it that, for regional airport managers to more professionally manage their airports. We think that is a sensible recommendation. So there are some good

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things, but there are more bad things than good in this report, this draft report.

The thing that really upsets us the most is that you've put forward an argument for the status quo when it comes to the subject of negotiate-arbitrate, and your position in the draft report, if I am correct I'm sure, is that the current system is more than adequate to deal with the normal commercial issues that airlines and airports experience during the normal course of their daily activity. We would argue that that is wrong. We would argue that for you to try and promote the status quo into the future is the wrong judgment, and we believe there's lots of evidence in here, which we don't think you read, or if you did you ignored it, we believe there's lots of evidence in here which actually demonstrates why negotiate-arbitrate is a better form of dispute resolution in the status quo today.

Effectively the status quo today gives us ultimately litigation. That is the end result of any dispute, and litigation isn't an efficient way of resolving disputes. We've had our own experience with airports in going down that path, and I can tell you they are lengthy, they are costly, they are inefficient and they result in both parties having a public slanging match that does no side any good, and I will give you the example, it's in here, but there are several others.

At Dubbo Airport where we had a dispute that resulted in us having negotiations over a security charge that wasn't required that added about $10 to a departing passenger's ticket price or to our cost. That negotiation went on for a year. We ended up in court. It took us a long time, it cost us hundreds of thousands of dollars and the local newspaper enjoyed it enormously as they ran lots of headlines about us abusing each other, the council and ourselves.

Now, that to me is not a very efficient process. That to me is the status quo that you are proposing to continue into the future, presumed to be the next five years, and we don't think that is forward looking. We don't think that is seeking out the most efficient way of resolving disputes, and we propose as have other airlines proposed that the negotiate-arbitrate process, the regime that sits around that is an efficient, fast and inexpensive way of resolving disputes between airlines and airports.

Now, you argued against that and I think you put four propositions as to why negotiate-arbitrate is not the correct way of dealing with disputes between airports and airlines, and if I can paraphrase those four points, they are cost and time, airlines using arbitration to hold up investments, and I think it was talked about in the terms of gaming earlier today;

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arbitration outcome may reduce efficiency for others, and availability of the national access regime. Those are the four points you make.

I would like to deal with those sequentially. In this submission, 500-odd pages, which we don't think anybody read, we give seven examples of negotiations with regional airports that have gone badly. These negotiations outlined in detail here in this submission demonstrates what our problem is, and all of them will show you that when it comes to the issue of cost and time the current system, the status quo, which you argue for, is expensive and takes a long time.

I just gave you the example of Dubbo a short while ago. I could give you many other examples, Mount Gambier Airport for example. We have been in dispute with Mount Gambier Airport which is owned by the district council of Grant, which is the shire around Mount Gambier. We have been in dispute with that airport for ten years.

COMMISSIONER LINDWALL: I remember you telling me.

MR SHARP: I have told you that, yes, and I did tell you by the way, I have been listening to your questions, I did tell you when you came to see me what the science was behind the 80 movements per hour, but you clearly weren't listening because you didn't know the answer today when you kept asking the question. You clearly didn't listen then.

Mount Gambier - we threatened to withdraw services from Mount Gambier, but do you know what, if we did those services would be replaced the next day by other regional airline operators such as Sharp or Fly Corporate, all of whom operate in this zone, and all of whom would be willing to try and fill a gap left by Rex departing or withdrawing some form of service to a regional community.

So cost and time - a long, long time; a lot of cost. So is the status quo without cost and time? No, of course it is not. It comes with a lot of time and comes with a lot of cost. The alternative negotiate-arbitrate, you've heard the experience of a gas pipeline. They managed to resolve their dispute within four months, which included the Christmas/New Year break, and they resolve it inexpensively.

Now, the next point you make is that arbitration will hold up investments. The status quo can result in disputes with airlines and airports holding up investments. You've seen Qantas talked about their dispute with Perth Airport. They believe - there's no reason not to believe them - they believe that that dispute will last for about four years as it goes its way through the courts. That will cost them many millions of dollars in legal

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fees. Surely that in the current system is a very lengthy delay and a lot of cost. So I don't understand and we are baffled why you think negotiate-arbitrate is going to be worse than that.

COMMISSIONER LINDWALL: We can talk about that - - -

MR SHARP: Well, I look forward to hearing what the explanation is, because it's not obvious in your draft report. You then talk about arbitrated outcomes may reduce efficiency for other users. You make the statement, but there's no example of how that actually works and we're baffled to find out what it is. We don't understand that. So we will be interested in hearing what it is you think this actually means, because just saying something doesn't mean it's correct.

Then you also talk about availability of the national access regime. This one has us more than baffled. National access regime - the last time anybody had a go at this in the airline business was Virgin Blue. It has been discussed already today. It started in 2002. It took five years to resolve it, and you know this. Virgin Blue ended up having to apply to the NCC. The NCC had to make a recommendation to the relevant minister. The minister could make a judgment. It was appealable by the tribunal. Virgin ended up in both the Full Federal Court, the tribunal, and there was an appeal in the High Court. This took five years. This cost many millions of dollars in legal fees.

You're proposing that this is a reason why we should be happy with the status quo. Now, you think of the cost of that and the time taken in that, and you think about if it wasn't Virgin Blue, pretend it's Rex, Virgin Blue has a market, or Virgin as it is today has a market cap ten times the size of Rex. Sydney Airport who was of course the person or the entity that Virgin Blue was appealing to the NCC for a declaration of airside services, Sydney Airport exhausted every legal avenue they could find to delay that process to try and wear the other side out. Sydney Airport has a market cap that is one hundred times the size of Rex. If you think about this from a practical person's point of view would Rex ever embark on a process like that where the persons or the entity that you are appealing against will have full access to a legal process that they can afford and you can't. I don't think having availability of the national access regime represents a solution that an airline like ours would contemplate using. I think it's a nonsense and I think nobody else has tried it since from the airline perspective.

COMMISSIONER LINDWALL: Tiger has.

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MR SHARP: Tiger? And I think BARA once tried too, didn't they. But the interesting thing, Paul, is that at the end of the process that Virgin Blue application was resolved by commercial negotiation, the day of or the day before the final resolution of the legal process.

COMMISSIONER KING: I think, John, we should just make sure the record is correct. There was an application for a declaration after Virgin Blue by Tiger at Melbourne Airport, and the declaration was then withdrawn by Tiger after Tiger and Melbourne Airport reached an agreement and that was obviously relatively quickly because the NCC actually hadn't even reached a decision in that situation.

MR SHARP: It doesn't take away the reality of the situation, and that is - if you go down this course you are going to expose yourself to very extensive legal costs and a very lengthy period of negotiation and legal activity.

COMMISSIONER KING: Even though factually - sorry for interrupting you, but even though factually that is not the case in the Tiger declaration application, so they actually achieved a very rapid outcome under Part IIIA. I don't wish to argue this, but I am simply stating that factually what you are saying is I understand not quite correct.

MR SHARP: Well, all I can say to you is that once you embark on this course of action, and you can't disagree with this, once you embark on this course of action you expose yourself to a very lengthy - potentially a very lengthy period of time. Am I not correct? Am I not correct?

COMMISSIONER KING: Potentially it could be a lengthy time - - -

MR SHARP: Potentially, yes. Okay, so I'm correct.

COMMISSIONER KING: - - - or it could actually be resolved very quickly as in Tiger.

MR SHARP: And it could rain tomorrow too, but, you know, it probably won't. So I'm correct in saying that you potentially expose yourself to a very lengthy period of time. Now, also am I correct in saying you potentially expose yourself to an enormous amount of legal cost. Am I correct in saying that?

COMMISSIONER KING: It's up to you to put your arguments to us.

MR SHARP: No, am I correct in saying it?

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COMMISSIONER KING: No, John, I'm not going to be involved in arguing with you.

MR SHARP: Well, you are, but anyway.

COMMISSIONER KING: I merely wish to point out that you stated there hadn't been any application since Virgin. That is factually correct and I think you would agree with that.

COMMISSIONER LINDWALL: Do you want us to ask some questions, John?

MR SHARP: Okay. We don't think the four reasons that you put forward, time and cost - I mean it's hard to argue that the current system doesn't take a lot of time. Am I correct?

COMMISSIONER LINDWALL: Some people would say, yes, that it doesn't take time.

MR SHARP: Some people say.

COMMISSIONER LINDWALL: Some people would say, yes, it does take time.

MR SHARP: The evidence is there to suggest it is, and we have got 400 pages of it here, which we would invite you to read, which actually proves that it does. So the four points; time and cost - it's a long time under the status quo, and the cost can be very great, can it not? Okay. The second point, which is arbitration can hold up investments, well that happens now under the current system. So negotiate-arbitrate is unlikely to change any of that, in fact it could actually speed up the resolution of a dispute because that's the experience others have had doing the same thing, and you can't disagree with the fact that the gas pipeline resolved its problems, it's negotiations, very quickly.

COMMISSIONER LINDWALL: Airports are different to pipelines.

MR SHARP: Okay. Is that correct? Am I correct in saying that?

COMMISSIONER KING: I think if you can finish your comments and then we will start asking you questions because I'm worried about our timing here.

MR SHARP: Well, I will continue, and I want to talk to you about the issue of your claim that airlines have countervailing power over airports.

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You made it in your draft report, remember, and it's a strong point in the proposals that you put for your justification for the status quo. Now, we talked to you about Mildura Airport. We talked to you about Mount Gambier Airport. Mildura Airport did not take any notice of Rex's so-called countervailing power, did it?

COMMISSIONER LINDWALL: What about King Island?

MR SHARP: If I go to Mount Gambier then I will go to King Island. Mount Gambier on one occasion put up its airport charges by 46 per cent in one year. That had been preceded by a 9 per cent increase the year before. Our threats of leaving or reducing services did not result in Mount Gambier Airport changing its behaviour.

COMMISSIONER LINDWALL: But did you act on your threats?

MR SHARP: No, we didn't in the end.

COMMISSIONER LINDWALL: So it wasn't a credible threat then. A credible threat is one which you act upon.

MR SHARP: We have in the past. Did we? We didn't reduce our services, did we, to Mount Gambier?

MR LODGE: Not initially, no.

MR SHARP: No. We did later. We didn't at the time. But you see your proposition is that airports - airlines I should say, and you make it particularly relevant to regional airlines, because they are often sole operators to airports, regional airlines have countervailing power, but you make a broader statement that all airlines have countervailing power over airports.

COMMISSIONER LINDWALL: Well, some. I think we would have said some airlines have countervailing - - -

MR SHARP: Okay, so we would put the proposition to you that that's absolutely wrong and we can demonstrate that with Mildura. We can demonstrate that with Mount Gambier and we go to King Island Airport and we can go to other airports if you wish. It's all here and if you're worried about time then I suggest - - -

COMMISSIONER LINDWALL: I did read it.

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MR SHARP: - - - rather than take the time of the meeting today, it's all here.

COMMISSIONER LINDWALL: Could we go to some questions, John?

MR SHARP: Can I finish?

COMMISSIONER LINDWALL: If you like, yes.

MR SHARP: Okay.

COMMISSIONER KING: Because remember, there is limited time so we would prefer to have some time to ask questions. If you're merely repeating things and - - -

MR SHARP: I know there's limited time, and I notice that Qantas had had an hour, for example.

COMMISSIONER KING: No, they didn't.

MR SHARP: Yes, they did. They did have an hour.

COMMISSIONER KING: A bit less than an hour, but all right.

MR SHARP: No, it wasn't less than an hour. It was exactly on an hour. I timed it, so.

COMMISSIONER KING: All right.

MR SHARP: So I note your flexibility in this regard and I note your flexibility in regard to the way you rearranged the program today. So we have some other points to make and we'd like to make them, and we want to talk to you a little bit about the cost of airports to a regional airline. Now, in your draft report you make about the cost of jet fuel and you say that jet fuel make up 20 per cent, approximately 20 per cent of the cost, the operating costs of an airline. Remember that? You did say that.

You also then draw on the AAA's proposition that airport costs, airport charges make up less than 10 per cent of the cost of an airline ticket. Do you recall that example that you used in the report, page 313, I think, of your report. Somewhere there.

COMMISSIONER KING: Yes, continue.

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MR SHARP: And you talk about that, and then that is used to justify the argument that airport costs are relatively immaterial to the overall cost of an airline ticket. We would like to make the point, and again it's all detailed here, in this submission, we would like to make the point that for Rex, airport costs represent in the financial year 18, most recent, airport costs make up 16.7 per cent of all our operating costs, not less than 10 per cent, 16.7 per cent. I would also like to point out to you in the same financial year, 18, that fuel costs represented 15.9 per cent of all our operating costs. Now, the assumption made in the draft document is that fuel costs are greater than airport costs, and airport costs are less than 10 per cent. It is not correct. Certainly not correct in our instance - - -

COMMISSIONER KING: Correct.

MR SHARP: - - - for Rex, which is a typical regional airline operator.

COMMISSIONER KING: No, that's good.

COMMISSIONER LINDWALL: That's good to know that.

MR SHARP: And theoretically you are supposed to be putting forward propositions which deal with regional as well as others. Now, I can go on further, and I can say to you that in, and that actually represents, I think it's about $26.16 per passenger is the airport cost, so take-off and landing, because there's a charge at either end, $26.16 is the average cost for an airport charge across our network.

Now that changes in some states. In West Australia, for example, that's much higher. In West Australia, in the network there, our average airport cost is $50.81, $50.81, and that represents 25 per cent of all our operating costs in West Australia and on our community fare, which is our most popular fare, it represents 40 per cent of our total ticket price, and this is a reason why airport costs and the subject that you are reviewing is so incredibly important to an airline like us, and why the status quo doesn't work for people like us because it needs to be better.

And why does it need to be better? It needs to be better because in the same financial year Rex made a profit of $10.46, was it? Yes, $10.46 per passenger, and in some years we've got down to $3 and $4 per passenger, and if an airport puts up its charges by 46 per cent or 13 per cent, or in the case of King Island by 111 per cent , that suddenly makes a service to a regional community unviable, and that's why we need to have an orderly dispute resolution process that brings common sense to the table to ensure that some of these regional airports don't behave against ultimately their own best interests and push up charges such that they end up without an

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airline service because it's no longer viable, and that's where government can play a role, and you're here to advise government. You're here to advise government. Okay?

Now, that's why this is so important to us. We talk about government and we talk about privatised capital city airports and privatised or council owned regional airports. You're aware that I, of course, years ago privatised those airports. I commenced the process. Not in 1994 like you said last week in your speech, Paul. I did it in 1996. Okay?

COMMISSIONER LINDWALL: All right, two years after, all right.

MR SHARP: And we started in 96 and you know that when we did that we introduced regulation to control certain behaviour at the airport, airports. You'll know that because it's referred to in your document. You've got a little time chart thing in your document.

We did that, why? We were a conservative government, who believed in dry economics you could argue. We did it because we understand that greed is a basic human instinct, and if you transfer a natural monopoly from a publicly owned body to a private entity, chances are greed will raise its ugly head at some point along the course of the way. This is something you'd be aware of in your economic studies on monopolies.

We decided to introduce regulation to protect the public interest, and we did it for five years, and after five years your predecessors argued that it wasn't necessary and there's been the so-called light-handed approach ever since which some would describe as a no-handed approach ever since, and airports have been allowed, in many ways, to operate freely, although there are some variations to that statement, and we did that, 1996, how many years ago it is, 30 years ago. We did that in order to protect the public interest.

Now, we are not, the airlines are not, A4ANZ is not, asking for you to reintroduce regulation. All we are asking you to do is to recommend to government to introduce an orderly dispute resolution process, one that is fast, cost effective and efficient, and that's why we argue that negotiate/arbitrate is a fast, cost effective and efficient method, as proven by others with similar challenges, if you like, in dealing with monopoly providers. That's why we ask for negotiate/arbitrate. It isn't a big ask.

We're not asking you to regulate. We're asking you to introduce a method of orderly process for dispute resolution. Instead you have argued for the status quo, and the status, quo as these documents demonstrate, and as your experience, you see now with Qantas at Perth Airport and we've seen

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with a few examples I've given you today, this is not - the status quo is not fast, it is not cheap and it is not efficient because litigation and the courts, as you well know, are not efficient methods of resolving disputes are by nature inefficient, and so we ask you to not try and defend the indefensible. We ask you to try and introduce something a little new, a little different, but proven and known to work to enable this industry, our company, Australia's largest independent regional airline, to actually continue to keep offering our services to the people who live in the 60 communities that we service throughout Australia. That's what we ask you to do and we hope you will do it, and for you to do it, we hope you'll amend your draft report and your final report, to include a recommendation to have a regime of negotiate and arbitrate between airlines and airports.

COMMISSIONER LINDWALL: Okay, thank you John. Could I ask, going back to the 80 minimum cap, could you remind me what you said back there?

MR SHARP: Well Paul, when you came to REX and you only came once and I note from Geoff's comments earlier, that you went to Sydney Airport on numerous occasions, he thanked you for that - well he said "numerous" I'm only quoting him back.

COMMISSIONER LINDWALL: We met Qantas a lot of times - - -

MR SHARP: Well I'm pleased you did and I'm sure they were pleased you went there too but you came to us once and on that occasion, I actually explained to you the background to the 80 movements cap and I'm fascinated to hear the attempts at the answers today. None of them were correct. The answer is it was purely political; there's no science to it whatsoever. Labor had a - - -

COMMISSIONER LINDWALL: I know that - - -

MR SHARP: Labor had an 85 movements per hour cap as air policy, aircraft noise was a huge issue, you recall that there were no aircraft noise parties running around with candidates, the airport had been blockaded I think on two occasions. It was a major political issue and 80 movements per hour sounded better than Labor's 85. It's pretty simple really.

COMMISSIONER LINDWALL: Yes.

MR SHARP: Basic politics, no science to it, the airport can and could and some would argue should, carry more movements per hour but that's not my job today. On that point, if you're talking about the slot system,

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we don't oppose a review of the slot system but what we would say to you is the slot system which I introduced also, also created the Sydney Airport Community Forum that was here earlier with John Alexander. The slot system that I created actually - and I should really get Warrick to answer this question but I think he'll tell you, it's worked extremely well, he is far better versed in it than I and as far as the rest of it is concerned with managing Sydney Airport, I think you should leave things alone.

COMMISSIONER LINDWALL: Okay, well we had better get on to a couple of questions. Do you want to go first or me?

COMMISSIONER KING: Sorry, just a couple of points that came up during your presentation, so thank you for that. Does REX consider that cost-based prices, that it should be paying cost-based prices at airports for its landing charges?

MR SHARP: The cost-based price would be what it costs to provide the service**.**

COMMISSIONER KING: So for example, if a building block model or a standard regulatory approach was used with the proper costs, so the operational costs, return on capital, that that should be the basis of REX's charge?

MR SHARP: Let me tell you the experience that we have and this is real-life experience. When a council gets a new general manager, the first thing they try to do, they think this will be a very good initiative on their behalf and show what a good general manager they are, is they decide they'll increase the charges at the regional airport that they administer and they think this is going to produce profits and the airport will be a profit centre and everything will be great.

Now how they do that, in the case of King Island Airport, for example, is you go in and you revalue the asset and you go and value an asset that for the ease of example is worth $100 before you valued it and after you value it, it's worth $400 so you then depreciate it at whatever rate you pick, five per cent, whatever you want. In the case of King Island Airport, it added another $400,000 to the so-called operating costs. So coming to your question, what is the cost - because the cost could be an inflated depreciation cost caused by a new valuation designed to get the charges up so that the airport manager and the council can say "But we're not covering our costs", which is of course what they do. Warrick can give you the example at Wagga, you might like to give the example at Wagga Airport, what they've done there.

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MR LODGE: Yes, it was probably only around five years ago that the assets were revalued at Wagga Airport and that revaluation process seen the depreciation costs at the airport blow out from around $700,000 per year to about $1.8 million. You know, when Wagga Airport has just over 200,000 passengers a year and you've got almost two million dollars in depreciation costs alone, that has a big impact on the financial viability of the airport.

I guess with regional airports, there needs to be some acknowledgment that many of the regional services that we operate are extremely marginal and if were to go down a path of ensuring that every regional airport was profitable, then there'd be a vast change in what our network would look like because there needs to be a balance between service viability and the community benefits that are driven by regional aviation. As a regional airline we experience the same inefficiencies associated with small passenger numbers as what regional airports do.

So I guess that's where the tension exists in terms of saying, well you know, we've got a loss-making service going to your airport and the airport wants to put up its airport charges by a dollar a passenger. That dollar a passenger might not sound like a lot at face value but with 60,000 passengers, that's an extra $60,000 in operating costs, which for a service that potentially is already loss-making, is difficult to swallow. So that's where, I think from a regional local government perspective, there needs to be that balance between all those other benefits that the air service bring to the local community and not just looking at the one-dimensional viability of the airport profit and loss.

COMMISSIONER LINDWALL: Because this comes back to negotiate/arbitrate, the (indistinct) access regime or the (indistinct) rules of the arbitration regime under there has been put up as being one that we should look at to see success and yet that is explicitly - part of the rules for the arbitrator is to take explicitly into account the costs. So from what you've just said there, my understanding would be you would have problems in setting that as part of the things that the arbitrator must take into account. Is that?

MR SHARP: Well you know, you're assuming the arbitrator's not very intelligent. I mean the arbitrator I'm sure is capable of working around what a reasonable cost is. I mean when you asked me that question a moment ago, would we be prepared to pay at just the cost, my answer to you is it depends on what the cost is. Is it artificially inflated in the case of say King Island Airport or we experience with others, it depends. So I think if you get an expert arbitrator who actually knows what he's doing

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and is intelligent, I'm sure he or she would be fully capable of working out what is a real cost, as opposed to an artificially inflated cost.

COMMISSIONER LINDWALL: What about a better solution - - -

MR SHARP: Okay, I'm looking for better solutions because we haven't found any so far.

COMMISSIONER LINDWALL: A lot of the money that you're talking about going to regional airports, which as you say, cannot make money actually, come from state and federal governments. Some people have proposed a fund for a cost delivered analysis for the investment that is made by the governments because capex for those airports is required to cover them external source, right?

MR SHARP: Correct.

COMMISSIONER LINDWALL: And it goes there. Perhaps as a condition of that, that the governments insist, since they are actually investing in it, that the airports cannot charge depreciation on the asset that's been provided to them and then that wouldn't form part of the charges, you wouldn't need negotiate/arbitrate and you'd have lower prices and - - -

MR SHARP: It's a very valid point to make and we would argue that is the case because in reality, it is an investment made by the airport owner, it's an investment made by the public in the public interest, so why would you depreciate it and then add it to the cost of operating the airport? Indeed it's a very valid point and I totally agree with you. Sadly, we see airport owners, regional councils, local councils, attempt to do that and so this is where your question, I keep coming back to your question, is a difficult one to answer because it depends on the cost. Paul's highlighted a very good way of dealing with it, how an intelligent arbitrator might indeed be able to identify what is a real cost.

COMMISSIONER KING: Would you see the negotiate/arbitrate solution, would the arbitration decision or the arbitrator's decision be appealable?

MR SHARP: Sorry, appealable?

COMMISSIONER KING: Could be - able to be appealed, yes.

MR SHARP: My understanding of what we want is that the arbitrator's decision would be final.

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COMMISSIONER KING: Let's imagine that an arbitrator did something that from your perspective was incorrect, in terms of getting the asset base or getting the cost. So perhaps includes facilities that you think are gold plating are over the top and shouldn't but the arbitrator comes up and says, no they're included in the price. It seems to me that's a very lopsided, if I can call it that, solution. The airport then can't say well you know, if the price is too low, they can't say "We'll take our airport and go away" but if the price is too high, as we've seen in Mildura, REX can say "We'll cease flying to that airport." So isn't the negotiate/arbitrate with no appeal process biased towards the airlines?

MR SHARP: I don't see it as such. I see it as providing a quick, affordable and efficient method of solving disputes. I mean, you are putting to us a hypothetical situation. We can be here all afternoon. I could put some hypothetical situations to you. But as a principle, which is what we should be talking about now, and what you should be proposing the government, as a principle, an arbitration system which leaves the arbitrator's judgment as the final judgment is the proposition, I believe, that we support and that we would hope that you would support.

Now, you can put these hypothetical situations where there may be a failure in law, in due process or some other thing, that would give the other side, the so-called loser if there is one, there may not be a loser in this, but let's assume there is for the moment, gives him cause to go to legal challenge. Well, that might happen, I don't know, but what I would say to you is, that is entirely available to anybody who is a so-called loser now, which is probably what will happen in Perth with the Qantas situation, where whoever wins or loses, if there is such a thing, if there is a loser they'll probably appeal.

And that's available now. So in that situation it's no worse than what we've got. But if you take an optimistic view of the world and you assume that arbitrators are intelligent, capable people who are expert in their field, know what they're doing, follow proper due processes, comply with the law as they know it, then the chances are they'll come down with results which would be deemed to be fair and reasonable and there won't be follow on.

MR LODGE: And I think that, from our experience in dealing with more than 50 regional airports that are predominantly owned by local government, that our experience in the way that some of those have been managed from the airport's perspective, our view is that some of those have been quite ridiculous in terms of the proposed increases that are being imposed onto us or put forward, and we believe that having that

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arbitration process or even the threat of having that arbitration process as a back stop, will actually avoid some of those outrageous things that happen.

You know, we put forward the negotiate-arbitrate process based on our real life experience in terms of dealing with airports, and we know that, any reasonable person looking at the process that we've been looking at for the last 17 years that Rex has existed, would say that many of the things that we have to endure are totally unreasonable.

COMMISIONER KING: Just one final one and I understand you don't want to deal with hypotheticals so I'll just put a high level principle, in an arbitration, let's say between Qantas and Wagga airport, would Rex believe that it should be involved in that arbitration, that it should have standing before the arbitrator?

MR SHARP: It depends on the circumstances. Again, you're putting a hypothetical situation, you said you weren't but - - -

COMMISIONER KING: Well, as a general principle, should airlines that are not directly involved in the dispute, having standing before the arbitrator given that decisions for an airline at an airport may have consequences for the other uses of that airport?

MR SHARP: Yes, Warrick, you can answer that.

MR LODGE: I guess with the regional airports, it's highly uncommon for different users to have different airport charges. Like, for example Wagga airport has a published per passenger head tax and at the end of the day if Qantas is going to have an issue with what Wagga airport is doing, I think that would be a uniformed issue that Rex would have. We operate – like we said, to sixty airports, more than 50 of those are regional airports. Eighty percent of those airports we actually operate as the sole operator. There's only about seven or eight airports where we compete alongside QantasLink.

So when you look at it from that perspective, I wouldn't see any issue in terms of having a regional airport and multiple users which in practical terms is probably going to be one or two regional airport users. We don't see an issue when it's exactly the same issue for both parties.

COMMISIONER KING: So different at regional to say Sydney Airport?

MR LODGE: I think so.

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COMMISSIONER LINDWALL: The issue John you mentioned about regional airports, who has – I said before many of them can't make a profit, right? I think we all agree on that. It is hard for me to describe them as monopolists with market powers and that usually requires that you'd make maximised profit. If you can't make a profit it's hard to be thought of as a monopolist. I think of them more as a pseudo government because they're actually owned by councils. They've got different agendas, they're not profit maximising. As you say, a general manager comes in and the first thing they think of is upping the charge.

So surely the solution is not something thought of commercial negotiation, but is more of a government policy, if you like, from perhaps a Federal and State governments to the local councils which vary in their quality. I mean, I did transitional regional economies and I can tell you they vary quite a lot because they're very small to very large councils. Brisbane City Council is highly competent because it is a very large organisation.

MR SHARP: Yes, some councils vary dramatically in their level of competency and professionalism, there's no question of that, and a lot – if you take an airport like Parkes. I mean, Parkes is a destination we've flown to for a long time. I think it is 36,000 passengers a year, Warrick, around about there. We do three return services a day. It's good service. We support the community there, particularly during their Elvis Festival, and we paint up one of the aircraft and call it The Hound Dog Express. We offer a $99 fare from Sydney to Parkes and Warrick turns up and dresses up as Elvis and the flight attendant does.

So some of these airports are never going to, in reality ever turn themselves into profit centres. They need to see themselves in the same way as the local community use the road or the bridge or the public park or the library or the swimming pool. These are part of the community asset that the community needs to sustain, and I hear people from local councils say to me at times "Why would we subsidise a privately owned airline so it can make a profit?

And this proposition is put in order to justify increasing the charges. And I say to them, "Well, when Mr Fox drives his truck down your main street, how much do you charge him for that?" "And when Woolworths delivers their supermarket goods in their van around the suburban streets of whatever town it is, how much do you charge them for that?"

I mean, the reality is these are pieces of infrastructure that support a community. An airport is a very important part of a local community and if you live in places like Broken Hill or Ceduna or Cooper Pedy or

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Bamaga or Esperance or wherever it may be, the maintenance of your airport is a vital piece of economic asset or infrastructure, and so it should be viewed that way. But you do get and we've given you examples, you're familiar with them, where these new general managers come along and you end up with these ridiculous fights and they can go on for years. Sometimes you can get a mayor, in the case of Dubbo we had that, where the mayor decided – he came up with his own brilliant plan, of how to generate more revenue from the airport. Now, these things are costly. They aren't based on any common sense.

MR LODGE: We have a lot more issues with the regional airports that have got higher throughput and higher airport revenue than we do with the smaller regional airports that truly value their air service and treat their airport like a piece of community infrastructure.

COMMISSIONER LINDWALL: That's what I don't understand when – you gave examples of King Island, 111 per cent increase, and Mt Gambier 46 per cent. Why aren't the other airlines just also withdrawing and then, of course, they would capitulate like nothing is instantly basically and – if there are no airlines flying something, I can tell you that council will fold very quickly.

MR SHARP: Well, if there is – if we were to withdraw from say Mt Gambier, I'm quite sure that – possibly even Virgin Regional or certainly Sharp or Fly Corporate, would be there in a flash.

COMMISSIONER LINDWALL: To pay the extra - - -

MR LODGE: I think in the case of King Island there are two operators servicing King Island which is Sharp which operates services to Essendon and King Island Airways which operate services to Moorabbin. So they're both alternatives to the Rex Service which goes to Melbourne Tullamarine.

COMMISSIONER LINDWALL: But I can't imagine they'd be more efficient than you. You once told me John, that you run on the smell of an oily rag.

MR SHARP: Well, I think just because we've been the most vocal, doesn't mean that the other airlines don't, you know, share the same view as us in regards to what the increased charges are.

COMMISIONER KING: To come back to Paul's point, I mean, you know, many of your airports you're the only carrier, so in a sense there surely if you said "This is uneconomic, we're leaving", that's got to be a

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pretty good threat, at King Island for example, where they're putting it up by 111 – the proposal is to put it up by 111 per cent. If they're doing that to all of the carriers, surely all of them are going to be in the same situation as REX, saying, "We can no longer make a buck out of service in King Island. Nice knowing you, bye." In which case, back to Paul's point, the council will pretty quickly learn that was an undesirable move.

MR LODGE: Well, council tried to implement those charges with no notice. It was effectively communicated in June, for the start of the financial year. And that's what triggered, I guess, discussions between REX and the council, and also between council and the other two airlines. And it's fair to say that probably the departure of the general manager of that council and the departure of the mayor of the council is a reflection on how mismanaged that process was, and that's still an ongoing discussion now. And this first surfaced probably two years ago, when this was first put on the table. Then it went quiet, and then it was put on the table again prior to the last financial year. And now, it's still out in the open, in terms of what King Island Council are going to do with the situation.

MR SHARP: There's an example of, take it or leave it. And we've got another example of take it or leave this week, with Melbourne Airport, moving us from one area to another for our aircraft departures and arrivals parking. It doesn't sound like much, but we were given two weeks' notice to move. Now, the problem with that is that you've got to cross live runways. You've got to cross where jet aircraft push back, and you're going to incur delays, which means your schedule is going to be thrown out.

Now, that's a take it or leave it example. So if I can go back to a point I was labouring on for some time, and that is that there are lots of take it or leave it examples we can give you, bore you to tears on it, that airports put to airlines. It happens all of the time. So, please, if you do anything, change your draft report, which says there's insufficient evidence, and say there is evidence, because there is. And we've been talking about it now, and you used it in your own report, in a different way.

COMMISSIONER KING: Can I come back again to the smaller, regional airports – and this is perhaps putting it more bluntly than Paul it – is it the case that you're not facing abuse of market power, incompetence in some of these pricing decisions?

MR SHARP: Well, the old theory, you know, "Is it a conspiracy or incompetence?" go for incompetence every time. It could well be that.

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MR LODGE: I think if you look back at King Island, you probably rewind the clock about four to five years ago, where they significantly upgraded their little terminal on the island, with Government funding. And then, effectively, that wasn't put to any of the airport users, whether that was required or not; that Government funding gets put into a new airport terminal. REX is only servicing King Island with one flight a day, at a modest 14 or 15,000 passengers, and then it's almost an afterthought, "Okay, how are we going to pay for this now?" It's all well and good to receive that upfront funding, that we've now got an asset that's increased in value, we've got other costs that have gone up. We would have actually been happier to operate to the old terminal and keep the costs where they are.

COMMISSIONER LINDWALL: Which is what I was – my point was, that that asset, which is provided by the Australian taxpayer, shouldn't be depreciated. I mean, the operating costs, that's a different issue (indistinct) different issue. But the actual asset, quite different.

MR LODGE: We didn't ask for that terminal. We didn't ask for the new terminal in Orange. We didn't ask for the fancy terminal in Dubbo. We think that the air services are more important.

COMMISSIONER LINDWALL: Could I just ask one final question, unless you've got any more.

COMMISSIONER KING: I'll finish – to what degree, given the issues with regional airports, in the longer term, to what degree will they be solved by actually setting investment at regional airports – and it may need to be more than investment, but investment, at least, in regional airports on the basis where there's a proper cost-benefit analysis done before investments occur, which then create costs that are passed on to REX and other airlines? I mean, is that at least part of the solution?

MR SHARP: Well, certainly it's part of the solution, I think, because we end up wearing the cost. We've given examples of Orange. Kangaroo Island is a recent example; a $21m investment there, an $18m investment at Orange. The largest aircraft that operated there at the time before the works was a Saab 340B. The largest aircraft that operates there now - - -

COMMISSIONER KING: Still a Saab.

MR SHARP: - - - Saab 340B, after $18m has been expended. A complete waste of money. So, having some rigour, some discipline which governments impose prior to handing out taxpayer's money would be welcome. Of course, in the real world, it's all about politics. But we

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shouldn't let that stop us from arguing a proper case for a principled argument, and that is that the taxpayers' funds should be invested wisely, not foolishly, and it shouldn't be wasted. And so I thoroughly agree with what you've put forward in your draft report in regard to that, and Paul has been making that point again today.

But what I would say – if I can come back – this is why we get so disappointed with what you've done. We have all these problems, and you're starting to see some of them now. We've been talking about them, and I think you can – maybe you can sympathise a little bit with us in some of the problems we deal with, because you were inferring incompetence might be a reason why some of these things are happening, and it's probably quite right. But we deal with this. We have 50-odd council-owned airports that we fly to. That's 50-odd councils that we deal with. That's 50-odd general managers, mayors, and other councillors, multiplied by – there's probably hundreds of people who are actually involved in the management of all of these airports.

It is a very difficult thing to have common sense prevail at times with some of these airports. And that's why a negotiated – an orderly process for dispute resolution is best. You ask Qantas, do they threaten to withdraw services? And I forgot the answer now, but if you ask me that question, which you haven't, but if you did, I would say, "Of course we do." And you know why? We don't want to do it. It's unpleasant. We don't want to live an unpleasant life. But we do it, because it's one of the few tools that you give us. It's one of the few tools.

The only other tool is litigation, and we've done that, and it's not a happy outcome. So why would you deny us an orderly process for dispute resolution, when we have so many obvious problems we have to deal with around this multitude of 60 destinations, 50-odd council-owned airports, where obviously we're going to have problems with the individuals who are involved in managing these airports? It's going to happen. It happens all the time. We're probably running two or three of them at any one time, all the time.

It would make our life so much easier. It would protect the interests of the ratepayers, the interests of the taxpayers, the interests of the travelling public, if there was an orderly process to resolve those disputes, rather than for us to have to go in and threaten to withdraw services, close down the airfield, get into a mud-slinging match with the mayor or the general manager in the local paper, which the local paper loves. We don't want to do that. But I'm going to blame somebody here for making us do that, and it's you. You are the reason why we do that. I mean, you will be in the future if you don't go with our recommendation. So bear in mind that

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if you don't do that, we'll blame you, because we've got no other tools to use. So do we threaten to withdraw services? Yes, we do. Why? Because it's one of the only tools we've got left.

COMMISSIONER LINDWALL: I think, John, you should also blame some of your successes (indistinct) who have handed out money to local councils without - - -

MR SHARP: I wouldn't disagree with your comment. I have been known to say it myself to some of them over the years, that this is a stupid thing for them to do.

COMMISSIONER LINDWALL: Could I ask one final question, and then we can go and have a coffee, is whether – and then we've got one more – is whether, after you mentioned about the Virgin Blue dispute with Sydney Airport back in 2002, how have your relations with Sydney Airport changed over time?

MR SHARP: Well, our relations with Sydney Airport have changed. My very good friend Max Moore-Wilton was the CEO, then chair of Sydney Airport, and I have a great deal of regard for Max, but we got on terribly when he was running Sydney Airport. We had very substantial near-physical altercations about the way they would operate. You heard from David Bell earlier about the increase in parking charges for the private business jets. We had exactly the same experience. We received a letter – and it was usual that it was written by Max, presumably.

It said, "Good news, we've revised the way the general aviation area is going to be working, and how it's going to happen. And as a result, your parking charge for your Saab 340B aircraft will now go to $3400 a day," something like that; about the same sort of charge that David Bell's members were threatened with, "and it'll take effect as of July 1, in a short while's time." Now, that was a low point in our relationship. I think we paid $64 a day to park our aircraft there at that time, so it's a fair increase by any measure, hundreds of per cent. I don't know how many hundreds of per cent, but a lot. And you would argue, I think, if I can assume you guys are reasonable men – are you?

COMMISSIONER LINDWALL: Would I admit otherwise?

MR SHARP: All right, well, I'll judge you when you bring out your final report, and I'll – but if you were a reasonable man, you would say that was an unreasonable increase, wouldn't you?

COMMISSIONER LINDWALL: It does seem rather - - -

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MR SHARP: And that was the low point. We had other low points, but I have to say, since Kerrie Mather came, and now with Geoff, the situation has improved. But Warrick deals with this more regularly than I do, so I should leave him to answer the question.

MR LODGE: I think our relationship with Sydney Airport is very good, and it's obviously underpinned by the declaration on the price cap for regional New South Wales services and also the protection of New South Wales regional slots. There's always going to be some tension in terms of general access issues, because we're a relatively small player at capital city airports. Sydney Airport is our biggest airport. We're probably the third-largest holder of slots behind the Qantas Group and the Virgin Group. We've got about 550 slots a week, which services our 14 destinations.

But that combination of the price cap and the protection of the New South Wales regional services obviously underpins what is a good relationship with Sydney Airport. We do only have two commercial agreements, or aeronautical service agreements with other capital city airports, and that's with Perth, that we entered into at the start of this financial year, and also Melbourne Airport. But outside of that, generally, our airport charges at the capital city airports effectively tie into whatever the rack rate is.

COMMISSIONER LINDWALL: So your issue that you are explaining today is about (indistinct) is really for the regional airports, not for the capital city airports?

MR SHARP: Well, in terms of number, yes. We still have problems at the moment with Melbourne Airport, and I think I may have mentioned that to you when you came to see us, and it's all detailed here, where Melbourne Airport refuses to introduce the runway demand management scheme, for arguments which we find failing. And as a result, the congestion at Melbourne Airport is severe, and we have our worst on-time performance – in departure, I should say, in Melbourne because of that, and it's getting worse every day. I think we did a forecast, and we're down to – our on-time departure will be down to about 50 per cent in about two years' time or something like that.

COMMISSIONER LINDWALL: (Indistinct) Melbourne would say the new runway will alleviate some of - - -

MR SHARP: Well, a new runway demand management system would indeed make the situation a whole lot better. Now, most airports – I mean, Sydney has a slot system which is legislated, and I introduced the

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legislation for those slots. But the other airports have, if you like, voluntary systems that they bring in to better manage departures and arrivals. Some of them are unfair. I think Brisbane has a condition where they won't allow scheduled charter services to operate with aircraft below 50 seats, which we think is unfair. But at least they have a system, and Sydney does; Melbourne doesn't.

COMMISSIONER LINDWALL: I think we've given you more time than Qantas, actually. So if you want to respond one quick thing about jet fuel, is there anything you want to tell us about that?

MR SHARP: Well, we don't have quite the same problem that the others have. It's not a big issue for us. The subject of fuel we've only raised in these discussions today, on the basis that we think you got it wrong. Because it isn't 20 per cent, it's 15.9. Airport charges aren't less than 10 per cent, they're 16.7, and that's why we - - -

COMMISSIONER LINDWALL: I'm happy to correct the mistakes that we make.

MR SHARP: Very good. I look forward to that.

COMMISSIONER LINDWALL: Thank you, John and Warrick.

MR LODGE: Thank you very much.

COMMISSIONER LINDWALL: Let's go and have a coffee, everyone.

SHORT ADJOURNMENT **[3.44 pm]**

RESUMED **[4.02 pm]**

COMMISSIONER LINDWALL: Well, as I said before to everyone, this is our last scheduled presentation. But after that there will be an opportunity, if anyone wants to come forward and give a brief presentation to rebut or agree or whatever. (Indistinct). So, please, Steve, (indistinct) yourself, and an introductory statement if you like.

MR FITZGERALD: Thank you. And good afternoon, Commissioners. Thank you for the opportunity to participate at the hearing. Morrison & Co's provided a brief submission, to support our appearance.

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COMMISSIONER LINDWALL: Thank you.

MR FITZGERALD: So I believe you'll have that. If you don't mind, I'd just like to mind a few opening comments for a couple of minutes, and then happy to take any questions. Morrison & Co's known as a specialist infrastructure manager. Our involvement in airport investment goes back over 20 years, and it's detailed in the submissions, so I won't read it. There's comments. The current investments include APAC, which are Melbourne, Launceston, and Queensland Airports, which is Gold Coast, Townsville, Mt Isa, Longreach, and Wellington Airport in New Zealand.

My role as head of asset management for Morrison & Co, and I've got responsibility for the performance of private (indistinct) investments on behalf of clients. I also sit on a number of boards, including Perth Airport and Queensland Airports. I've been involved in the airport sector for 27 years. I work for the Commonwealth Departments of Finance and Transport through the privatisation process. I was an executive at Sydney Airport for several years, including as an economist, and then I was Chief Executive of a group with European Airports and Chief Executive of Wellington Airport.

As noted in our submission, strong investment outcomes rely on a predictable, regulatory framework. Providing investors with confidence in their ability to recover operating and capital expenses over the industries long investment horizon is in the best interest of final customers, the passengers, as it ensures them the appropriate level of airport services will be provided.

I commend the commission for the evidence based approach taken in the draft report, which I note is a continuation of a (indistinct) applied since 2002. As noted in the submission from Harry Bush, Australia is in the fortunate position of not having to unwind a regulatory system over decades to gain the benefits of responsive investment and service quality. With investment and quality outcomes generally observable in Australian airports, there's no case for the imposition of a heavy-handed regulation with its attendant cost in the form of resources, and delays to investment.

The point I wish to most emphasise, however, is that the proposition that there are simple and quick regulatory interventions that would not have significant negative consequences, is simply false. Airport owners and managers understand their responsibility is custodians of significant infrastructure, to invest the appropriate capacity and a quality that facilitates economic growth of the communities they serve. Airports need to balance the needs of all airline customers, and consider the need to passenger customers. The framework for this is set out in the planning

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requirements under the Airports Act, that is taken through extensive consultation and negotiation, prior to agreements being struck and investments made.

If a third party is introduced to determine outcomes based on a limited number of factors, and the needs of a limited number of stakeholders, such as a single airline, or subset of airlines, the outcome could be materially damaging. We've set out the reasons for this in our submission, but examples of issues that would cause net damage if put through a "simple and quick" process, would include a major common user terminal development, which Perth, Gold Coast and Townsville, all having current, live examples.

The allocation of costs between users or user groups, creating winners and losers amongst - amongst a set of customers. Capacity enhancements that increase competition, or the potential for airline competition, that may be opposed. And the enabling of arguments for fundamental changes to the regulatory understanding of investors at the time of investment, such as stranded asset risk, or pinpoint rate of return specification.

The evidence over 17 years that airports have been able to navigate these complex issues have arrived at balanced outcomes that have facilitated strong growth and delivered increased levels of quality. Given this, increased regulation is unwarranted, and would be unwise. I'd be very happy to take questions.

COMMISSIONER LINDWALL: Okay, thank you for that, then, Steve. Could I start by the examples of negotiate-arbitrate, which some participants have been pushing for, and then claims that the airports have made that might lead to gaming by airlines, against interests of other parties. What do you think of that as a credible outcome, and how would the gaming be manifested?

MR FITZGERALD: Look, I think if the - if a negotiate arbitrate is seen as the way for an airline to ultimately achieve a lower price through a third party, then I do think that derails the good faith negotiations that genuinely are - are progressed towards an outcome. I think there is a risk, and I think - again, the UK example through - through Harry Bush's experience is interesting. It does take - it does take a great deal of maturity, good will, and a system that somehow protects against just the - the negotiate part of a negotiate arbitrate, just being - just being a testing out to get to the lowest possible level before always seeking to go to a - to an arbitrator to seek something even better.

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COMMISSIONER LINDWALL: Is it conceivable that under negotiate arbitrate, you might get more investment than you would under the current system?

MR FITZGERALD: Well, one of the concerns I have with negotiate arbitrate as it's being put forward, is - is it would seem to be triggered not by all of your customers, but by a single customer, or group of customers, and therefore you'd be going into a third party arena, where not all of the facts are on the table, not all of the stakeholders are represented, the benefit of - the benefit of whatever's proposed, or being opposed, to other parties is not taken into account. So I think that - that environment takes you down the "swallow the spider, catch the fly" methodology where you continue to broaden out the participants in that regime, until ultimately, you have a full blown price and inquiry type of outcome to avoid the selective outcomes that you would achieve through a limited – a limited scope and limited (indistinct) arbitration process.

COMMISSIONER LINDWALL: Yes, well, I mean, when I asked about investment obviously, it's a very lumpy investment. CapEx program (indistinct) the airports, there was Frontier Economics in the UK did a study of Heathrow which showed that when there were capacity constraints there was insufficient investment. The rates from that were – went to airlines, not airports. Did you find – have you seen that study?

MR FITZGERALD: Yes.

COMMISSIONER LINDWALL: And - - -

MR FITZGERALD: I'm aware of the summary of the outcome study.

COMMISSIONER LINDWALL: So – so would that be fair to say that if a new system led to less investment at an airports, our major airports, you know, could actually lead to higher returns for airlines?

MR FITZGERALD: I absolutely think that that is a risk and a potential driving force of incumbent airlines. And I don't think airlines are unique in this, but I think if you have incumbency in a system with limited capacity, you're incentive is not to have that capacity grow at a rate that you're not ready personally, as the incumbent organisation, to take up.

So look, I've experienced and seen cases where investment is opposed because I would say the market is concentrated, yields are high, new capacity leads to greater competition and it leads to lower fares and therefore is not in the interest of the incumbents.

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COMMISSIONER LINDWALL: Now, you're on the board of Perth Airport, as you've said. It's currently in a dispute with Qantas before the Supreme Court in Western Australia. Is there anything you can say to us now about that? Obviously there's sort of things legal privilege type rules that's applied, but - - -

MR FITZGERALD: Look, there are, and I certainly won't go near the legal privilege elements and also I note, I think, you have Kevin Brown, the Chief Executive of Perth Airport protecting (indistinct) Melbourne, so I think Kevin is probably better placed to go through the detail. But I would say it's been amazing in some senses that this is the first legal action to recover charges, short paid by Qantas over the last 17 years. I mean, the commission has evidence of fairly long-term behaviour and what the lack of legal challenge suggests is that people think very, very long and hard before they take legal action against their major customer. I think in the case of Perth, you know, the extent of the short payment and the fact that the short payment was coming off an offer to reduce charges, invoicing them without an agreement at a level below the consulted rate, and then what I consider to be an unjustified and really unexplained level of low remittance, is taking place. It's – it was – I think on public record over $11m in four months of short payment. I think when you're a commercial organisation you need to act to protect the company.

And look I – this is only part of the ongoing – the discussions, negotiations, a legal case to recover a past invoice only really deals to that invoice. It will provide some guidance as to what might constitute a fair and reasonable price for service and facilities that continue to be delivered and continue to be accepted. And I think that the – the legal – the legal case, if it were to run its course would add to the body of knowledge of how we should be looking at pricing.

COMMISSIONER LINDWALL: (Indistinct) NZ (indistinct) submission said that this was indicative of why a negotiate arbitrator's needed because it's a very costly situation going to court. I take it you don't agree with that?

MR FITZGERALD: No, look, the – it is costly to go to court. But in the context of economic cost of a system that has been working well for 17 years in a national (indistinct) infrastructure, to have one legal case, I think is actually a pretty modest cost. I think the legal process can be relatively efficient. The courts do deal with cases every day. Protagonists can choose to drag things out. And they can choose to delay. They can choose to go through multiple appeals. They needn't. And in the background, there's always the potential for negotiation to continue.

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The legal process also tends to include attempts to bring the parties together through some kind of mediation anyway. So look, I think the Western Australian Supreme Court is a – is in my view, a valid place for Perth Airport to be going to seek some form of outcome for the level of short payment that it's currently experiencing.

COMMISSIONER KING: I'll ask one question then if you don't mind. I was going to ask (indistinct words) Perth Airport (indistinct) case. Yes, just rather than change topic. Just to follow up on your last point. Perth Airport hasn't gone to the Supreme Court in WA and asked for payment, back payment based on its own invoices. It's gone to the Supreme Court and actually said, or asked the Supreme Court to work out what are fair and reasonable charges on which Qantas should be paying for these back charges.

That does sound an awful lot like something that would be better put before an arbitrator rather than put before a Supreme Court Judge who may have absolutely no or very little background in regulated returns, utilities, how you actually come up with pricing structures and efficient prices. So the argument that's been put before us is yes, it's the first time it's gone to court, but it's ended up in exactly the wrong forum compared to what you could have under an arbitration system.

MR FITZGERALD: I don't necessarily agree. I think that we are operating in a commercial framework of light-handed regulation and recourse to a common law outcome is actually the continued working of remaining in that commercial framework rather than going to an outcome. Again with one party, Perth Airport has reached agreement with every other airline, other than the Qantas Group at Perth Airport, has been transparent in the information its provided, has gone through an extensive process published its documents so it has attempted to run a fair and reasonable process as negotiated in good faith. Now, the point being made by Qantas, publically, is that there is no contract. So there's not a contract against which to submit an invoice.

We're getting – we're straying into the – straying into the legal territory but in the absence of an invoice, you need to decide – there are services and facilities being provided by Perth Airport that Perth Airport believes it should receive recompense for and is asking a commercial jurisdiction in the Supreme Court to opine on what that might be. And you know, the building blocks model approach to setting price is not the be all and end all in either regulation or the commercial world. It's rarely seen in the commercial world. And in the regulatory world, it's not ubiquitous.

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COMMISSIONER LINDWALL: (Indistinct words) Wellington Airport in New Zealand, is there anything you can contrast and compare the New Zealand regulatory system to our one here in Australia?

MR FITZGERALD: Yes. And unfortunately, in my view, the New Zealand system's taken some retrograde steps recently. And over a number of years – so recently, my experience, I was Chief Executive of Wellington Airport from 2008 to 2011. And that was about the time the Commerce Commission started to really inquire into their role. And I think prior to that, there'd been a process of their legislation as you're probably aware, has a – specifies that airports can set charges after consultation. That concept of consultation is quite weighty. It has been legally tested and actually they use the judicial process in New Zealand to really test what does litigation mean. Sorry, consultation mean. And it does mean entering into a process in good faith, with an open mind, taking on board the - the views of all the parties, and ultimately coming to a decision, and I think embedded in that is this common user concept, that you listen to everybody, but ultimately someone has to determine what are - what the investment's going to be, and what the prices that come from that will be.

Now, the commerce commission now has gone down this process of - of really doing a report post pricing. Now, I appreciate, although I haven't been close to the system, but I appreciate that it is a broader report. But everyone is focussed on price and WACC, and that's what the media's focussed on, there's, you know, coming out of the Auckland decision recently, they were talking about 50 - the price was 50 cents too high, and the minister's released - the commerce minister doing a press release about expecting Auckland to reduce its prices, down to what is a - what was a process that had led to an investment outcome, had been a consultation, but everyone they spoke to, well, you need to reduce your price by 50 cents.

In the end, Auckland Airport did see that as pretty much price regulation, because they reduced their price pretty much to the point that the commerce commission would like them to reduce it to. So, in some senses, I think they're - they're actually detracting from all of the rest of the negotiations between the airlines (indistinct) come down to a, "Are you getting accounting return that we think has a bit of extra profit in it," and that's the thing we're going to focus on.

And in a national test of what - what is - what's Auckland Airport's role in the future economic growth of New Zealand, as the major gateway hub, constrain capacity, needing a new runway, pretty - as a regular user of Auckland airport, not the best of - not the best of experiences all the time.

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So I think they've really taken the focus off the regulatory system down to a pin point WACC, two decimal places, and we all know that's no - no more right than many other two decimal place answers, and I worry that that investment is going to suffer, and Auckland Airport subsequently has had delays in its investment, they are not linked as far as we're told, but investment's been pushed back. So the return actually probably will be higher than that, but they've lowered their price to the price the commerce commission want it.

COMMISSIONER KING: Just to follow up on that, when the commerce commission's looking at Auckland, how do they determine the capital base? Is there a set capital base, do they do a - a test of whether capital investment has been reasonable or not? I mean, these are standard tools that occur in, effectively, regulation everywhere else, so I was wondering what happens there.

MR FITZGERALD: Look, I will stand to be corrected, but my understanding is that it's a - that element of it is actually fairly light. They do, sort of, read the materials, and so they are still - the commerce commission still claims they use a light-handed approach, so they would be - I'm not sure if they engage experts to review capital plans. I suspect they read the views of Air New Zealand, other airlines, and Auckland Airport, and sort of say, you know, have they reached some consensus here or not, and (indistinct).

So I don't think they're exercising judgment over that, and it is - it does just come down to almost the press release element of the report. Um, I think if there were a more material economically consequential outcome from - poor outcome from that sort of process, perhaps they would - perhaps they would look in more depth, and I think the - the case there in Air New Zealand's market - market position in New Zealand puts Qantas' position in Australia to shame, in the sense that it's concentration are in the domestic market, 80-plus percent, and flying out of other centres, even internationally pretty strong.

So, I think the - the way that expansion of airport capacity is done in New Zealand - the concerned regulator are a regulatory body, or a government should have is that there is some compact between the national carrier and the airports to not invest fast enough, because it's in both of their interests. Now, I haven't observed that, and I certainly think from the Wellington Airport perspective, and Wellington's - Wellington's running a, you know, a pretty strong campaign to try to get approval to extend its runway so it can compete with Auckland for direct long-haul services.

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Now, that's been heavily opposed, by Air New Zealand, who like the hub and spoke of Auckland, and Wellington - but Wellington is very much out there, it has enormous community support behind it, it has - it has, you know, council financial support. The Airport's a third owned by the council. Two thirds owned by one of our clients. And so, so I'm not seeing the hold up of investment coming up on the airport side, but certainly the incentive's there for Air New Zealand to try to maintain its strong market position in New Zealand.

COMMISSIONER LINDWALL: Very good. When you look at the airports as an investment, how riskily do you - do you (indistinct) the airport investments in Australia, compared to other asset classes?

MR FITZGERALD: Look, within infrastructure, within core infrastructure, I think airports are right at the top end of the core. Now, core, fundamentally, is a low - a low risk investment class, because of - because of the additional volatility - because of the system in Australia where - where airports take the passenger volume risk within set periods of time, there is greater volatility in passenger numbers than things like electricity consumption, and then you have investments that need to be paid for on, this is another electricity analogy, on merchant's, sort of, basis for the commercial side of the business.

They are at that upper end of your core class, and you could - some people do call them core plus, and certainly when I look around the airports we have interest in, you know, getting to Townsville, let alone Mt Isa or Longreach. You're way up the spectrum. Gold Coast, even, is an interesting case in point, such a strong leisure destination, so you do need - and we certainly, when we invest and advise clients, we look at the - for the volatility of folding the underlying passenger traffic, and clearly government, business, visiting friends and family, leisure are kind of your continual of increasingly volatile passengers.

So, an Airport like Gold Coast, which has a degree, now of business traffic, as that region in northern New South Wales is developing decently VFR a strong leisure focus, is certainly a much riskier airport than a Sydney or a Melbourne, and I'll stop there. I could go into different types of traffic as well, but there are different volatilities.

COMMISSIONER LINDWALL: No, that's all right. So you wouldn't agree characterisation by someone (indistinct) very low risk, you know, put the higher return assets?

MR FITZGERALD: No. And certainly, with there now (indistinct) board of transport, we have - we also have investments in UK water that

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we manage, we have investments in various other asset classes, and I - you know, we also invest in data infrastructure and other things, and so we invest across the spectrum, and that's where I'd say, they're not the top of the risk of where we sit. But they're well above the core utility type (indistinct).

COMMISSIONER LINDWALL: Has that risk changed over time? So, if you look at airports today compared to 10 or 20 years ago?

MR FITZGERALD: I think the risk of an airport inherently reduces as it grows. So I think - and I think when you're in a small airport, especially a small international airport, one service can be a fundamental swing of your revenue and cost base, and Gold Coast has only a couple of international carrier, those are quite fundamental to its success. And it runs very hard, those. When you've got a much more diversified base, so I think the inherent growth has probably taken a little bit of risk out of some airports, fundamentally.

In terms of how the market operates, when Morrison & Co first got involved, people just didn't understand the asset class. So in some senses, it was mispriced, and some of those early investments have done - done well, because they were expected to.

COMMISSIONER LINDWALL: Yes.

MR FITZGERALD: They were priced that way, actually relatively - relatively well priced, and I think knowledge over time, and - and quality of management teams, and quality of governments has probably managed to bring that - bring that balance in, so people understand it better. We have got some opportunities within a company structured to - to push more into property development or not, and someone like fixed property development with long term leases is less volatile than the aeronautical business, so you can make some choices about the business as well.

COMMISSIONER LINDWALL: How do you perceive regulatory risks since the design of the system (indistinct words) you said on the basis of if you look at successive reports of the PC, that the large airports are not (indistinct) and not systematically exercising it. But the threat of regulation (indistinct) more heavy handed regulation which is always (indistinct) that the holder is omnipresent if you were to take that logic. Does that effect the way you view the assets?

MR FITZGERALD: Absolutely. And I can guarantee you that we see the threat of regulation is very real. I feel it in my role advising clients. I feel it in my role around the board table. We have taken this process

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extremely seriously. We've done a lot of work. Really the Airports Association has sort of led what I'd say is a very robust piece of statistical and economic analysis which came at some cost to the airports because it is a very real threat of regulation. And I think you'll see that you've published – you've analysed and published in the draft report the returns of the major airports over time in their aeronautical (indistinct) and they're not – they're not out of sync with what you'd expect from pretty much a regulated business. Because, you know, there is that degree of (indistinct) regulation, self-regulation that keeps returns very, very much top of mind.

COMMISSIONER LINDWALL: Yes, Steven, did you have one more - - -

COMMISSIONER KING: Well, just to follow on and keep on the risk area. From the airports you deal with, how do you think about the returns from the different services? So I'm just looking through them, but I don't think there's any that have – although Perth may have a Business park on it. But earlier today, we were discussing airport services where you've got Core Aeronautical Services. You've got other services have sort of related to passenger traffic and car parking (indistinct words) then you have sort of a grey area (indistinct words) go from business (indistinct) or you may say, well, being close to the airport is (indistinct words) can be higher through to having shopping centres which have separate entrances and probably have no relationship to passenger transport at the airport.

So from the airports that you're involved with, how do you think about those different investments and the relationship between those investments? How much – how much are they thought of as a package (indistinct words) thought of as separate investments? I'd like to understand that a bit more.

MR FITZGERALD: The answer to the question is that we think very deeply about the individual characteristics of each airport in trying to value it and trying to think about its returns.

Now, some airports have more opportunity to be (indistinct) risk than others. And Perth actually has quite an extensive property of state, both developed and potential. It has distribution centres for Coles and Woolworths. No particular reason to be on the airport (indistinct words) but the airport is located in a place that has good road accidents.

Recently opened a DFO joint venture shopping centre on the (indistinct) of the airport. In some senses, the airport, being that was one of the issues, you don't want to have traffic congestion overlapping. A lot of work is done in urban planning to prevent the almost mixing of the traffic

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types, because you don't want people complaining about missing flights, because people are queued up to go to the DFO.

The Perth Airport has, for example, a large office for Rio Tinto, there's over a number of buildings operation centre, yes, I think that has benefits to Rio being on the airport, but it's – you could assume it's at a cheaper rent than A grade office in the centre of Perth at – or at least the A grade office prices of a few years ago.

So you know, that is something that is a feature of that airport. Now, when I was at Sydney airport, it's a - Sydney airport is a tiny geographic footprint. And so has less capability, but as an investor, I think you – these are substantial investments and they're big enough to be taken on a case by case basis and to look at the characteristics of a (indistinct words).

But I think you asked about the hierarchy of risk. And I do think long term property leases to good credit counterpart (indistinct) is right at the bottom. And it's not part of the aeronautical till but it's there. Sometimes property's talked about as, you know, sort of lounge leases or office leases of the airlines. They probably are next up because they don't fluctuate with the number of passengers. (Indistinct words) the passenger volatility comes into your aeronautical till and there I think you've got greater volatility with things like car parking and retail because you are seeing particularly at the moment, you're seeing quite a lot of substitution going on with car parking for rideshare, for other ground transport modes, you've got competition of public transport et cetera, et cetera.

So I'd say that they are riskier than (indistinct words) aeronautical. So aeronautical is not the top or the bottom, but it's probably – it's probably in the middle.

COMMISSIONER KING: So some parties, either explicitly or implicitly, so explicitly called for a single till presumably because it's not always clear, but presumably as all airport operations, other parties have implicitly done that by saying, well, we're going to analyse a return on all airport assets and argue that that's too high and therefore there needs to be more regulation of airports. What's your view, again, from the investment perspective of the consequences of if you started moving towards a single till type approach, rather than explicitly separating aeronautical services off from the other services?

MR FITZGERALD: I think you would – you would really dampen any appetite to take any risk. So I think you – you will – why do we work hard at those other parts of the business, not aeronautically related

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businesses? Well, because they are businesses in their own right. They're substantial businesses.

They're standing in a market with competitors and being priced competitively against alternatives. Now, if they are making a reasonable return and they may have some locational advantage or something else we've spoken about, I don't know what the economic efficiency benefit of taking that return and giving it to airlines would be. And I think – I think this goes to the issue of your – of what is the appropriate economic signals to be sending through pricing. And I think we're all in a world where average cost is seen to be accepted as the right way to go. Whereas I think you know as – as a (indistinct) you sort of think well, actually, we're sort of really – we really should have an eye on what long run incremental cost is. And if you're pricing too far below long run incremental cost, what are we doing; and in a constrained market, all we're doing is transferring wealth around. And I don't think that is of any great economic consequence. And even if you did behind that, you know, with the people we represent, essentially, Australian superannuates, you know, our – Wellington Airport is based on New Zealand superannuates?

But the Australian airports are owned partly – the future fund, which is the commonwealth generally, but also our other clients tend to be dominated by Australian superannuates. I think that wealth transfer out of that pool doesn't seem to make a lot of sense to (indistinct).

COMMISSIONER KING: (Indistinct) airports. Yes.

MR FITZGERALD: Yes, (Indistinct) airline (indistinct).

COMMISSIONER KING: (Indistinct words).

MR FITZGERALD: And – and – yes. And look, I don't think – I know the Commission doesn't tend to (indistinct) wealth transfer type issues because it's not particularly (indistinct) to what you do, but I do think that, you know, those equity and ownership arguments do fade with the airports if you were to want to run down that rabbit hole.

COMMISSIONER KING: Yes, okay.

COMMISSIONER LINDWALL: Anymore questions?

COMMISSIONER KING: Just on financial indicators.

COMMISSIONER LINDWALL: Yes, that's fine.

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COMMISSIONER KING: Yes, so in our report, we used a range of financial indicators to try and estimate or provide evidence of whether there was market power or whether there was the airports were taking advantage of their market power. I was keen for your views on what are the financial indicators that really – the investors and the airport boards pay most attention to, and if you've got views on – well, did we choose a decent set? Have we missed obvious ones? Anything along those lines.

MR FITZGERALD: Look, I think maybe with some regret, I think we're all drawn to the return on invested capital of measure of the aeronautical till. And I think that's because we're somewhat conditioned that that is the – the point that placed a first look. I note in passing that you know, even the margins are still used by others, but I think I can say that there's really no economic merit in - in such a - - -

COMMISSIONER KING: Well, (indistinct). He doesn't invest in companies and boast about their effort to (indistinct).

MR FITZGERALD: Yes, no, absolutely, and you can certainly buy (indistinct). There's no - investors know well that even management teams incentivise (indistinct), are ones who want to spend your capital unwisely. But, so return investment capital is probably the overall benchmark financial indicator. I think where our opportunity, and where we're moving as an industry and particularly the airports that I am close to, try to move away from the financial indicators to more surface quality type indicators, and I think BARA has been incredibly constructive in pushing airports to, you know, get - get more definitive, more measured, more measurability into the quality and service indicators, as - as a way of, you know, of demonstrating value for money.

Value for money is that concept of price and quality, and I think for too long we've - the price element of it has been the - has been the dominant factor. I mean, at a board level, we look at, you know, return by - when you're trying to manage a business in the very short run, you're looking at real measures on the passenger basis, because really, you have some control in the medium to long term of passenger numbers, and airports put a lot of effort into trying to grow passenger numbers, and in that sense, airports are aligned to their communities, because growth is good for airports.

But in the short term, you have relatively little control over the passenger number, and therefore, when you're trying to pull the levers of a business, to try and extract from that, we look at per passenger measures, and I certainly like looking at real capacity measures, rather than nominal.

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COMMISSIONER KING: Anything else?

COMMISSIONER LINDWALL: Well, one other final question, Steve, is about jet fuel. Now, you know that many of the airports, the major airports, they JUHI with the joint venture owned by peak companies. Darwin has moved towards buying back the asset by the airport. Melbourne's moved to open access. As an investor, do you think you have an appetite for the airport actually owning the infrastructure for fuel and supply?

MR FITZGERALD: Yes. And I think that's - look, I think that, my view from an investment point of view, is that that is - that is a good place to be in terms of having someone who can be more the honest broker, to encourage competition in those related markets, and I haven't observed that concentration in those markets as being something that pushes up price to - to airlines, and that's bad for airlines. We want airlines with cheap prices, we want - we want affordable fuel in our airports to encourage growth in airlines.

It's particularly important for international carrier, who are taking up relatively large amounts of fuel, have relatively constrained abilities to tanker fuel between ports, depending on their ranges, and in the airports I deal with, and I include Melbourne in this, but I'm closer to Perth and Gold Coast, particularly that low cost segment, and even that sub-segment of long-haul, low cost. Being able to make sure that they have a competitive fuel offering is absolutely critical to (indistinct), and therefore whether they serve your airports or not.

COMMISSIONER KING: I think that's great, and thank you very much.

COMMISSIONER LINDWALL: Thank you, Steve.

MR FITZGERALD: Thank you.

COMMISSIONER LINDWALL: Now, thank you again, Steve. I think we have Virgin was to appear, is that correct? Something like that.

MR STEEDMAN: (Indistinct).

COMMISSIONER LINDWALL: Happy to answer any questions after the statement?

MR STEEDMAN: No, I think we're going to rely on the statement.

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COMMISSIONER LINDWALL: All right. Just identify yourself and make your statement about your client.

MR STEEDMAN: Glen Steedman from Virgin Australia. So we'd like to just make a statement today, and that statement's really just forward our submission that's been sent through to you, and also the A4ANZ, their submission. So, firstly Virgin Australia has a strong preference to negotiate our commercial agreements to the betterment of both parties, and that's the way we approach our negotiations. We believe that gives us a better pro-active and long-term relationship with the airports. However saying that, we don't always reach a position that we believe is equitable to both parties.

PC, as itself recognised, that the airports are in the position of a natural monopoly, and we provided examples in our submission, where we outline that. We also think that PC is incorrect in its assessment that the market power can be controlled through the withdrawal of an airline from an airport. We don't believe that is the case, and we believe that an airline would suffer significantly more detriment than the airport if that occurred, and that's - that lack of account of our market power effectively leaves the airport free to exercise their market power - excuse me.

So, we are not seeking the re-regulation of airports. We don't believe that's beneficial, but we are looking for a circuit breaker we can activate when negotiations break down. We do not share the concern that a negotiate arbitrate regime is inefficient, or it won't work effectively. A well designed negotiate and arbitrate framework will encourage information sharing and genuine commercial negotiations between the parties from the start to the finish. I think the effective thing is we want to use the arbitration mechanism as a way of starting negotiations on the right foot.

And finally, Virgin Australia would encourage the PC to reconsider its position on the negotiate arbitrate regime. We believe that will deliver the best benefit for the traveling public of Australia and the broader economy. And apologies for not taking questions,

COMMISSIONER LINDWALL: No, no, that's perfectly fine.

MR STEEDMAN: We haven't represent ourselves, about that (indistinct) - - -

COMMISSIONER LINDWALL: You're not prepared for that, and that's - - -

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MR STEEDMAN: So we'd just like to make that submission, and rely on the reports. Thank you very much.

COMMISSIONER LINDWALL: Thank you. Now, does anyone else want to come up and have their say? No one wants to rebut or agree vigorously with (indistinct)?

COMMISSIONER KING: Going, going.

COMMISSIONER LINDWALL: All right, in which case I think we'll adjourn the proceedings, and we resume in Melbourne on Thursday. Thank you, everyone, for being here.

MATTER ADJOURNED AT 4.47 pm
UNTIL THURSDAY 28 MARCH 2019

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Australian Government
Productivity Commission

PRODUCTIVITY COMMISSION

ECONOMIC REGULATION OF AIRPORTS

MR P LINDWALL Commissioner
DR S KING, Commissioner

TRANSCRIPT OF PROCEEDINGS

AT PC OFFICES, LEVEL 12, 530 COLLINS STREET, MELBOURNE ON THURSDAY 28 MARCH 2019 AT 8.56 AM

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COMMISSIONER LINDWALL: There's a little bit of an introductory spiel that we need to go through so I'll welcome you all here. So good morning, welcome to the public hearings for the Productivity Commission inquiry into the economic regulation of airports. I am Paul Lindwall and Presiding Commissioner of the inquiry with Stephen King here is my fellow Commissioner. I would like to say that we're on the lands of the Wurundjeri people of the Kulin Nation.

The inquiry started with a reference from the Australian Government in June 2018. The purpose of the inquiry is to investigate whether the economic regulation of airport services promotes the efficient operation of airports and related industries. We released an issues paper in July 2018 and have talked to a range of organisations, individuals and others with an interest in the economic regulation of airports.

This has included representatives from the Australian State and Territory Governments, local councils, airports, airlines, industry representative bodies, academics, researchers and other individuals with an interest in the issues. We held public hearings focused on competition in the jet fuel market in Sydney and Melbourne in late November 2018 and following the release of our draft report in February 2019, we, the Commissioners, called for further submissions and is undertaking consultations along with these public hearings. We received 88 submissions prior to the release of our draft report and about 30 since then and I think they're still arriving of course.

We're grateful to all of the organisations and individuals who have taken the time to prepare submissions and to appear at these hearings. This is the third public hearing for the inquiry this year. Following this hearing, another day of hearing will be held tomorrow here in Melbourne. We'll be then working towards completing a final report having considered all the evidence presented at the hearings, in submissions, and through meetings, and other work that we undertake and the report will be submitted to the Australian Government in June 2019. Participants and those who have registered their interest in the inquiry will be advised of the final reports release by the government which may be up to 25 parliamentary sitting days after completion.

The purpose of these hearings is to provide an opportunity for interested parties to provide comments and feedback on the draft report, or what other people say. We like to conduct all hearings in a reasonably informal manner but I remind participants that a full transcript is being taken. For this reason comments cannot be taken from the floor but you will have the

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opportunity at the end of the day if you wish to come up here and have another say or rebut or concur with someone else's presentation.

Participants are not required to take an oath but are required under the Productivity Commission Act to be truthful in their remarks and they're welcome to comment on issues raised in other submissions or anything else they wish to that's relevant to the inquiry. Transcripts will be made available on our website after they've been processed and submissions, of course, are also on our website. For any media representatives attending today, we have some general rules. Please see one of our staff for a handout which explains those rules.

To comply with the requirements of the Commonwealth Occupational Health and Safety legislation, you are advised that in the unlikely event of an emergency requiring the evacuation of this building, you will listen for instructions over the P.A. Follow the exit signs to the nearest stairwell and lifts are not to be used. Please follow the instructions of floor wardens at all times. If you believe you are unable to walk down the stairs, it's important that you advise the wardens who will make alternative arrangements for you.

Participants are invited to make some opening remarks, preferably not much more than five minutes. Keeping them brief will allow an opportunity for us to have a conversation about these submissions and your points. So now I'd like to welcome Melbourne Airport. Would you like to introduce yourselves for the record and make your statements.

MR STRAMBI: Good morning.

COMMISSIONER LINDWALL: Good morning.

MR STRAMBI: Thank you, Mr Lindwall and Mr King for having us here today. We're both very pleased to be here. My name is Lyell Strambi. I am the chief executive officer and managing director of the Australia Pacific Airports Corporation, the parent company that owns and operates Melbourne Airport under licence from the Commonwealth government. With me today is Lorie Argus. She's our chief of parking and ground access.

I'd like to start today really by thanking the Commissioners and their staff for the terrific work and time that's been spent on this inquiry, all of the effort that's actually gone into it. The inquiry itself does form a really important part of the regulatory environment in which we operate within. An engagement on substantive issues has been of high quality. This time round your job has been made harder by the bluster and noise that has

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accompanied this review. But your job clearly is to look through the noise and assess the facts. And the facts show that the existing light-handed regulatory framework should be preserved.

When you look back at what's actually been achieved under the system of regulation, the facts show that it's delivered strong outcomes for passengers through more competition resulting in greater choice and cheaper fares; it's delivered for airlines through the delivery of capacity and improved facilities that allow them to reduce costs in their businesses; and for airports through sustainable returns for our investors. And then finally, and probably importantly, for the Australian community through the economic development and employment that aviation (indistinct) actually generates.

In 1997 when Melbourne Airport was first privatised, there were some 14,000,000 passengers travelling through the airport in any one year. Only one in seven of those flew on an international service directly out of Melbourne. Of course many more were flying internationally, they just didn't have the option of flying internationally directly out of Melbourne. Usually they flew somewhere else to join an international flight.

Today the overall number has grown to over 37,000,000 passengers and in fact we're getting very close to 38,000,000 passengers. But importantly with 11,000,000 international passengers now flying out of Melbourne and that's almost one in three; so from one in seven to one in three. And while it took around 37 years to reach the first 5,000,000 international passengers, it's only taken another ten years now to achieve the second 5,000,000 passengers so not hitting in excess of 10,000,000 annually.

This enormous growth that we've seen has been delivered largely through incremental investments to get more efficient utilisation of existing assets. Like many airports that were privatised in the late nineties, we were lucky to acquire an asset that actually had some headroom in it. We've grown our capacity at the airport by augmenting the existing infrastructure by extracting greater efficiencies through better planning and innovation. By being able to grow into this legacy infrastructure, it's had many benefits and it certainly allowed expenses to be kept low. And another benefit was that the base infrastructure costs were booked in 1960's values when that airport was developed, on what were empty paddocks, and construction was relatively simple and cheap at the time.

But the scale of that incremental investment since, required just to really grow this asset in line with the market, should not be underestimated, it certainly is significant. The book value of the aeronautical assets has increased since privatisation from some $460m to $2b today. That's under

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a world where we've been efficiently using the assets available. As we have demonstrated, passenger growth has been strong and investment in infrastructure has managed to keep with that demand. This investment has helped to create an environment in which strong competition has seen international airfares decrease over the long run and that is why the facts show these outcomes of Melbourne Airport and probably similar to other major airports, underlying the effect of this current regulatory regime.

This regime has evolved and matured in the 15 years since it was first introduced. As well, agreements have become far more sophisticated and the best elements of deals struck in various places have been shared and incorporated in future or in current deals that are being done. I think our recent ASA is a really good example of this because it contains a number of new features that have been introduced to improve the consultation process and share more risks, as examples. Talking of the risk sharing, our last agreement includes service failure rebates and also annual price resets on capital expenditure.

Now, these additions were added to address the issues that were raised during the consultative process and actually, in a lot of cases, actually to the benefit of all parties including the airlines. The risks of the proposed mandatory negotiate-arbitrate framework would significantly outweigh any potential benefits. Such a framework would almost inevitably change behaviour and it does have the potential to be gamed resulting in very poor outcomes. Given the complexity that's inherent in aeronautical agreements, just think about it: it often involves multiple parties and we're not just talking here about airports and airlines but even within the airline community. Very different parties with very different motives and very different goals.

And then you think about the variables which you have to deal with, which are many complex and often interrelated. A great example of that is the interrelationship between passenger volume variables, capital spend and operating expenditure and you can (indistinct) more passengers should drive more capital expenditure. Capital expenditure often can be to reduce operating expenditure so you're trying to solve a very, very, complex and multidimensional puzzle with multi-partners. Given the complexity that's inherent in those aeronautical agreements, it is still preferable to take the necessary time to reach a good outcome. I know some have argued that a negotiate-arbitrate process would be quicker and I think that's something we agree with, but quick is not necessarily good or better. So our preference is to have a process that actually works and delivers the right outcome even if that takes a little bit longer, the stakes are so high.

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Again just reflecting on a negotiate-arbitrate framework, such a regulatory approach would really only serve to distract from the progress being made within the existing framework and put future investment at risk without any tangible benefits for passengers or the community. There's been some comments on parking and ground access and we can say really clearly that the price of parking at Melbourne reflects the need to effectively manage congestion. It also reflects the convenience of amenities provided and competition from other services provided either near or even at the airport.

Our parking business is subject to strong competition from at least 15 different off-airport car parks. Certainly from other modes of transport, such as taxis, buses or rideshare and even from our own products of free pick up and drop off. We are definitely seeing disruption of this space at the moment. Last year total car parking transactions declined despite an additional 1,600,000 passengers flying through the airport. This, I think, highlights changes in customer's preferences. Passenger demand, particularly being strong for rideshare at the moment. This alternative mode of access is one that we've actually taken submitting of steps to facilitate.

Investment in new facilities has included for rideshare, the indicated of dedicated holding areas and pick up zones. We have also invested in a taxi management system to streamline taxi pick-ups. We've upgraded facilities for car rental operators. We've also invested in the free options and in some cases actually sacrificing parking revenues and car parking space to provide these facilities for free. That's been driven really to reduce congestion and to provide passengers with choice and better and safe access to and from the airport. And also at the airport we've been a very strong advocate for rail. A project which will introduce even greater competition but more importantly choice between modes and enhanced passenger experience and frankly meet an expectation on major airports such as ours.

So while I respect the Commission has reserved its judgment on ground access at Melbourne, we have certainly provided significant evidence that through pricing and consultation with a myriad of operators, we are prioritising the passenger with a clear focus on congestion management choice and safety in what is, and obviously, a very constrained environment in which we actually operate the front of our terminals. Now, we agree with the intent of all of the Commission's draft findings or recommendations however we do propose an alternative approach to providing additional financial monetary information and that is to use the existing ministerial instructions that already exist rather than promoting a change in regulation.

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We think this just provides a simple lower cost approach and it's already been used in monitoring of aeronautical and car parking prices. Other than this one change we have no other concerns with any of the recommendations in the draft report and we've set out the detail behind this position in our response to that draft report. So now looking forward, Melbourne like most airports faces a very significant growth challenge. Our projections are that our passengers forecast almost double to around 67,000,000 over the next 20 years.

We're approaching, and I guess a compounding factor is, we're approaching the practical capacity of some of that legacy infrastructure that we were so lucky to have. At the same time we also have a need to now replace ageing, hopefully not an emergency, ageing 50 year assets with new for old. Often with upgrades they have to now meet modern environment construction and safety standards and by the way we have to do this in a live operating environment, it's a challenge. So in order to meet growing demand we are going to require a step change in infrastructure investment. The most obvious example at Melbourne is our third runway and in that particular case we can't add incremental runway capacity, we had to build a whole new runway that almost doubles capacity of the airport the day it opens.

Airlines who are not seeking to grow potentially won't like this. But it's important that all stakeholders in our sectors, be airports, the airlines, the government, the regulators, really need to approach this next phase of development with a clear understanding of these challenges. The existing light-handed regulatory environment has delivered to the Australian community since 2002 gives us the best chance of success. This major investment in long life infrastructure requires a stable, predictable, regulatory environment. Unnecessary regulatory change creates risk for investors. It increases funding costs and it compromises the delivery of economic infrastructure at the time it's needed.

We must remember that the ultimate beneficiary, our first and last priority, must be the passenger. We succeed commercially by providing an airport where more airlines can fly more people to more destinations. Regulatory stability is critical to facilitate the necessary investment to continue to make this happen over the next decade and beyond. Thank you.

COMMISSIONER LINDWALL: Can I just ask you about countervailing power. Now, some of (indistinct) have said that the airlines have no countervailing power against the airports and Qantas the other day gave an example of Newcastle where (indistinct) because of the pilot shortages, withdrew services from Newcastle and immediately was

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replaced by Virgin Airlines so is that an example that you would agree is an example of not having countervailing power?

MR STRAMBI: I really can't talk to the Newcastle example but I can - - -

COMMISSIONER LINDWALL: Hypothetically if one airline withdraws services, another one would come in with similar service.

MR STRAMBI: Yes, I don't believe that is always the case. I've heard people say, "Of course we can't stop flights to Melbourne, therefore we have no power". Well, to be honest having been in this industry for decades and actually being on the other side of the fence for decades, you know, on the airline side of the equation, airlines will make lots of choices around fringe services, for example, it might be just marginal. You know, clearly with an airport like Melbourne, a major airline will have to have Melbourne in its itinerary. But does it have to really do those fringe services and they could be used tactically to exercise some power but I think there's a lot of other ways in which that power is actually exercised. It doesn't just have to be (indistinct) services.

COMMISSIONER LINDWALL: And presumably if Melbourne's growing and other airports are growing, an airline has the choice about where to place any additional growth that he might see too.

MR STRAMBI: Yes, it's really interesting. You compete very hard for traffic, particularly international traffic, and it's often not against the obvious. You know, people say, "Oh you're competing in Sydney for traffic to Australia"; well, when they're determined to come to Australia that may be the case although there are other good airports in Australia (indistinct) destinations of Australia but I can't tell you how many times I'm out on the road talking to airlines and governments and you're competing against Paris, you're competing against New York, you're competing against a lot of destinations and airlines - the great thing about running an airline is you have an asset that you can move around to where the market actually is. We don't have that luxury as an airport.

COMMISSIONER KING: Sorry, just to follow-up on one of the things you just said. So you said there are other ways that countervailing power or power by the airlines can be exercised other than withdrawal of service. I think I may have your words quite correct. Do you mind just expanding on that, so you said that they could withdraw "fringe" services, what other sources of market power, bargaining power, could they have?

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MR STRAMBI: Yes, whether it meets your definition exactly. The negotiations are extraordinarily complex. There are all sorts of different perspectives that could be brought to bear. So an airline that has a substantial sizeable operation in your airport could continue to grow by juggling its aircraft around between different service and could continue to grow by upsizing aircraft. It has a lot of different ways of growing. That's real power when it comes to the table when you're talking about growing the airport facilities for the benefit of the entire community.

And so people could come at this with very different motives and very different positions around that to say, "We can continue to grow. We don't need that growth asset. We can grow within (indistinct) that we have" and in fact sometimes that might be an advantageous way of keeping competition out so there's a real mixed bag of market power out there in terms of not just - it's not a discussion, I think, solely between airlines and the airports, it's also between airlines themselves so it's very complex.

COMMISSIONER KING: The negotiate-arbitrate framework was introduced from the east coast gas market about 18 months ago and since them agreements have been concluded and they have been not having to go to arbitration so does that suggest that perhaps you're overstating the concerns about negotiate-arbitrate?

MR STRAMBI: Let me address this in two different ways. Look, I'm not a gas regulation expert, I know little about it. But from what I've learnt and read it's actually quite a different problem. It's very different in the context of there is no inability to deny access at an airport whereas in the gas
pipeline - - -

COMMISSIONER KING: Do you mean no "ability" to deny access at an airport"?

MR STRAMBI: Yes, yes.

COMMISSIONER KING: I thought you said "inability" to deny access at an airport.

MR STRAMBI: So I might have used a double negative, sorry. Thank you for the correction. No, but there is no ability to deny access, we have to allow access and I'm not sure that is the case in the gas pipeline case. I think it's also a different problem which is actually trying to be solved, they don't believe it's a capacity conversation. So our problem is far more complex than that. But maybe let me answer it a different way and come

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at this from a negotiate-arbitrate perspective. I know we talk a lot about the costs and the time of these arbitration techniques as being a big barrier, but I actually (indistinct) it as I think the biggest problem is the risk of regulatory failure. That's the real concern here.

So if I think about the way the system works today, is the parties will sit around the table and actually start from quite wide positions, very different perspectives. You may start with your version of the building block models but it actually starts from quite different positions. What you've got though is very well informed and very smart people in the room then and the task is to how do you move those positions together so that you can meet in the middle and often at the very end you've still got a gap and that's where you start to move away from the building block model and you get to a situation of actually making trade-offs to say, "What's important to you but maybe less important to me that I'm prepared to trade" versus "What's important to me and less important for you that you might be prepared to trade" and you get to that final conclusion. But it's two parties working on actually getting to the right answer.

The great concern for me around negotiate-arbitrate is it's a different game completely. To stare into that and say okay, knowing that you're going to potentially go to arbitration and a very low effort to get to arbitration, who is going to move towards the middle to only then be arbitrated between that position and follow a resting point. And in fact your resources, those great resources, that great knowledge, the people with skin in the game will get very, very, focused on actually their starting position and arguing for their position in arbitration rather than actually being at the (indistinct) of the problem so now all of a sudden the adjudicator is lumped with making all of those trade-offs, all of those concessions, because the parties actually are starting with, "How do I maximise my position going into arbitration?" not, "How do I solve this problem?" and that becomes (indistinct) and I can give you an example. I did witness this a little bit in the UK when I worked there and I was on the other side of the fence of the airlines.

It ultimately doesn't work for all of the parties unless - it's very hard to work for all the parties. What happened there was, they actually did have some very good techniques around consultation in the early part of the process so through the (indistinct) the players. But you knew that you were always going to end up in front of a regulator in that case, at the tail end of it, so you never gave away too much, you never really sought the balance - you actually just worked up to make sure your position was one you could defend in that regulatory test at the final end of the game and it does influence behaviours. So I stare into this and say, "Why are some people proponents for this?" and I'm not sure I can figure that out.

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My suspicion is that some parties, some clever parties, stare into this and say, "In that world…", if you use the term "gaming" involved and how to play it, some people might believe that they can play it better than others and therefore win in that process and it's the only reason I can understand why it would be desirable because the risk of regulatory failure is huge. And by "regulatory failure" it means just a wrong decision when you're trying to decide volumes, capital, operating expenses, and, you know, in a messily complex world and I'm not sure how it works when you've got other parties who are not in agreement that it's part of a network problem that you're actually trying to solve.

COMMISSIONER KING: Sorry, just to clarify something that you said. You used the word "gaming", what do you mean by "gaming"?

MR STRAMBI: Yes, well think about - I probably should use a different term because actually "gaming" implies something negative. Businesses and teams and management are paid to optimise an outcome, right, so if your lens is, "How do I optimise the outcome?", I will make arguments to optimise the outcome. And if that's what this process is all about, making strong arguments to optimise your outcome, that's all you'll be focused on. You won't turn those energies into, "How do we optimise a compromise that actually works for everybody" and from what I've seen already through this process, it's really interesting.

I don't see too many occasions where, you know, we work really hard and it takes a long time to get the parties to this final point of actually resolution and it does feel like at the moment nobody walks away - you don't walk away in a scene where everybody walks away happy. What it tends to be is everybody walks away a little unhappy and probably that's the best result that you can hope for because it's this massive balance in compromise you actually have to achieve. Everybody, you know, kind of walks away thinking, "I didn't quite get all I want" and that's probably the right outcome actually.

COMMISSIONER KING: But you've said the current system works and gets compromised on an outcome, the case before the Western Australian Supreme Court between Perth and Qantas tends to suggest the opposite. That's a situation where the parties have ended up before a judge trying to work out differences and indeed to act as an arbiter on what Qantas should be paying to Perth. So doesn't that run counter?

MR STRAMBI: No, no, it's a good question, Commissioner, but I think there's an obvious answer to it which is: firstly, there has to be a pathway as a last course of action and there are already in the current environment.

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You can take court action, you can declare - you can seek declaration, you can take those paths. I think the fundamental difference here between even that action, I can't speak for Perth and I wouldn't dare to and I think a good question to ask them, however putting myself into that place, you say what you don't want is a system that makes that your first port of call not your last port of call. Because, as I say, going to that there is a real risk of regulatory error and I think all parties are staring into that now as to what that error might be. And then you must think through, "And what happens if this action becomes not just a once-off event but actually a regular event?" and that's the danger here because you'll get learned (indistinct) behaviour as a result of that.

So for example, let's say the arbitration has done something very simple and it doesn't go the airport's way and actually let's say it gets a piece of asset that it has to deliver at a poor return. You can live with that, right. In the overall context it's not the be all and end all. The problem is though, when you go for the next round of a conversation around something, that is going to change your thinking going in there and it's also - if you think about it as a management team going to their board saying, "Well, we didn't get a great return on that and in fact we are actually now (indistinct)", whatever the outcome that you might not like, whatever it is.

You then say to the board, "But we're going to go forward with another thing", well then clearly they're going to say, "Well, is that really, really, worthwhile taking that risk?" and this is the danger is that this (indistinct) but I think that fundamental difference is you have got the mechanisms today. They're there but they're rarely, rarely, used. I would say they're only used in an extreme situation when everything else fails and that's right because it's not the best process at the end of the day, much better if the smart parties in the room were actually reaching that combined outcome and conclusion.

COMMISSIONER LINDWALL: When you have negotiate-arbitrate and you compare it with a status quo, would you posit, speculate here I guess, would you lead to less investment and more congestion or more investment and less congestion to compared to the status quo? Is it possible it can see more investments than you would have currently planned?

MR STRAMBI: More?

COMMISSIONER LINDWALL: Yes.

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MR STRAMBI: It's an interesting - the thing is any of these variables can go in its direction but let's - and it is nothing more than hypothetical. A regulator might be inclined on the basis - I'm not sure who they're decided for so I'm just going put that caveat out there because who's bringing the arbitration and what's the nature of the arbitration that it actually represents? Because it might be one topic for the one airline but it actually might have community interest. Let's go to the extreme and say they're there for the community interest, then it might actually lead to - and who's the expert in the room? How does the arbiter decide what is the right level of capacity to introduce given the passenger volume coming out to the airport but it's complex, it's really complex. Because every airport in every case is going to be different, every asset's going to be different.

This ten per cent growth rate doesn't mean a ten per cent growth in gates. Maybe in one airport, yes, maybe in another airport, no, because of a whole lot of different factors in here: the aircraft size, how you utilise (indistinct) all sorts of things. So we're going to ask an arbiter to decide that or adjudicate it to decide it. I think that's why regulation in this space wasn't the best answer in the first place because you've got people making decisions that probably lead to, "Well, what's in the national interest", "Well, let's have a Taj Mahal" because that will present our nation better to the world, is that the right thing to have? But it could go the other way so I'm not - this is the danger, I think it could go anyway, maybe not the right way, it may result in regulatory failure - - -

COMMISSIONER LINDWALL: (Indistinct) negotiate-arbitrate (indistinct)?

COMMISSIONER KING: (Indistinct) land side?

COMMISSIONER LINDWALL: Yes, go onto land side, yes.

COMMISSIONER KING: So just some of the issues with regards to land side access. You said that it's driven by the need to effectively manage congestion. One of the things that stands out when you look at car parking prices, which are obviously a large media issue, when we do our comparison to other venues it seems, for example, the short term less than say three hours seems comparable with other venues but the at terminal car parks, those day long charges so if you park there all day or park there for a couple of days at terminal on the drive up rates, they do seem to be out of line with what you'll get at other venues or equivalent, you know, places where you would have scarce parking so can you explain why they seem to be out of line or you may say they're not out of line, but - - -

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MS ARGUS: Yes, sure. We've done a fair amount of consumer research that says that that is the right price but taking your point, I think what we have to balance is occupancy and congestion. So you can imagine a world where if we've got 23,000 car park bays and equally our competitors together have the same amount, if you had a price that was too competitive then you could imagine a world where you've got a queue of congestion and not enough car park bays to offer to that convenience traveller. The real challenge for us is to make sure that when you're a drive up customer and you want to go to that convenience car park, there is an expectation that you have occupancy there for that customer driving up.

So we really balance the utilisation and the congestion as well as the right price but when you compare - well, you can't really compare it to I've seen in the report around hospitals or even an entertainment location, because we work on a 24 hour basis so one day parking is in fact two days of parking because a one day price at $51 means that if you come in at 9 am in that morning, you have that car park until 9 am the next morning and that really means that the really early morning peak of meeters and greeters may miss out on that car parking bay.

So I think in the report, the Rod Laver example for me is an interesting one because their one day parking is cheaper than their event parking but they're driven by a consumer result which is you're going there for an event so you will be there for three hours and you will pay your $30. They may have a one day price that's more effective than that but there's no events there so therefore you might not be going there. And equally when you compare hospitals, I think it's about what drives that market so their three hour price is very similar to their one day price which says to me they're maximising their market which is likely to be the three hour market. So I think it's quite difficult to compare.

COMMISSIONER KING: But I think in the opening comments it was stated that the utilisation of car parks have gone down in the last 12 months. Doesn't that just indicate directly that your prices are too high?

MS ARGUS: Well, I think that we compete. So we compete with the free public pick up and drop off as an example so you may choose to have a loved one drop you off and pick you up instead of park, you may choose a rideshare option, you may choose a bus option. So I think that our decline in parking performance is genuinely competition particularly when you look at we've reduced our prices by up to 20 per cent over the last 18 months particularly in that market because we heard from that consumer that they thought that price was not competitive enough. But ultimately

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there is multiple choices for one day parking including the long term car park which, yes it has been named "long term car park" but you can park there for $25 for a day and still walk with close proximity to the terminal.

COMMISSIONER KING: So you've argued it's competition and part of the competition is I think, again, in the opening comments it was mentioned there was at least 15 off-airport car parks that are competitive but you control a critical part of their price which is the price to pick up and drop off passengers using their shuttle buses at the terminal. The off-airport car park operators that raised concerns with us about the land side access at Melbourne Airport, that the prices have gone up despite the fact that the facilities haven't improved and surely there's, you know, just an obvious competition problem when you control a direct cost of your competitors, those same competitors who say are keeping you honest in your car park.

MS ARGUS: I think if you look at our car parking, I think it's important not to lose sight of the fact that we're only 13 per cent of the mode for people's choice to get to that location and we compete with off-airport just like we compete with our own car parking but I do think it is a different product as well. So there is a convenience location car park as well as off-airport decisions but if you look at the access fee, we attribute that equally so - and including it's quite a small proportion of what your off-airport would be charging, but we have communicated and consulted with all of the bus industries.

I mean, there's over 300 companies that we work with at the airport, to say, "Well, this is the cost of our capital and this is the cost of maintaining those lanes, ensuring that they've got the security for congestion to keep flow moving, ensuring public don't go into those areas", we've built up and shown to that community, "Here is our proposal for what we're paying in capital and operating costs which works into an access model for that fee" and that's similar for all of those buses. So arguably it's not just for the buses that we compete with, it's for all of the buses in that location that would pay that access fee.

MR STRAMBI: It's a cheap shot too to say that we've not invested and you'll be charging for things. You know, we've created a multi-modal transport hub at terminal four which the ground floor is allocated to that mode of transport largely. So that's not free, that's a big investment and it's an investment in a competitor's product. But that's not what's driving us, what's driving us is actually access to the airport because throughput at the airport is really important. There's no point having an airport that can grow to 60-70,000,000 passengers in the next 20 years if nobody can get there; that's the bigger drive actually and also the criticism we get for

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congestion is the forecourt, means we do have to make lots of investments and lots of tweaking.

Now, for example, at the moment we've just invested in millions of dollars' worth of dynamic signage to try and optimise the use of that particular space. Now, if we were minded to boost the car park, we'd spend that $6m or more on the car park not on that forecourt, we'd make it even more congested. Our actions show that we're actually trying to deliver a better product for all of the different segments because it's actually important for the overall working of the airport. There's no point optimising a car park business if your airport fails and that's the thing that really drives us and I think that's why we're very much in line with the traveller interest here. You know, our business is really linked to the success and the volume of travellers coming through here and nothing we should do should constrain that. So if you're not behaving well in the car parking space, (indistinct) so if you're not behaving in the (indistinct) access space to (indistinct) your car park up, then you're potentially risking airport throughput and that's silly economically.

COMMISSIONER LINDWALL: Can I move onto quality of service and that was an example of it but obviously you have a lot of range of customers from passengers to retail clients, airlines and so forth; what type of measures do you have to try and give yourself an incentive to improve the quality over time and meet your customer expectations better in contracts, for example?

MS ARGUS: So on the land access side, I think there's - we use the same quality measures that we use for aeronautical which Lyell can touch on through the aeronautical agreements but equally we do the same land side so we have regular quality and mystery shoppers, we look at the cleanliness of it, is it intuitive to get through the experience, in particular to Lyell's point on congestion, we measure everything from throughput to access to cleanliness to safety and security and those are measured on a regular basis as well as net promoter score for our direct customer relationship with our parking and then there's the aeronautical agreements.

MR STRAMBI: And talking more broadly about quality across the airport, I mean, this is a conundrum which is also part of that commercial consultation we actually have with our partners at the airport. And again it's complex because it's different people at the table here but let's talk about the airline piece of it. It's an important part of the conversation and you are dealing with partners who might have very different views on what quality actually is and this is one of the dilemmas you have here. One of the challenges we have as the airport is we are often the last person to blame when things go wrong.

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I had a problem with Melbourne Airport. I didn't have a problem with an airline at the airport, I had a problem with Melbourne Airport. So you've got this incredible balancing that you're trying to do which is you have to facilitate your customers and I understand this very well, you know, given again my history, that we'd have to enable them to be able to differentiate their product and find a sweet spot in the market that works for them so we have to be able to give that flexibility and at the same time there are others who are saying, "We want absolutely the lowest possible cost here, hang the quality" because you'll get blamed for it, Melbourne Airport.

And we have a live example of that at the moment. You know, we don't always get it right but please - you know, I think the system works very well but we don't always get it right and we're always looking for ways to improve that. When we were designing terminal four, and I would argue as a low fares terminal experience, it is a great experience but it was designed with travelators to take people out to the more distant gates. A certain airline, remember these are our customers who I'm talking about here, certainly one felt that that was not needed. You know, it didn't match their business model because customers want the lowest price and we listened to them and we took those travelators out but not only that, we also took the structure out of the building to produce the lowest cost building and now we, Melbourne Airport, get the complaint that says, "It's a long walk down to those gates" and I think we got it wrong. I actually think we got it wrong in that particular case.

And so there's always this trade-off. You do have to listen to your customer, there's no doubt about that because at the end of the day their business model is reliant on being able to square the circle in terms of incomes and expenditures. But the challenging bit is this: what is the baseline? What is the right baseline and that's a role that we have to play, I think, as an airport. This is not about gold plating. This is about where that right lower level actually is and the thing that does motivate us enormously is the pressure that we get, the brand damage that happens to us when we don't get that right.

COMMISSIONER KING: Can I say it is a long way.

MR STRAMBI: And the facts are that for those particular customers, if you actually measure the distance of what they were travelling previously, it's the same distance but it doesn't matter, it's a long corridor and it feels long and these are - no, I'm not arguing your point. I said at the start we got it wrong, right, we should have put a travelator in.

COMMISSIONER KING: Nothing's ever (indistinct), yes.

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MR STRAMBI: But again though, that discussion, that debate, Your Honour, it might have actually brought us to a slightly different answer so, let's be smart. Now, what we're doing halfway down the way to actually make it a relief for passengers on the way, you can find different answers here but gee, you're going to have a world where an adjudicator's trying to decide these things, I just struggle to see how it's going to work.

COMMISSIONER LINDWALL: As long as you don't put in an extra type of diagram that makes it look like they're forever walking. Could I ask about, because we're running out of time, jet fuel. You've announced or you've moved towards more of an open access for the jet fuel JUHI at Melbourne Airport. How has that gone and has it been manifested with new interest in trying to enter the JUHI?

MR STRAMBI: So again just to be clear here, our role in the provision of aviation fuel was actually a relatively small one. We lease the land on which those facilities are built. We don't own them, we don't control and we don't operate them but we had a problem. We had a problem where there was a constraint of supply in fuel at Melbourne Airport and there were very difficult access provisions, or very little opportunity for new access to those facilities. So in renewing those land leases, we argued for and got better contractual arrangements around those things. So, for example, open access: other companies can actually now come and apply to use that facility which is great; another company can come along and bolt a new pipe into that facility which is great. So we kind of created that framework.

I think at the moment there are other problems we were trying to solve in terms of storage on site and reliability and throughput challenges and I think they're now coming to fruition and looking really good but I think on that access piece, the real question there is, I think it's a bit too early to call, the challenge I think in that JUHI space is there are a number of players in that market but they are really different competitors - I'm trying to think of the right word, they're not on an even playing field even with the existing operators because unless you can give access to the pipes that feed that facility, you're bringing your fuel by road, of course your costs are higher than a pipeline cost, you know, so even that's not great. We'd love to see that improved but we'd also like to see the opportunity if someone's interested.

Now, we've had a number of people express interest. At this stage, as I said, it's too early to call whether those changes there will work because this is a much bigger problem when you're trying to address the fuel market because it's not just the access at the airport, it's all the other pieces

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upstream that you've got to get right as well and we can influence but our role is quite small as I say.

COMMISSIONER LINDWALL: Do you have any final questions? Well, I think given the time, Lyell, we might have to end it there. Thank you.

MR STRAMBI: Thank you.

MS ARGUS: Thank you.

COMMISSIONER LINDWALL: Now, I'm trying to fix this up because we're getting that echo in here. It might be the microphone.

MR STRAMBI: It might have been me moving that microphone forward.

MS ARGUS: No, I don't think so.

COMMISSIONER LINDWALL: Now, we'll call on A4ANZ, we've got Graeme and an Alison. So welcome and if you could just introduce yourselves and perhaps give a statement.

PROF SAMUEL: I'm Graeme Samuel, Chairman of Airlines for Australia and New Zealand.

DR ROBERTS: Alison Roberts, CEO of Airlines for Australia and New Zealand although we might variously be known as "bluster and noise", I'm not sure to use Lyell's point, who's bluster and who's noise but we can work that out at the end. Thank you very much, Commissioners, for the opportunity to present. I do want to open by saying that the tone of the responses from A4ANZ to this draft report is not one that we'd hoped to adopt when we commence the process. We'd hope for a constructive process, a debate of ideas and key policy questions.

Some other stakeholders have approached us, you know, from other airport users to politicians, regulatory, legal and economic experts, have expressed to us a view that any further engagement in this process seemed futile and many were completely discouraged from responding to the report or attending hearings. And I think it has to be said that this is an extremely damaging outcome from a public policy perspective and we're quite sure not one that you would have intended. Obviously we are engaged and as you've seen we've decided to provide a strong response and this is in the interests of continuing our contribution to the

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formulation of evidence informed policy. We don't pretend to speak for all but offer our comments today for your consideration.

When making any decision but particularly when considering big policy questions, there's a tendency towards what's called "status quo bias". As the name suggests this phenomenon is where decision makers stick with or defend what is known. Once made policies frequently persist and are often viewed as a success by evaluators even if they were measured through say as a cost benefit test that was applied to a new policy, they would have little chance of passing.

There's also another type of bias known as confirmation bias and that is those who hold a particular position seek out and give greater credibility to those who support or share the same views. Now, advocacy groups have been known to do this from time to time and we'll cop that but the PC is not an advocacy group. Our assessment is that this draft report, the commentary that's followed, some of the nature of the questions at the public hearings thus far are indicative of both sorts of bias. Now, why we're talking about this? Because these biases have the effect of diminishing independent thought, proper appraisal of evidence and the search for truth. In other words, their presence makes it hard for the Commission to do its job given that your duty is to "*use the best available evidence and the most rigorous analytical techniques to reach its conclusion*", that's from your report.

But most importantly the reason we're talking about this is, as you've heard loud and clear, many of us, both within and outside the sector, were genuinely perplexed by this report and by your comments. We sought to understand how the PC could have arrived at these conclusions? What was influencing the processes in thinking? We don't accept it was laziness, as I think someone suggested on Tuesday, and we know it's not a lack of intellectual ability. We wanted to give words to an explanation for the collective scratching of heads and the general "what-the" that followed the report's release.

Many other submissions coming from a range of interest groups all shared the same theme and we've seen it now coming up on the PC website. It's perhaps best summed up by a quote from one of them. It said, "*We were hoping for an in depth analytical forensic assessment of the practices adopted by these airports and their customers based on actual experience and with real data*". That is not what collectively we got and it should give the Commission cause to reflect, as Qantas said on Tuesday, that the only people congratulating you on the quality of the draft report are the airports. So we offer this as a genuine reflection of what we think has happened and we share it so that Commissioners and the staff might

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reflect on this perspective in the hope that these biases will have no place in the formation of the final report.

We think also that this failure of process comes from the Commission's explicit decision to adopt what you've terms a "philosophical perspective" in undertaking this review. We would ask, "Is that the role of the Productivity Commission?" Sure, as Commissioner King highlighted on Tuesday, there are philosophical differences between regulators on whether a sector should be regulated only if market power is shown to be exercised or the alternate view, whether they should be regulated simply because they have market power to protect society from its potential abuse. But an independent body like the PC should not be taking a philosophical position. Surely if the Commission accepts that there are different positions out there, different positions put by different regulators, it's in your court to weigh up the relative merits of both otherwise it leaves the Commission vulnerable to the very types of bias I've just outlined.

We believe that this has led the Commission to firstly, seek out and treat more favourably any submissions and expert views that are sympathetic to this perspective and to not undertake an economic analysis of the current regime. The draft report doesn't consider the costs of administering the current regime or assess a cost benefit ratio. There's no gap analysis, no comparison of the existing regime to others and there's very little reference to other reviews that have taken a look at this kind of thing. We also think it's led the Commission to ignore other reviews and assessments dating back to the Hilmer review in 1993 which all reached the conclusion that: yes, regulation is necessary for monopoly assets. It would seem that at some point, Commissioner King, you also shared this view in that piece that you authored for the Conversation in 2014 which was titled, "A privatised monopoly is still a monopoly, and consumers pay the price", you said:

> *If competition is not possible then the privatised business needs to be regulated so that it cannot exploit its market power*

We also believe it's led the Commission to describe the prospect of airport regulation in the absence of more evidence of market power exercise as unfair. Naturally, the airports agree. The Sydney Airport CEO on Tuesday argued that any change to the regime was unnecessary as "airlines can more than stand up for themselves in negotiations" and this is a similar sentiment we heard this morning from Melbourne Airport and by Canberra Airport on Monday. That may be a genuine perception of the airports but let's not forget that those comments are made from the position of privilege, that being a monopolist affords them. It's been said that to those in a position of privilege, equality can feel like oppression. Is

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that why the airports are describing the proposal for negotiate-arbitrate as unnecessary and unfair? Because it seems, and we've heard from them, they seem blind to the fact that when they turn up to a negotiating table, the bargaining power is significantly uneven. No one can argue that the bargaining power of a monopolist is not greater than their opponent who's operating in a competitive market.

If the conditions and charges are as reasonable as the airports describe, what are they so afraid of? Perhaps the Commissioners might consider putting that question to the AAA and other airports yet to present. It's rather extreme, and certainly to consumers, to hear proposals for access to dispute resolution mechanisms through arbitration only in the case of intractable disputes remember, described as "unfair" or judging the airports as "Guilty until proven innocent" but it's of even more concern to us that these are words used by Commissioners. No one is being punished here. This is not a case of saying everyone's guilty. As Commissioner Lindwall has said, the gas pipelines have had just one case referred for arbitration in 20 months. Have the 50 plus monopoly gas pipeline operators all been treated unfairly because users have access to arbitration if negotiations don't work out?

I can tell you that the Australian Energy Regulator doesn't think so, the ACCC doesn't think so, Dr Michael Vertigan didn't think so when he recommended the framework designed after extensive consultation and review of alternatives. All of the State and Territory governments didn't think so when COAG adopted the framework. The Federal Minister at the time, now our treasurer, didn't think so when he announced the framework. And finally, the Australian Energy Market Commission didn't think so when it conducted a 273 page review of the scheme nearly a year into its operation. But the PC disagree. Just why, has not been made clear to us. Where is the review of different regulatory options like the one Dr Vertigan undertook over a similar timeframe to this inquiry or the one that the Energy Market Commission undertook last year?

Their terms of reference, if you have a look, were very similar to the PC's. They had to take into account the exercise of market power and long term interests of consumers and like the PC they were expected by government to provide independent assessment informed by best available evidence. But a quick at the consultation questions they asked shows what at different conversation we might all be having today if a similarly rigorous approach had been taken here.

To be crystal clear, nobody, not the ACCC, not A4ANZ, has suggested that we simply parachute the gas pipeline framework into the airport sector. Nor the UK model, which is quite different where you've got the

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arbitrator sitting in the room, we recognise the obvious differences in the markets. It's called a "sector specific scheme" for a reason. But here's where we've got to get real: are the objections to a negotiate-arbitrate regime for airports based on reality? When airport representatives were asked about this in Sydney on Tuesday and again today, they cite gaming, inexpert arbitrators, competition, multiple airlines, as reasons it would be no good. But no one's actually backed that up with actual evidence or even reference to situations from other sectors where this has occurred. Just that we should avoid it "just in case".

Surely these claims are worthy of further scrutiny and surely it's worth looking at the Vertigan review which considered questions about gaming and investment incentives. These were raised in that review. They undertook a significant consultation on this. In response, investment analysts found that the framework did not fundamentally alter investment cases. The review also identified that gaming could be an issue where there was information asymmetry but this was addressed through the guidelines which specifically talk about how to address that information asymmetry. There was and is nothing to stop the PC from seeking these same inputs in your review given that those same concerns are again being raised but without substance. And if the PC objects to looking at other sectors, perhaps it might be useful to look back at the Australian Competition Tribunal's final ruling when Sydney Airport's air-side services were declared in 2005. So this is an airport-specific example.

Refusing to recognise these spurious arguments about the risks presented by arbitration and in response to Greg Houston's submission on behalf of Sydney Airport, Justice Goldberg said:

> *We consider Mr Houston's analysis to be of little probative value. It is speculative and based on a number of assumptions that will not necessarily be valid at any given point of time. Much would depend upon the nature of the dispute and the extent to which there had been negotiations to resolve the dispute. Any estimate of such costs, particularly where arbitration is not inevitable, is speculative in the extreme. It should also be remembered that the legislation anticipates a speedy and cost efficient arbitration.*

So given that this inquiry is not yet completed and we're still discussing a draft with requests for more evidence but much of the evidence having been ignored, it is deeply concerning that in a speech last week to Infrastructure Partnerships Australia, Commission Lindwall made the rather conclusive statement that a negotiate-arbitrate regime for airports would, and I quote:

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Profoundly change the way in which contracts are negotiated between airports and airlines, disrupt investment and harm the community

It does make us wonder if Commissioners are really open to listening in these hearings. Even the CEO of Melbourne Airport said this morning that these concerns were nothing more than hypothetical. It will be up to the government to determine if the PC has fulfilled its obligations in undertaking this review so far. We clearly do not believe it has but this information is all out there and there is still time before the final report is due. I'll hand over to Graeme now.

PROF SAMUEL: I want to get to the heart of the issue and that is the choices available to the Commission to resolve what is clearly a difference of option between the airports and/or their users or their customers. And the choice is this: we already have a monitoring regime. As Commissioner King and I will both agree on this issue, the monitoring regime is virtually useless. Commissioner King and I attended a meeting of regulators within the ACCC several years ago and a presentation was made by an economist and the last slide was the most telling one when it said:

Monitoring is a heavy handed regulatory process that has no other purpose than to serve the political process or the political purpose and objective, of being seen to be doing something

And that was the view that was put and was accepted by every regulator within the ACCC at the time because that's what monitoring does. Monitoring just simply looks at what has happened in the past, provides information. One airport, traditionally it's always been Sydney airport, has objected to some of the monitoring reports, unless it's a good one, but ultimately what happens is that within 24 hours it's vanished into the ether and no one takes any notice of it. So monitoring is a basically useless practice and we know it, and Commissioner King and I know it and we've agreed on that in the past.

And so what we have is a monitoring regime. What's the other choice? It's negotiate-arbitrate. Negotiate-arbitrate is not in fact a regulatory process. It's a normal commercial process. In fact we have already, in relation to airports and airlines and other users, a negotiate-arbitrate process, it's already there. It's called the courts. And Perth Airport, in its action against Qantas Airlines group, has already got - has already started to exercise the negotiate-arbitrate process in respect of the arrangements, the agreements between Perth Airport and Qantas, and the judge there has

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been asked to opine on the reasonable prices that should be charged to the Qantas Airline group from July 2018 in respect of airport services. That's in the statement of claim. That's the negotiate-arbitrate processes there at the moment. I'll call that the "litigation process".

Now, it's very interesting. On Tuesday when the questions were being asked of Sydney Airport - and I have to say that I was very, very, disappointed in the process that occurred Tuesday because the questions that were asked were questions that led the person being asked to give a standard stock answer of a vested interest and I'm sitting there thinking, "Now, the next question is surely going to be...", and it never happened. And Commissioner King and I are well used to this process because both of us have sat on two inquiries, groceries and petrol, and we knew that we were being giving a stock standard vested interest answer.

The next thing you do is start an inquisition. You'd actually start delving deeper and asking deeper questions and so when, for example, the Sydney Airport CEO, Geoff Culbert, said that he didn't like negotiate-arbitrate because arbitration was subject to gaming. I'm waiting for the next question which thankfully, and I do thank Commissioner King that he asked Lyell Strambi the next question, "What do you mean by gaming?" and although the answer from Lyell Strambi was not terribly satisfactory in informing on that, there was no answer from Geoff Culbert because he wasn't even asked what he meant by "gaming".

COMMISSIONER LINDWALL: Correction, we did ask about gaming. I think you'll find it if you check the transcript.

PROF SAMUEL: No, in fact what you asked was about gaming in negotiations and he never even suggested that there was gaming negotiations.

COMMISSIONER LINDWALL: Let's not argue. The transcript will determine who's correct.

PROF SAMUEL: Yes. Anyway, and there were a whole series of questions that were asked. There was a standard answer that was given and then there was no further interrogation so what are we looking at here? We already have negotiate-arbitrate. We have a litigation process that's there by a judge who would not, I think, claim to be an expert in aviation or an expert in airports or the various intricate or complex issues that Lyell Strambi has talked of this morning, he would not claim to be an expert in setting regulatory prices but he's been asked to do all of that as part of the litigation process. What are your other choices? Well, there are two. One is to say that what we ought to do is to give any party the

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chance to be able to refer an intractable dispute, such as appears to have occurred in Perth, to a commercial arbitration. Now, that's one choice that's open, you've rejected it. But then what you've said is, "Well, there is another choice" and the other choice is to go through Part IIIA declaration process.

COMMISSIONER LINDWALL: Excuse me, Graeme. You've used 15 minutes so far and I did say at the beginning there'd be about five minutes, so (indistinct).

COMMISSIONER KING: Well, it just means that you can't ask as many questions.

PROF SAMUEL: Yes, you'll have plenty of time for questions. I think the fact that we actually represent airlines that use about 80 per cent of the capacity of the airports means that we've got a bit to say and we're quite happy to take the questions. But let me just simply say this: so the issue of commercial arbitration is one choice you've rejected, you've said use Part IIIA. We've already provided advice from Michael O'Bryan QC, now a justice of the Federal Court, and recommendations from the National Competition Council which say Part IIIA is no longer available in these circumstances following the amendments made to Part IIIA in November 2017.

However, it's very interesting. You recommend that Part IIIA ought to be a process that's exercised. Where does Part IIIA lead you? Actually to an negotiate-arbitrate outcome except the ACCC becomes the arbitrator. Now, both the ACCC and A4ANZ and other parties have said, "We want to go with negotiate-arbitrate but we don't think it needs to be done by the ACCC. It can be done by a proper expert commercial arbitrator who's got expertise in the area, he's selected for that reason. Set process timelines, which are very, very clear.

Timelines that say that the arbitration should be completed in the following process that can enable the arbitration to be completed, the only one occurred with the gas framework in four months, not four years, as may well occur with a litigation process. And has guidelines or directions as to the matters to be taken into account including enhancing competition, taking account of the interests of consumers, and importantly as occurs in every arbitration, taking account of prospective CapEx investment, the sort of things frankly that Lyell might have well found had operated to his benefit if there'd been a debate between airlines and airports about whether there should have been travelators put in to cover the 500 metres between terminal buildings -with terminal four.

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So we say take your choice. Your choice is there at the moment which is litigation arbitration, time consuming, costly, unproductive, can take many, many years and clearly has the hangover of great uncertainty until the outcome is determined not by the single judge and not by the appeal judge or judges but ultimately potentially by the High Court of Australia after up to six years as we experienced in the Sydney Airport access position; that's one choice. Another choice is Part IIIA and if you want to go Part IIIA then again expect a similar sort of process that occurred with Sydney Airport and Virgin back in the early part of the naughties which went on for six years and the then chair of Sydney Airport said, "Frankly, I could run this on for 12 years if I wanted to". Now, in the end they gave up and ultimately an agreement was reached, as Commissioner King knows because he was involved in it, on literally the eve of the ACCC about to present an arbitrated outcome in respect of the landing charges applicable to Qantas and to Virgin at Sydney Airport.

So there was very good evidence of where the negotiate-arbitrate process led to an agreement that ultimately was reached between the parties. It was the threat of the arbitrator that caused the difficulty. So what we say is, "Okay, Part IIIA, you say we should do that" rather than go through a 6-12 year process of trying to figure out whether Part IIIA still applies contrary to the advice that's been given by Michael O'Bryan, now Justice Michael O'Bryan, and the NCC, deemed declaration, if you like, deemed declaration in respect of airports and say, "Okay, we'll deem the declaration, then the negotiate-arbitrate process under the Competition and Consumer Act will apply.

But the much simpler process would be simply to say: where an intractable dispute exists between an airport and the users of the airport service, that dispute can be referred by any part to commercial arbitration subject to the following directions as to the matters to be taken into account and subject of course ultimately to the process of guidelines and directions that were set by the arbitrator.

COMMISSIONER LINDWALL: Well, I don't think - yes, the echo. Someone might have dialled in. I don't think we're going to respond to every one of those examples of verballing and also they've a lot of assertions there, but we do have a number of questions that I think we need to ask. In particular, I mean the status quo bias that Alison mentioned - I mean, the way the PC always thinks about this is this is where we are, we only move somewhere else if there's a net benefit to do so to the community and we take it very seriously on that. I think we need to talk about specifically what you mean by negotiate-arbitrate in a "practical" sense because airports are quite different to many other forms of business like gas pipelines, there are many users.

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For example, A4ANZ has spoken a lot about car parking and yet I can't see that a car park user would resort to negotiate-arbitrate so (indistinct) does it rely on airlines to look after the interests of car park users? I mean, how exactly would negotiate-arbitrate be implemented and don't try and pretend that it's costless. Everything that is introduced, it's mandatory so it's like it's a new regulation, it has benefits and costs. We need to ascertain whether the benefits are more than the costs, it's as simple as that.

DR ROBERTS: I mean, just on that issue of costs and your opening comment about taking seriously you know that there's going to be a net benefit, it also ought to surely be compared when you're talking about a "net" benefit to the costs of the existing system and what's going on currently and I guess - - -

COMMISSIONER LINDWALL: We are where we are. Everything's from - no, nothing can start from - that's what net benefits - it's always from where you are, you can't go back to 100 years ago.

DR ROBERTS: Sure but the question is whether it's fit for purpose in a current environment and I guess if you have a look at these other reviews and the way they've looked at things, they've also weighed up the benefits and risks and downfalls of existing regimes and that was simply my point, just to clarify.

PROF SAMUEL: Negotiate-arbitrate, you pick the one area where negotiate-arbitrate can't operate and that is car parking and car parking ultimately, if there is a continued view amongst consumers and amongst parliamentarians that car parking charges are too high, we can get to a debate about that but I won't because it's not an airline issue. Then, yes frankly that may have to be the subject of regulation and Parliament will do that if that's what (indistinct). It's been always the hot issue as far as consumers are concerned. Negotiate-arbitrate works, and you know it because I've described Perth is a very good example but I won't get into too much of it because obviously it's subject to litigation at the moment. The parties negotiate, they negotiate until they get to a position of an intractable dispute.

At the present time the only way that a dispute like that can be referred to arbitration is by the agreement of both parties and Sydney Airport talked about mediation, mediation is a different thing, Mediation, we all know that, you know, where parties are brought in to see if we can't get some agreement, but in the end they said it's not binding. Of course it's not because mediation or conciliation is where you try to get the parties to

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agree and it fails. What happens after that? Well, then you've got a problem. You've got an intractable dispute. What does the Competition and Consumer Act say in the event of a, for example, a declaration where any one party notifies the ACCC that there is a dispute, an intractable dispute, then the ACCC can be called in to actually arbitrate and the ACCC then steps in and starts through an arbitration process.

How can it be gamed? Well, the best ways of gaming is what invariably happens, and will happen in negotiations as well, is that one party puts in a bid or an offer like that, another party puts in an offer like that, then the arbitrator's got to sit there and say, "Well, I better start from the beginning and see if I can't work out what is the appropriate process". The process that's been adopted in Canada and the United States and has rarely been done in Australia is what's known as last offer or final offer arbitration which is where the arbitrator says, "I'm not going to put up with gaming. I'm saying to the two parties give us your final offer, give me your final offer, and I will look at those and I will take one or other offer".

Now, of course what that does is it forces the parties to come to what they would perceive to be a reasonable position and then the arbitrator will make a choice of one or other. Of course what that invariably does is it says to the parties, "You better reach an agreement because you're going to come so close together in terms of a reasonable outcome in terms of your final offer" but gaming won't be part of the process. Now, what of course it also does is it makes it much easier for the arbitrator to reach a final decision. The arbitrator should be able to do two things: (indistinct) set process guidelines. You have 30 days to put in your final offer. I have 60 days to look at those final offers and reach a determination. If I request material from you it should be provided in 30 days and then I will reach my decision within four months. That's the timeline factor. No judge will do that, not with the process of appeals et cetera.

And then the other thing is that the guidelines that are set for the arbitrator, the directions that are given to the arbitrator, say, "You must take into account enhancing competition. You must take into account future investments", that's a standard process for arbitration anyway, "You must take into account the interests of consumers. You must take into account a whole range of different factors and they're all put there". Now, that's all part of the process. It's part of the process that doubtless will occur in Perth versus Qantas Airline Group but that will be a long, tedious, complex, costly, litigation process to ultimately get the material before the courts for a single judge who would, I suggest, claim no specific expertise in this area to try and reach a decision as to what are reasonable prices for the charging of aeronautical services by Perth Airport to Qantas Airline Group.

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COMMISSIONER LINDWALL: Would you agree that in much of this time, airlines and airports have similar objectives and similar ways of thinking of things? There's a lot of common interest but they diverge in a couple of areas. One being an airport will have an incentive to try and grow its capacity to bring in new airlines. Incumbent airlines will try and resist that. If you take that, you might say that there would be an incentive by airlines, incumbent airlines, to try and restrict a new investment at an airport and therefore they would go to negotiate-arbitrate and use that to reduce that level of investment. Now, Frontier Economics did a study of Heathrow which found that when there is congestion, the rents from which went to airlines through higher fares. You've claimed, which we might be persuaded, we're open on this, that negotiate-arbitrate would lead to lower fares. Could it not lead to higher congestion and higher fares?

PROF SAMUEL: (Indistinct) not the arbitrator is required to take all those issues into account in determining what's appropriate. I refer to the matter that Lyell Strambi raised before. Now, maybe an arbitrator may have looked at all that and said, "I hear the airline's view. I hear the airport's view", actually Lyell Strambi said himself, "We made a mistake" about travelators. In the interests of consumers which I'm bound to take into account, I'm saying to you that a 500 metre walk is too long and put in a travelator. The travelator and the CapEx investment ought to be made or alternatively if it's a third runway or whatever it might be, they're the sort of factors they'll take into account yet arbitrators are skilled at looking at all these factors and taking all of them into account and it may well be that there will be circumstances where the views expressed by airlines in their own interests, are not necessarily of the view that ultimately is determined by the arbitrator.

COMMISSIONER LINDWALL: Sorry can I get you to clarify it please.

COMMISSIONER KING: Because you have said, as I understand it, that A4ANZ supports final offer arbitration. The sort of decision you've just come up with where, for example, the airport says, "No travelators" and the airline says, "No travelators", the arbitrator under final offer arbitration cannot say there will be travelators so I'm now - - -

PROF SAMUEL: No sorry, Commissioner. No, what I was suggesting was that the airport says, 'We really did need there to be travelators", the airline is saying - - -

COMMISSIONER KING: No, no, but take the example because we had a live example where the airline and the airport both put the positions

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and you've said the arbitrator has to act in the consumer interest, I'm not sure how that gets put to the arbitrator unless there is consumer representatives but let's not go down that path yet, and in final offer you can't have three things unless there's another consumer group coming up with another offer, I don't understand how the final offer arbitration, they could come up with a solution that isn't part of either offer?

PROF SAMUEL: Look, you're absolutely right. One would expect though in those circumstances, and I don't want to presume what Mr Strambi would have done in those circumstances, but one would expect that he would say, "Look, I sincerely believe travelators are necessary". The airlines say, 'We don't think they are". The final offers have travelators and no travelators and ultimately the arbitrator reached a conclusion but let me emphasise this: final offer is but one of the processes of arbitration that we've suggested. It's not the only one. There are a whole range of different ways.

The ACCC has the discretion at the moment, for example, in arbitration to set whatever guidelines it wants, whether it wants final offer, it might say, "We want final offer but in doing so we reserve the right to deal with the interests of consumers" or "We reserve the right to deal with the issue of competition that would take us outside what the two final offers have provided". That's the beauty of arbitration, is that you've actually got that flexibility for the arbitrator to be able to do that and the guidelines or the directions that can be given to the arbitrator can say, "You can conduct your arbitration whichever way you want but above all you must account of enhancing competition, the interests of consumers, and taking into account the issue of capital investment. That's the arbitrator's determination.

DR ROBERTS: And the gas code and the accompanying guidelines do deal with that issue so they talk about the use of different types of arbitration based on the complexities and the multiple factors that are involved so they do - - -

COMMISSIONER LINDWALL: But isn't that the nature of commercial agreements as they stand, that the two parties put their position and they reach an agreement, they have reached agreements, and you haven't shown a problem yet that requires a solution.

PROF SAMUEL: Well, hold on when you say we - - -

DR ROBERTS: I think we have shown a problem.

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COMMISSIONER LINDWALL: No, you made a number of assertions.

PROF SAMUEL: No, no, there's not an assertion. Perth Airport is one where an agreement hasn't been reached.

COMMISSIONER LINDWALL: Correct, yes.

PROF SAMUEL: I don't quite - you might well ask Mr Strambi whether have been reached in respect to Melbourne Airport and, you know, the services agreements there so don't assume and don't make an assertion that agreements have been reached (indistinct) as Sydney Airport said that the last set of agreements were made in 2015, I suggest you might well want to ask Perth Airport, and I have no knowledge now about what the position - - -

COMMISSIONER LINDWALL: I understand there have been three agreements that have been concluded since our draft report has been released.

PROF SAMUEL: I don't know.

DR ROBERTS: That's (indistinct). But I mean, the other thing is to say we're just asserting it, you have numerous submissions including confidential ones because of the nature of what was involved, that point to the challenges and the problems in the negotiation process and the protracted nature.

COMMISSIONER LINDWALL: Correct, (indistinct) protracted.

DR ROBERTS: And the things that are included in there so we see lots of inclusions of non-aeronautical things in aeronautical charges. Just last night I had emailed to me an example from one of our member airlines of one particular airport, of a range being given for a capital project ranging from $83m to $127m, 'details will be provided after you sign'. That's while this Productivity Commission process is going on so if you're asking us for evidence of a problem, I think we have more than provided that and if you look through all of the submissions, including the confidential ones, there are - - -

COMMISSIONER LINDWALL: But it has to be more than evidence of a problem. There has to be evidence that the problem is so great that the net cost or the net benefit of going to a new system like negotiate-arbitrate would outweigh that.

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DR ROBERTS: But has that been measured?

COMMISSIONER KING: Yes, has that been measured because in a sense that's what I would like to spend the remaining time on which is exploring negotiate-arbitrate in trying to understand the benefits and the costs a bit better and because there's no point quite frankly, in the Productivity Commission putting a theoretical principle to the government and saying, "Let's go down negotiate-arbitrate" unless we have worked out those costs and benefits and that is the exercise we're engaged in.

DR ROBERTS: Understood and that's what the Vertigan review did.

COMMISSIONER KING: And to do that you have to work on the practical aspects. So, for example, I understand one of the submissions that has come in post-draft has suggested that there should be a regulatory return on capital that is set for any arbitration. Is that the position of A4ANZ that there should in a sense be some - maybe the ACCC, maybe another body, but they say a fair rate of return or reasonable rate of return on airports if X per cent.

PROF SAMUEL: I have to say I am sympathetic with the view that you expressed on Tuesday that this is not a thing that the government needs to get intimately or intricately involved in. If the ACCC is the arbitrator, it ultimately sets the WACC, it sets the rate of return. If there's a commercial arbitrator, the commercial arbitrator would do that according to the relevant circumstances at the time which will take into account the risks, you know, associated for example with investment, factors such as that but you will know the issues in setting the rates of return. Look, from my own part I think if you've got a commercial arbitrator, then what it does is it puts it into the hands of the parties and the commercial arbitrator to resolve the intractable dispute.

COMMISSIONER KING: Can I just then follow-up on that. Let's say there's an investment that is being considered in the arbitration, a new investment, but that investment will involve common use of facilities. So there's the airport, the airline, that are having the dispute but there is also another airline out there. Should that airline, that other airline which will be affected by the investment, should they automatically be included in the arbitration or should they not be included?

PROF SAMUEL: Well, they won't necessarily be included in the arbitration but the arbitrator I think would clearly take it upon himself or herself to actually enquire of the other airline whether they have views to express as equally they'll take into account the views of consumers. They'll take the views of potential new entrants into the market. That's the

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issue of competition, that's the issue of taking into account consumers. In terms of investment there may well be that the arbitrator says, 'I want not just the view of the airport as to costs of the investment, I want the view of others. I want to understand what the real efficient cost of the investment might be".

There'll be other issues such as, "When do the users of the capital investment start to get an economic return?" and that will also be taken into account as part of the process. So effectively you will have multiple airlines - I mean, they've got to be at the table whether officially at the table or whether the arbiter says, "We need the input of multiple airlines to be able to make a sensible decision".

DR ROBERTS: Yes. In order for them to take account of the, you know, the competitive outcomes, yes.

COMMISSIONER KING: Other parties that may be affected by investment decisions so, for example, if it's a terminal decision, there's the airlines, there's the retailers that operate in the common user facility. Those retailers, are they also at the bargaining table?

PROF SAMUEL: Well, frankly the retailers as a collective group if they were to get together collectively, might well have another issue on arbitration in terms of their rentals and the like. But again, they would be part - you see, we're giving you the detail of arbitration. Arbitration - - -

COMMISSIONER KING: I'm trying to work out if it will work, that's the - - -

PROF SAMUEL: Yes, yes, well but - - -

DR ROBERTS: But isn't it the same processes under Part IIIA? I mean, if you were take this to its natural conclusion, wouldn't it be the same process that an arbitrator who was making an arbitration under Part IIIA, say it was - - -

COMMISSIONER LINDWALL: You've have to meet a hurdle first.

DR ROBERTS: Yes, yes.

COMMISSIONER LINDWALL: Which the NCC has given the submission to us they were being reasonable in the circumstance.

DR ROBERTS: Yes, okay, just assuming though because you're asking - - -

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PROF SAMUEL: No, that's the declaration, that's the declaration.

DR ROBERTS: Yes.

PROF SAMUEL: We're not talking about a declaration at the moment, that's the Part IIIA declaration issue which the NCC has got jurisdiction over. Let's jump over that - - -

COMMISSIONER KING: Yes, let's say it's been declared and - - -

DR ROBERTS: Yes because you're asking about the arbitration process that - - -

COMMISSIONER KING: Yes and the answer from the arbitration perspective is that the declaration is for particular services and there are very strict rules about investment, particularly on the basis that, and there is an assumption in Part IIIA, that - well, they're a statement in Part IIIA, that an existing user cannot be required to pay the cost of any investments required by another party. So I think there is a legitimate argument that you're putting up there, is whether Part IIIA is appropriate for common user facilities and I think that's an interesting point. But if you're putting up as an alternative negotiate-arbitrate and you're saying that Part IIIA doesn't work for common user terminals nor does negotiate-arbitrate so you may have a great argument against Part IIIA but I can't see how you've (indistinct) but negotiate-
arbitrate (indistinct).

PROF SAMUEL: No but forgive me, forgive me. The choice is litigation arbitration, all right. There are no rules. That's Perth Airport. The second one is commercial arbitration where you can set the rules, they have to be taken into account. The third is Part IIIA which we've said frankly on all the legal advice we've got, it doesn't apply anymore. It's no longer available because you can't get declaration. If you had declaration then you are bound by the Part IIIA requirements in respect of negotiate-arbitrate by the ACCC.

COMMISSIONER KING: But I want to discuss your proposal though rather than the alternatives.

PROF SAMUEL: All right, our proposal is to say litigation is there, right. Any person exercising normal common sense would say that's not the most efficient means. Part IIIA we put aside because we don't think it's available in fact our advice is it's not. So we look at commercial arbitration, then you're asking, "How do you structure a commercial

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arbitration?", right, and what we've said is, "Well, the beauty of commercial arbitration is you've got total flexibility as to what you can build into it or not and then it's a question of how much, if you like, how much envelope providing - envelope edging you want to provide to the commercial arbitration and that involves, you know, and we've suggested two or three issues.

It involves setting criteria that say you must look at competition, you must take account of the interests of the consumers, you must take account of investment that is required to satisfy the issues of competition and consumers. And then it must take account of other affected third parties. There are all those factors you take into account but that doesn't make the arbitration any more costly or complex. What it really says is, "That's the way you make the arbitration work to (indistinct)".

COMMISSIONER KING: Can I come back. Again, I still can't see exactly how we have (indistinct) and all the other airlines involved in the negotiation if they're affected? Maybe that can be overcome. Can I come back to say an investment example. So let's say that there's a dispute about an investment. The airport says they need a hurdle rate of return - let's say it's 15 per cent, let's say it's quite a high rate, they think that's necessary for the risk. The arbiter says that this investment needs to go ahead and the rate of return will be ten per cent. So you would then see that the airport would have to make that investment, they would be forced to make that investment to meet the arbiter's decision?

PROF SAMUEL: Well, what we've got is we'll have, you know, two proposals put in; one by the airport and one by the airline. It may well be that the result of the arbitration, as Mr Strambi has indicated, is that the Airport Board says, "Well, look we're not going proceed with that investment", right, so be it. Then it will be a matter of the parties sitting down and saying, "Well, hold on. You said you were going to proceed with the investment, you wanted a 15 per cent rate of return, the arbitrator has said 10 per cent. Well, that's clearly not going to work. Well, we better start sitting you down and seeing, you know, what we can deal with in terms of rates of return and the need for the investment. The airlines might well say the investment is not going to occur. The airport might say it's not going to occur or alternatively they might say, "Well, we better have a look at this in another way to see whether we can make - - -

COMMISSIONER KING: So the arbiter's decision isn't binding. It may lead simply to further negotiations.

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PROF SAMUEL: No, the arbitrator's decision as to prices will be binding but the arbitrator can't be in a position where it says, "I require you to make an investment".

DR ROBERTS: I mean, that's not the case in any arbitrations

COMMISSIONER KING: So let's say that the arbiter has made a decision about an investment, the airport is going ahead with that investment, it's on particular passenger forecasts. Those forecasts are not met, those forecasts have been put forward by the airline possibly in good faith, who bears the risk of the passengers? At the moment it would be the airport but given that the airline has put forward those forecasts, should it be the airline that bears the risk?

PROF SAMUEL: Well, that's - - -

DR ROBERTS: Is that assumption actually correct though that they bear all the risk in the agreements, I don't know.

PROF SAMUEL: As I understand it that's the case for most of the agreements, yes, I can't be sure but it's in all of the agreements, so that's my understanding.

COMMISSIONER KING: Sorry, who bears the risk?

DR ROBERTS: That the airport bears all the risk.

PROF SAMUEL: Yes but that's part of a process, isn't it, at the moment. It (indistinct).

COMMISSIONER KING: No but again I'm just trying to understand, under your solution the arbiter has certain information provided to be (indistinct) and to give the example, you know that in, for example, electricity transmission investments where the regulator says there are certain demand forecasts that underpin an investment. If those demand forecasts are later shown to be incorrect then the regulated asset can say, "Well, we didn't make as much money. We need to make it up next period". Your arbiter is in a similar position where the arbitration is based on passenger forecasts provided by the airlines because they're the ones with the information, if they are not proven to be correct who bears the risk? (Indistinct) say, "Well, you didn't make the expected return. The arbiter said 10 per cent and you only made 8 so therefore we must be allowed to make 12 next time and the arbiter says, "Yes, that's fine".

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DR ROBERTS: To be clear, this solution as you're calling it, our solution, is also something that's been proposed by the ACCC. We haven't just plucked it out of thin air. It also exists as a solution in the gas code but part of the solution is actually that these types of schemes discourage the seeking of the arbitration and that has been borne out since the gas code came in. It also has been borne out in other sectors that use these types of schemes, is that it actually drives parties to reach agreements but I'll park that, I just - - -

COMMISSIONER KING: As agreed under Part IIIA with Tiger and Melbourne Airport but - - -

DR ROBERTS: Well, Tiger withdrew that application but anyway - - -

COMMISSIONER KING: Yes, after they reached an agreement but can - sorry, can I just have an answer to that question.

PROF SAMUEL: Because what you've got this is, and forgive me but the airlines don't on their own make assessments of passenger growth or whatever it might be, airports will make their own assessments of those and there may well be some debate or dispute about that because that will impact on the timing, for example, of building a new terminal facility, the timing of building new runways and the like, but let's assume that the airports and the airlines reach a decision where they don't agree on passenger growth and the airport then says, "All right, here's the deal. We'll build this runway or we'll build this terminal facility based on your projections but in the event that your projections prove to be wrong, there's going to be an adjustment".

An arbitrator will look at that surely and say, "Well, that's the way it ought to be" or in the alternative, and you talked about the electricity transmission light, alternatively what then happens is in the second five year agreement, or whatever it might be because most of these agreements are five year agreements, the arbitrator says, "The airport actually had a lower rate of return than what was appropriate" and arbitrated upon in the first five years, that's got to be made up on the second five years. That's all part of the arbitration process.

COMMISSIONER KING: So an arbitrator now can make binding decisions on a future arbitrator?

PROF SAMUEL: No, no, I didn't say that. I said what the arbitrator did - - -

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COMMISSIONER KING: No, because if it goes back in five years to a different arbitrator - - -

PROF SAMUEL: Yes and the different arbitrator will then have one of the factors to be put to them will be that the airport will say, "We were last time arbitrated, determined by arbitration, a 10 per cent rate of return". It turned out that it was 8 per cent only because the airlines projection of passenger growth wasn't met, right, and that wasn't adjusted through the period of the five years of that first agreement and therefore, and this is the proposition that would be put by the airport, "Mr Arbitrator, we want you to take that into account in this second five years".

DR ROBERTS: It would be part of their justification for the pricing.

COMMISSIONER KING: Can I do one more, or?

COMMISSIONER LINDWALL: One more, yes.

COMMISSIONER KING: All right. And again, so you've got the risk in the second arbitration feeding into the rate of return in the first which is interesting. But an airport wants to make an investment. Currently there are no disputes and the airport wants to go ahead and make that investment but it knows it's doing it again. Let's say it's a - I can't remember what I used before whether it was a 15 per cent hurdle rate, it believes that that will be a relevant investment but it (indistinct) the services involved in that investment may be subject to future arbitration so a risk to the airport in currently, you know, building those facilities is that the prices that will lead to a rate of return, an appropriate rate of return, in its view are subject to potential future arbitration.

How does the airport then take that risk? Does that mean that the risk that the airport needs to take into account is such that the hurdle rate has to go up to 20 per cent or can the airport, in a sense, approach an arbiter and say, "Well, look these are the prices we need for this long term 30 year investment", or whatever it is, "So can we have those built in today?" So is there, in a sense, a forced upfront arbitration negotiation process before - because to reduce the risk of future arbitration, just again, how does that work? And again I'll run the gas pipeline or the transmission network approach, what happens there is the people doing the investment go and see the regulator and say, "Please approve this investment" and say that it's an appropriate investment and therefore we'll get the appropriate rate of return before we do it and that's the standard approach that occurs by default in these situations. So I assume that's not what you want so how would it actually work?

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PROF SAMUEL: Well, I'm a bit bemused you asked that question because you've conducted a few arbitrations back at the ACCC yourself so you know how these things work.

COMMISSIONER KING: I think there's only ever been one Part IIIA application.

PROF SAMUEL: I'm not talking about just Part IIIA applications and the like, all of which have got long life in terms of the investment itself. So there have been a number of arbitrations that you've been involved in as I have and of course these are all factors - you know, the fact that these agreements are five year agreements doesn't meant that what is done is that rates of return are set only on a five year basis lifetime of the investment if the investment has got a 30 year lifetime of (indistinct) and so they are the matters that were taken into account by you and by me and others in terms of the ACCC telecommunications. The one arbitration we actually never finally reached which was the Virgin Sydney Airport, (indistinct) Sydney Airport arbitration because they reached an agreement on the 11th hour but they're all the factors that are taken into account by a commercial arbitrator. There's nothing magic in it. It's nothing terribly impossible. It's the sort of thing the ACCC has been doing for years.

COMMISSIONER LINDWALL: It's very easy to say something is simple but I think we've decided at this stage that we need to move on to another group but there is a complex situation. Airports are quite different to moving gas molecules. If you want to give some more thought and perhaps give us another submission about the practicalities of negotiate-arbitrate I think we'd welcome that.

COMMISSIONER KING: And I must say I'm impressed, Graeme, that at your time as chair of the ACCC, you thought telecommunication regulation was simple.

PROF SAMUEL: But I did think that telecommunications arbitration in the end resulted in what we - - -

COMMISSIONER KING: Thank you, Graeme and Alison.

DR ROBERTS: Thank you.

COMMISSIONER LINDWALL: Thank you.

DR ROBERTS: Thank you, Paul.

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COMMISSIONER LINDWALL: Thank you, Graeme.

PROF SAMUEL: Righto.

COMMISSIONER LINDWALL: I'd now like to welcome the AAA and then we'll have - and sorry for being a bit late but we might have to eat into our morning tea to some extent, we'll see how we go. I'm sure people are not too keen to have the instant coffee of PC.

COMMISSIONER KING: Which is why we want the 15 minutes to duck downstairs and get the decent stuff.

COMMISSIONER LINDWALL: Well, if you could just introduce yourselves and give a statement. Trying to keep it within five or so minutes would be preferable.

MR THOMPSON: Equal time would be reasonable wouldn't it, Commissioner?

COMMISSIONER LINDWALL: Yes, it's up to you.

COMMISSIONER KING: It just means there's less questions and we can't get through all the issues (indistinct) so it's in - - -

COMMISSIONER LINDWALL: It's in your hands how much you would like for issues to be explored.

MR THOMPSON: Fantastic. So, thank you. Guy Thompson, Chairman of the Australian Airports Association and I have with me Dr Warren Mundy who is the Chief Economist for the Australian Airports Association. Conscious of time and certainly pleased to leave sufficient time for questions, I'm quite comfortable to ensure the Commissioners have what they need. But some very basic facts around the AAA. Founded in 1982 as the voice for Australian airports. We currently represent in excess of 340 airports around Australia and some 160 members that are in the corporate space that provide services to the aviation airport sector.

We are pleased to be here to answer questions and provide further information for the Commission in its inquiry. We acknowledge and are pleased with the findings that the monitored airports, the Commission found in the draft report that the monitored airports have not abused their market power to the detriment of the community and strongly support the recommendation for continuation of the existing regulatory regime for those monitored airports. The Commission is correct in its assessment

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that with the exception of the four largest airports in the country, airports do not possess significant market power to warrant any form of regulation.

We do, however, recognise concerns raised during the inquiry and remain keen to work with airlines, the Department and all the other stakeholders to find pragmatic and cost effective ways to improve outcomes for the industry as a whole. We're also very pleased that the Commission has recognised the very difficult financial position that regional airports find themselves in. We find that the funding gap for essential infrastructure in that space in 2016 figures was in the region of $170m combined across the country and that is just stuff to ensure the airports can continue to operate and service their communities.

We think that the solution to the funding gap and we have been advocating the government, in fact both sides of politics, around the need for some form of funding but we recognise and in fact agree with the Commissioner's observations that any funding provided in that space in a grant sense ought have a robust business case that demonstrates the benefits and the costs associated with the spending of any money in the public purse. So I think that's all I will say. I will hand over to Dr Mundy who I know has got a few things he would like to outline and then we're happy to take your questions, Commissioners.

DR MUNDY: I say this not to seek to curry favour but as somebody who has been an active participant in the proceedings of this Commission since June 2001 when Commissioner Byron conducted the Prices Surveillance Act inquiry and having served six years as a member of the Commission I have to say that, in the broad, the conduct we've seen from the domestic airlines in questioning the integrity, the motivation, and the competence of the Commission is in my experience unprecedented and it is unfortunate, I think, that this has occurred and people have tried to, I think, politicise the proceedings in the Commission in a way that we didn't even see when tariff reform was a live issue. So I just make those observations to start.

I think it's also quite peculiar the claims that are being made, that the Commission has ignored the evidence of experts put to it. It seems to me, particularly in relation to the analysis of Frontier Economics, the Commission has given it some extensive consideration and quite frankly has found it wanting. Now, I don't want to go through the Frontier Economics analysis because we are pretty comfortable with the Commission's analysis and it looks pretty much like what we thought of it. But it's equally fair to say that significant expert evidence from competent international experts has been put to the Commission by ourselves.

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Greg Houston, as you know, was one of the leading expert economic evidence providers in this country and indeed it's the fact that Greg provided advice to Qantas in its submission to this Commission in 2006. Mike Tretheway who is the principal economist of InterVISTAS is actually cited in the most recent submission from A4ANZ for his 2007 work about elasticities work he did for IATA and indeed Mike has provided advice on competition pricing matters to the majority of A4ANZ's members at various points in the past and it's interesting to note Michael, who has helped us form our views about the appropriateness of final offer arbitration, probably has conducted more final offer arbitrations in Canada than any other person. So we come to this and the last point I would make is now legal advice, I have read at length the legal advice that has been provided by A4ANZ. We have provided legal advice from Simon Uthmeyer who acts for the ACCC in the Port of Newcastle arbitration and who acted for the National Competition Council when the Virgin Blue declaration was before both the tribunal and the Federal Court.

So we come to this matter with experts, everyone's got them. The question for the Commission is to examine that evidence and weigh it up. So we think the Commission has looked at the evidence, formed its own view, and applied, and I think this is an important issue, has applied the test that the government has determined certainly in relation to returns. It is patently clear that the pricing principles lead the Commission when assessing whether excess returns have been earned in the aeronautical business to look at pre-tax returns on tangible assets having applied the line in the sand methodology determined by Treasurer Costello at 2007. That's the test. Now, we provided evidence by HoustonKemp to that effect. The Commission, whilst not having determined what a reasonable return is, has formed the view that the returns are not excessive.

This furphy of we now must create a single till analysis, a debate which has been had in this country for a very long time and in fact was rejected on recommendation of the Prices Surveillance Authority when it reviewed the pricing of the FAC chaired then by Professor Fels has been a set piece and the Commission in 2002 made very clear that the sovereign risk issues of arbitrarily switching the character of the till. So the Commission has got that right. It has undertaken assessment, it's landed on the facts.

We note that that assessment on the basis of the test as set out in the pricing principles, is not challenged by the material that has been put by others to the Commission. Others say that there is an alternative test but our members having seen the test set down by the Commonwealth, have complied with it and it would simply be a great regulatory error to now say, "Regulation is required to be single till returns rather than dual till

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returns are excessive". It's up to the Commission to form the view that the single till is a better way to think about these things and make that recommendation to Government but it is not right to ex post change the nature of the test.

I'd like now probably to move on to the interesting question of negotiate-arbitrate. And again the outrage that has come in this matter, I find really quite surprising. The Commission has looked at an industry specific arbitration framework for airports on no less than five occasions before. Each of the previous airport's reviews considered this matter and so did both the reviews of the National Access Regime and therefore that the Commission might not fall now in a different place should not be surprising and the arguments that have been put really are not that different but I just think I want to - there are just some issues that have sort of come to my mind during the course of today which I'd just like to explore. It seems to be that the proposition is that any airport user can seek to have its dispute arbitrated. When you're driving to Melbourne Airport, on the right-hand side there's a Mercedes Benz dealership. Arguably this is an airport user.

Now, this airport user could locate their Mercedes Benz dealership in Essendon say. They might even be able to find a bit of land about 400/500 metres back along the road that isn't on airport land. So what we're going to have, it seems to be proposed, is that this Mercedes Benz dealer will go and work out what the property market is in the general vicinity of north west Melbourne and all the sites will essentially be the same except one. That's the one where I can go and get my dispute arbitrated by the ACCC over what my rent should be. I think when you start to unbundle this, at least the scope of persons who arbitration should be available to needs some serious consideration.

I am interested also in how an arbitrator is going to ascertain abuse of consumers. To the best of my knowledge there is no consumer group that the Commission could currently turn to about uses for Melbourne Airport. I think the Commission should validate that itself. The regulation in the energy sector has been problematic in trying to find a way that consumers can be given a voice in decisions around the setting of tariffs, both transmission and distribution. Progress has been made but it's been a long time coming and it's going to be a struggle to work that out.

The other thing that is beginning to quite concern me is the ability of the arbitrator to intervene in what might be planning and design decisions which as a matter of law are rightly the purview of the Minister who was administering the Airports Act and that would need to be carefully considered. I think what also needs to be considered is that airports have a

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range of statutory duties which they must undertake and these duties from time to time bring them into conflict with airlines and other persons and that can range from safety issues, it can be issues about security of persons who may or may not be permitted at the airport, a whole range of matters. Under the propositions that are being advanced it seems that all of those matters may be subject to dispute and in some final determination.

The last point I'd like to make is that I think there is a very, and I think you were getting to this Commissioners, is what happens to the other parties who have an interest in investment and how that's resolved? And it seems to me that inevitably they must have the same rights in that arbitration as the disputing parties because if an outcome were to be such that the return on an investment were to be so low that it prohibited the meeting of other contractual obligations, this is going to become a very, very, messy circumstance. I just make one other observation about the - as you were trying to get at, Commissioner King, the issue about over and under recoveries of returns. As you'd know the transmission code in fact doesn't work every five years. It tops you up and makes you whole every year.

The problem is with the thing of course, as you would know with transmission, is that the customers are there and they're pretty stable, we know where they are. But in an airport - I'm thinking particularly and let me give you a real life example of this: Mr Strambi's airport built a small terminal to facilitate the entry of Impulse and an airline called Virgin Blue in about 2001. Melbourne Airport reached a price with Impulse Airlines uncontracted and proceeded on that basis to build that terminal to facilitate the entry of those two carriers. There was a dispute around the price of that terminal brought by then Virgin Blue and the price that Virgin Blue was allowed access for was significantly lower and it subsequently transpired that Impulse Airlines exited the industry and Melbourne Airport experienced a significant reduction in its revenue for that terminal. It couldn't turn to Virgin Blue to make it whole.

You could perhaps consider it a more obscene example of what happened with the collapse of Ansett. And the fact that this sort of situation will exist is exactly the circumstance that Qantas has objected to pre financing of the new runway in Brisbane. Why should we pay for things that we mightn't ever use? What if - and international carriers may not be there. So how this is made whole is very difficult. The simply reality is, is that airports bear volume risk. In the vast bulk of the agreements that have been written by Australian airports with airlines since the first one was written by Mr Strambi's company in 2002, have left the airports fully exposed to volume risks. That's the reason why, when you compare their

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returns to say electricity transmission businesses. They are higher. So I think we'll just leave it at that.

COMMISSIONER LINDWALL: Can we start with the case before the Western Australian Supreme Court over Perth airport and comments you've heard earlier from A4ANZ that this showed that negotiate-arbitrate might have been a better solution rather than going to a Supreme Court for what looks like a negotiate-arbitrate in some form anyway.

DR MUNDY: Commissioners, I have to be careful about what I say - - -

COMMISSIONER LINDWALL: I understand that.

DR MUNDY: - - - about the litigation of Perth airport because I advise Perth Airport. But I make the more general observation. In the 20 years since privatisation, airport investors have been able to reach agreements with the airlines and others to underpin the investment in this industry that has enabled airlines to grow their businesses and has enabled airports to grow their businesses, that has facilitated the reduction in prices for international carriage, arguably for domestic carriage depends on the time period.

But that has happened without this framework, other than the more distant framework of Part IIIA that is currently proposed. The fact that there is a legal dispute is not – one dispute in 17 years is, in our view, not evidence that the system needs replacing, it's evidence that the rest of it has worked. And the vast bulk of disputes that arise, and certainly the vast bulk of agreements that exist between airports and airlines, have extensive dispute resolution procedures written into them anyway.

So the only issue that is really at large here are disputes about the formation of contracts because once a contract's formed – they're all modern commercial contracts, they all control dispute resolutions, and one would have thought that if there was a serious dispute within a contract, that is absolutely a matter that should be resolved in a court under the normal contract law, not having some regulator who – I'm one of them in Queensland – may not be expert in resolving a question about contracts.

So all we're talking about here is the formation of contracts and as we increasingly get off a fixed term basis, all airlines have the same contracts, contracts are growing in length. The common length of contract now is probably longer than five years, these things start to overlap. So not everyone's forming contracts at the same time, so there's going to be this interaction of contracted rights, people who want to enter and the whole

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thing is going to be not amenable to the sort of, you know, final (indistinct) arbitration system that is proposed.

I think there's two questions here. Question 1 that needs to be answered is, does there need to be an arbitration framework, and if so, how is it accessed? We say there's the courts. We say there's Part IIIA. We don't agree that access to Part IIIA is more difficult than it was when the tribunal declared Sydney airport. We say it is less difficult, and then there are other arrangements if the parties can agree to them, that you can have the matter commercial arbitrated under the relevant statute that exists in that state. So that's - - -

COMMISSIONER LINDWALL: Do you want to talk more about negotiate-arbitrate or do you want to - - -

COMMISSIONER KING: I want to move on to the commercial negotiation, the proposal that - - -

COMMISSIONER LINDWALL: All right. Let's move on.

COMMISSIONER KING: One role of these hearings are to explore the alternative ways that have been put forward by participants. One that has been put forward by the AAA together with BARA and Sydney airport is that the airports and airline stakeholders should work together to develop contracting and negotiating principles, at that point, it seems to me that seems innocuous. However, it's also proposed the Commonwealth government should work with those airports and airline stakeholders to develop these contracting and negotiating principles. Please tell me why is the government suddenly in here?

DR MUNDY: Well, I have to say this, with respect, Commissioner. I've worked with the Department of Infrastructure in the aviation sector for 20 years. I find them helpful. I find them thoughtful and they are able to sort their way through things. It may well be, it may well be that in the fullness of time the chief-executive officer of the AAA and the executive-director of BARA and some other people, can sit in a room and resolve these issues and maybe the Commonwealth doesn't need to be there. Maybe the industries can just sort them out.

But sometimes the presence of an interested but, if you like, interested but stakeless person in a room, can just help it through. It is nothing more than that. This is not a proposal for a memorandum of understanding. It is not a proposal for some sort of binding guideline. It is a proposal simply to move things forward and it is certainly not a cynical response as was described in Sydney on Tuesday. Our response is a recognition of

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legitimate concerns raised by a major user group about matters that they wanted clarified and we thought those issues are important and they are fair enough.

What we didn't agree with BARA on was their mechanism for solving the problem. So what we're trying to do is – with respect, I think you are reading too much into this. Now, maybe I should have expressed it better.

COMMISSIONER KING: I may be reading too much into this but there is a long history in Australia of groups getting together under various guises, often before the current competition laws were put in place, and working against the public interest by doing such things as coming up with template contracts, particular pricing schemes and so on. I worry that this starts looking like a collusive device.

DR MUNDY: As you are well aware, the board of airline representatives is authorised by the ACCC to collectively bargain on behalf of its members. Our industry has consistently supported that because it brings benefits to our members and it brings members to the travelling public. This is really just us saying "Let's sit down and talk about these things". BARA has in the past expressed concerns, for example that there are a range of boilerplate clauses in these agreements and I'll just – I have an agreement between a major international carrier and a major airport in front of me. I won't disclose who they are and I don't intend to table the document. It is not necessary.

And these deal with such complex and competition imperative matters such as the service of notices. Dispute resolution clauses. The treatment of stamp duties. The application of the new tax system legislation in relation to goods and services tax. And what happens from time to time is that the drafting of these things moves on, and it is quite annoying, I understand, for international carriers to have to confront this plethora of clauses which are pretty unimportant, but they all do the same thing, and it is my experience that the time – these sorts of matters take up quite a substantial amount of time for their commercial worth and they cause a lot more grief on top of that.

So all we're saying, all we're saying is "Let's just have an understanding about where the drafting of these clauses are". This doesn't go to quality of service provision. It doesn't go to price. It doesn't go to rights of access. It's just a simple proposition to try and facilitate the bargaining and contracting processes. It is nothing more than that.

COMMISSIONER KING: I just want to make sure I understand the proposal because you keep mentioning BARA, and you've said that they are

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authorised by the ACCC to act as a bargaining group which I don't know off the top of my head but I'll take that as being fact.

DR MUNDY: I think you might have authorised them once Commissioner.

COMMISSIONER KING: Possibly. Would you - - -

DR MUNDY: Maybe twice.

COMMISSIONER KING: I am not sure if I was the Commissioner. It depends if they came up twice in five years. Would you see this really being BARA and the airports or do you see BARA and Qantas and Virgin Australia as being all part of this group to be work out - - -

DR MUNDY: It would be all of them. Of course, BARA and Virgin are – Qantas and Virgin are members of BARA.

COMMISSIONER KING: I understand that, but would they have separate seats and would it be limited to international or go to domestic as well?

DR MUNDY: All the boilerplate clauses, the application of the Goods and Services Tax, all those things are the same for all of them. So yes.

COMMISSIONER KING: Okay. So how would – and again, I'm pressing you on this but again, we can't put what sounds like good ideas to the government unless we have explored "Are they workable and what are the costs and benefits" as being - - -

DR MUNDY: Obviously a new approach by the Commission but - - -

COMMISSIONER KING: Perhaps in your time.

DR MUNDY: And before.

COMMISSIONER KING: Sorry, now, I've completely lost my question after that.

DR MUNDY: I understand, it happens.

COMMISSIONER KING: No, I have completely lost my - - -

COMMISSIONER LINDWALL: Can we move on to a different topic?

COMMISSIONER KING: Please move on to a completely different - - -

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DR MUNDY: Send me an email and we'll put the response on the record.

COMMISSIONER KING: Let's talk about the regional airports now. Now, in a number of testimonies, say from Rex for example, they talk about the concerns where the government gives a grant to an airport of an amount of money for a new bit of infrastructure and then the airport or the council, if you like, adds that value into the asset base and then depreciates it and charges for that in landing fees, something which it actually receives as a grant.

Would you agree that anything that's received as a grant from government shouldn't be depreciated by local councils?

MR THOMPSON: So I think again that there are, in a general sense, the funding of the asset comes via a variety of means. Often grants, and in fact in most cases, grants are either multiple contributions or (indistinct) contribution state, local government and Federal. I would say at the outset that the issue in a general sense around Australia is a small one because there just isn't enough grants available to fund regional infrastructure at airports.

So I think working your way down a decision around how funding is allocated, in most regional airports settings, the replacement of the assets and the ongoing upkeep of the assets is where the cost of depreciation is spent. It's lovely to get a grant, and in a lot of local government scenarios not particularly airports, but in fact airports in a very general sense regionally are under the ALOP and were given to local councils with an amount of money and very aged assets and serviced a very different fleet and a very different Australian network a very long time ago, and now don't work properly anymore.

So the concept of being able to upgrade your assets and seek funding that sees other than the local communities funding them, because our data identifies that something like 45 per cent of the regional airports operate at a loss. They can't cover the cost of operating facilities, let alone replacing and upgrading the facilities, and the rules are the same. So the rule book that comes from CASA about operating your airport says you'll have a certain standard and if you don't, you can't fly planes there because it is deemed not safe.

The cost of doing those works in regional areas is more difficult and harder often, and the costs are higher. Grant funding is often the only path to getting that solution. Now, at a fundamental level, how you then deal with grant funding going into ongoing charging, I think, depends on the source,

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the nature and the volume of the grant funding. I said earlier, we've said we think there is work to be done in that space. I don't reconcile from that. I think there is work to be done in that space. You can put an argument that if you've got some of the money gifted to you in a grant, why are you charging for it?

Well, the equal and other end of that argument is, "The money we are charging for is to enable us to have sufficient funds to operate it and then replace and maintain it as it goes". So it continues to serve the purpose. Often grants come with that as a requirement. You need to be able to maintain the asset to a certain standard.

COMMISSIONER LINDWALL: Of course.

MR THOMPSON: So I don't think there is one answer, but I don't think you can say you should never be allowed to put grant funding in your costs, and I don't think you can say you should automatically be able to put whatever funding you've got in.

COMMISSIONER KING: Would you see a benefit in having a coherent Federal, state organisation, if you like, or fund or something, which, as you say, cost benefit analysis for the regional airports? They come up with proposals. They work together. They finance them. Provide guidance on how it should be spent and then how it should be accounted for and so on, over time, including for the maintenance and operations of it?

MR THOMPSON: So I think the short answer to that is yes. The devil is then always in the detail of how do you make that work efficiently and effectively and not add a layer of operating costs and administrative stuff and reporting.

COMMISSIONER KING: Yes.

MR THOMPSON: But I think generally and under the guise of beggars really can't be choosers, to be perfectly honest whatever guidance came with an additional amount of money that came from Federal, state and allowed local governments to continue to fund their necessary infrastructure, would be welcomed. Not quite sure it gets to handcuffs in gaol and reporting every 15 minutes, we would hope not. But at this point of time, we nearly take anything, almost any set of guidance, because at the moment there is a void. There is not enough money there.

So it is hard for me to say would you not accept guidelines if money came with it? The answer is absolutely so and in fact, I think it is necessary with an industry this diverse and wide to actually have a pretty solid test. Can

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you come up with a standards one that applies across the country? I think that would be a hard task, but I don't think that should stop you having a go at it.

DR MUNDY: Sorry, can I just answer? There's two issues here. There's one about appropriate funding mechanisms for regional airports and I think we all agree that Commonwealth money should be prudently spent. The question is, what are the relevant issues in the benefits test? I just make that observation.

But the question you originally asked, Commissioner Lindwall was how should that relate to the setting of local prices? There is a body of regulatory precedent across particularly the state jurisdictional regulators about the treatment of gifted assets, and this sort of waddles and quacks a bit like that. But I'd make this observation. A council owned airport, the equity in that airport is owned by the ratepayers, whatever the equity is in them. It should be remunerated on a competitive neutrality basis on the same basis as the equity provided by someone like Cbus. Competitive neutrality tells us that the source of the equity should make no difference.

It is not clear to me, so therefore if council says "We need to spend $15m on upgrading our terminal", let's just say that's a reasonable decision, council should be able to earn a normal return on that $15m because otherwise it is in breach of its competitive neutrality obligations, I would say. So then the question comes along that says "Well, what if the Commonwealth gives the council that money for that purpose to be equity within that business?" It is not clear to me what the issue is here.

The other point I make is that the funding of the infrastructure – and this is the position of the Commission as you'll recall, you and I sat on the public infrastructure inquiry – is that the source of the financing should not be the consideration. So the absurd observation to make in relation to your question is that if the proposition is that an airport funded by Commonwealth grants should not be able to earn a return on the assets that the grants support, would suggest to me that the Commonwealth should not charge for the use of Badgerys Creek when it opens.

COMMISSIONER KING: Can I just follow up on regional airports? I don't know if you were present for the testimony of Rex in Sydney?

DR MUNDY: No, we are aware of it.

COMMISSIONER KING: Okay. Rex – and I am going to paraphrase their position as I understand it, so please take it on that basis.

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DR MUNDY: Yes.

COMMISSIONER KING: I won't try and – and if Rex believes that I haven't got it right I would hope they tell me, but my understanding is that Rex felt that our draft recommendations, I think they're 10.6 and 10.7, provide a framework for a longer term solution of what they see as pricing issues at regional airports, but, and we had a short discussion about whether some pricing decisions at regional airports related to market power or incompetence.

Regardless, and understanding the pressures that sometimes exist from local councils through their regional airports, the changes in state depreciation rules may feed through to local airports on islands, those sort of issues, Rex, in my opinion, had the view that whilst there may be a long-term solution, that still leaves them very exposed in the short term to situations where there may be completely uneconomic rises in price from their perspective. That leads to a lot of dispute and a lot of argy bargy is the term we use, very unproductive argy bargy on both sides, and you will be aware in certain situations there's been threats and actual situations where services have been withdrawn.

How do you see from the airports' perspective, and regional airports' perspective, how can that be addressed in the shorter term? Is there a - well, I'll put it in two bits. Is there a problem? You may not think there's a problem, but if there is a problem, how can that be addressed in the short term?

DR MUNDY: Can I just make first observations?

COMMISSIONER LINDWALL: Please.

DR MUNDY: It is generally promulgated guidance by most states that the trading activities of councils, and I've used the word trading very loosely, should achieve lower bound pricing. They don't earn a return on the capital but they should at least try to cover their depreciation. That to me, I think, is a non-contestable proposition if you understand how competitive neutrality has developed for councils in this regard.

The bulk of small regional airports don't cover their depreciation. It seems to me in some of these disputes, in particular King Island to look at, what King Island has I won't say has been told, but what they're trying to achieve is lower bound pricing based on some understanding of local government financing principles that prevail in Tasmania.

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COMMISSIONER LINDWALL: That's what they told us when we spoke to them, yes.

DR MUNDY: Yes. So that, and for example, a lot of businesses in country Queensland, that is a direction, so this proposition about lower bound pricing is common as mud. The problem is, as Guy alluded to earlier, these businesses don't have enough cash, and in particularly in a small community like King Island, if the airport needs cash, council can only get it from two places, or three. It gets it from a government, it gets it from the ratepayers, or it gets it by not doing something else, and the problem I see in this part of the issue in this, and particularly the proposition that a regulator should deal with this is that that regulator runs the risk of effectively suborning the fiscal decisions of elected councils because their resourcing is so - this commission has looked at the economic viability of local government in the past and I don't imagine it's changed. So I think there is a real fiscal problem. To be frank, most councils set their aerodrome fees on the same way they set the dog catching fees. They just index it to CPI every year.

COMMISSIONER LINDWALL: Yes. Could I - sorry, go on. We're running out of time because we've got another person coming on teleconference so I've got one more question because you did say in your submission that you think there should be fewer of the PC reviewed durations or gaps should be logged, though. Is there anything - I mean, does the reduce the credibility of it?

DR MUNDY: Your five yearly review is effectively a six-yearly review if you think about where the start and end dates are. Discussion has occurred in the past of a longer period. We, unlike Qantas, don't think reviews should be abolished, and nor do we think that this matter should be put in the hands of Parliament. That, I don't think, would serve anyone's interest. My proposition was more that, what is the magic about five years. It was me more - we were more seeking an explanation of what's the reasoning rather than it should be 10. It's not a big issue of dispute.

COMMISSIONER LINDWALL That's all right. We'd better finish it there, so thank you very much, Guy and Warren.

DR MUNDY: Thank you.

MR THOMPSON: Thank you.

COMMISSIONER LINDWALL: Then have a quick cup of tea and then we'll continue, I think.

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DR MUNDY: Thank you.

SHORT ADJOURNMENT **[11.15 am]**

RESUMED **[11.22 am]**

COMMISSIONER LINDWALL: All right we have Adelaide Airport on the line. Welcome Mark Young and Brenton Cox. I'm Paul Lindwall and we've got Stephen King. So if you could introduce yourself and make an introductory statement.

MR YOUNG: Thank you Commissioners, my name is Mark Young, I'm the managing director of Adelaide Airport and with me I have Brenton Cox who is our Executive General Manager of Finance and Corporate. Thank you for the opportunity to participate in the hearings this morning. I propose that we'll make less than 5 minutes of opening remarks and add some additional substance to our written submission. And then leave time available for any questions that the Commission might have.

So following that brief introduction I will cover the topics of market power, commercial agreements and consultation, the negotiate-arbitrate model, anti-competitive clauses and landside access. So by way of brief overview, Adelaide Airport is the capital city airport. We are focused on serving the city of Adelaide and the state of South Australia.

We very much view our success as being linked to the strength of the South Australian economy and vice versa, and we can only realise our business goals through passenger and route growth, and by providing our passengers with value for money, retail, car parking opportunities, and by ensuring that we remain efficient, which in turn can then support volume growth.

On the topic of market and countervailing power, our history is that our success is inextricably linked to the success of our airline partners at Adelaide Airport and their success within their broader networks. We can't, and we don't, take for granted the fact that airlines will serve the underlying passenger demand. The market doesn't automatically serve itself. We need to actively seek to promote Adelaide as a destination with current and potential airlines to receive growth in airline capacity.

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Our practical experience is that underlying market demand, will and does grow above airline capacity if we do not promote that airline capacity growth. This is particularly the case internationally where nearly 40 per cent of our customers looking to travel between South Australia and destinations overseas have to fly via another Australian airport first. When we negotiate with airlines, our objective entering these negotiations is to provide as much and as many operational options and flexibility as we can to ensure that we have a level playing field that can promote to all of our customers, while at the same time attempting tailoring bespoke arrangements for each of our unique airline customer needs.

In practice, during negotiations, we find ourselves constantly having to compromise on our objectives or otherwise unable to achieve them. This is because of the need to agree capital and capacity plans with airlines and there is the tension between what might serve the market as a whole and what might serve the individual commercial interests of each airline, and where the interests of encumbrance and competitors looking to grow do diverge.

As evidence of that, we have been unable to achieve our goals and that we have had payment withheld for a number of years as a result of these sorts of disagreements around where capital should be deployed and what our view of where it can be most effectively be deployed to benefit as many airlines as possible in order to continue to grow capacity.

In an international context we are competing with airports around Australia and Asia, if not globally. Every scheduling season we have potential airline customers tell us what they think that they could profitably grow from Adelaide, but they subsequently choose other destinations because they can make more money. For example, in the past years various airlines have stated that Adelaide Airport has come second or third behind destinations such as London, Madrid, Venice, Paris and other locations, Japanese, Chinese and South Korean cities in Asia, a number of North American cities in addition to all four major Australian airports and the major New Zealand airports.

I want to turn quickly to the topic of commercial agreements and consultation. Over time both consultation processes and commercial agreements have become more and more sophisticated. Increasingly our experience is that the commercial agreements reflect the deep mutual understanding of our airlines' needs and our investment requirements and service level expectations. Our approach is always to ensure that we engage in extensive consultation with airlines and other key stakeholders as early as possible in the process to ensure transparency and efficient

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outcomes. This approach generally does result in sensible commercial outcomes for all parties including (indistinct).

For example, it's typical for our airline agreements to include service level agreements which includes targets and financial penalties, infrastructure plans which include capital expenditure envelopes, directional plans including specified projects, and consultation process for updating the plans, elements of operational plans such as gate allocations and commercial agreements in relation to some of the aviation related services, and finally, an airport pricing including overall price path and incentive structures to encourage volume growth and efficiency improvements.

We take risk in relation to all of those areas, including risks related to traffic, aeronautical yield, expenses, capital expenditure and service level of commitments. It shouldn't come as any surprise that those agreements do take a long time to conclude and that they require the dedication of significant resources and that the negotiations are tough and challenging. This is the case and it should be the case as the stakes are high and the outcomes of those negotiations impact our community as much as they do the airport and the airline involved.

Briefly turning to negotiate arbitration model, our view remains that due to the complexity of these contract commercial agreements and consultation, and the strong interdependencies between the contracts with different airlines and other customers we simply do not understand how a negotiate-arbitrate model is practical and will advance the discussions in any meaningful way. We think it would create high risks for all parties and the broader community, and it's an unduly blunt instrument and we think it undermines the benefit of bespoke commercial agreements that have been progressively evolving.

In relation to any competitive clause removal, we consider that the Productivity Commission's draft recommendations to remove anti-competitive clauses in commercial aeronautical agreement may help. We say this because it's just not appropriate for the business and contractual terms of one customer to be brought into the room when considering the terms of an agreement with another customer.

Our view around landside access is that it is critically important to us that landside access is never, and should never be, a reason not to fly. We have, and we continue to work closely with our South Australian government to ensure that both off-airport and on-airport road infrastructure networks are development to meet the demands of both passengers and freight. An integral part of our upcoming master plan

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process is to agree a set of infrastructure principles with our state government.

By way of supporting travellers, Adelaide Airport doesn't charge access fees to public buses or shuttle buses used by off airport competitors, and we also look to ensure that the facilities for all of our public and private buses, our car parking, our taxis, and ride share operations are all broadly equivalent in terms of their convenience.

Our car-parking prices are set by competition from alternatives. In addition to off-airport carparks, public buses, taxis, drop off, pick up and ride share, we also have many passengers using informal, free onsite parking. In fact, I see every day people walking past our office to and from the terminal, using the informal free parking in areas around the airport. So the economics of car parking can be – is more challenging than it might appear, and this is due to the need to provide capacity for the peak hour, and the relatively high cost of providing multistorey car parking spaces in premium locations.

So in terms of introductory remarks, commissioners, that's all I wanted to say upfront. We thank you for the opportunity, and I trust that those remarks have added to our original submission in terms of market power, commercial agreements, consultation, the negotiate/arbitrate model, any competitive clauses and landside access. Happy to hand back now and take questions.

COMMISSIONER LINDWALL: Thank you very much, Mark. Could I ask about your terminal expansion plans? The Australian Airports Investors Group made a submission saying that Adelaide Airport significantly descoped its plans because of - a major airline didn't agree to the plans. How has that affected your operations and costs, do you think, going forward, and your customers? How does it affect your customers?

MR YOUNG: It's true that we had a number of years of negotiation with all of our airlines, domestic and international around a terminal expansion that we thought may provide in the longer term a more efficient facility over the long term. However, we accept the fact that dealing with our domestic airlines, that ultimately they had a different view about where our traffic would grow, how our traffic would grow from a domestic and international point of view, and ultimately we have to accept that. They're our major customer, and they are the counterparty to any successful airport fee negotiation.

However, we have the need and we have progressed with a project that is designed around improving, substantially improving, our quality and

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offering our customer experience service to our international airlines, and that's the project that we're getting on with.

COMMISSIONER LINDWALL: Okay. So does that not suggest that airline had a significant amount of countervailing power, because if you were able to build it as you originally planned and charged, they would have been forced to accept it, but clearly you've backed off that.

MR YOUNG: I'm not sure about the ability to force them – you know, charge and force them to pay. That's certainly not – in my experience, in 15 years of negotiating airline agreements, starting with the original terminal that's here now. I think we'd accept that we had a very robust interaction with our airlines and that the risks of not doing the expansion that we believe was the expansion required at that time, or could have been a longer run, more efficient expansion, may still materialise depending on where the growth – where the view about growth might come from.

I think the best that can be said is we had a – we agreed to disagree. We moved forward. We need to take control of our business. We cannot be kept in the spotlight where we are constrained in being able to improve our facilities and provide the best facilities that we can to the South Australian public, but also enable as many other airlines to get in and out of Adelaide as efficiently as possible. We had to move on the international side of things. That's what we've done; it is what it is.

COMMISSIONER KING: Okay, now - - -

COMMISSIONER LINDWALL: Yes. Sorry, go on.

COMMISSIONER KING: Sorry, just to clarify some points there. You said it was a robust interaction, but am I right in just characterising it, there were differences of opinions between yourselves and the domestic airlines about future passenger growth, and that was really the source of what you called a robust interaction, so it was really about forecast.

Did it go beyond that, or was it simply that the airport decided, well, we'll go with the airline's forecast and move ahead? What other action – why the term "robust", I guess is what I'm getting at.

MR YOUNG: Because of the fact that so many other factors also came into that consideration, i.e., where the terminal should expand, how it should expand, where the aprons should expand, how they should expand. One airline's view about where aprons should expand and why they should expand that way versus the other end, another part of the terminal that in

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our view may have suited a broader range of airlines. So there are - a number of considerations came into play. Then we also, we didn't even get to the point of having pricing discussions because we could not get to the point of agreeing the style and the scope and the timing of the expansion.

That said, the expansion that we are undertaking will be an extremely good expansion, and it will benefit all of the international airlines that operate here out of Adelaide. Some point down the track when we have to expand domestically, then we'll have to cross that bridge in terms of, where is the best place to expand the terminal or the aprons to accommodate what then hopefully may be an agreed position around where domestic growth is coming from.

COMMISSIONER KING: So again, just to clarify, did the airlines have a uniform position – the domestic airlines have a uniform position with a different view to Adelaide Airport, or did the domestic airlines themselves have differing opinions, for example, you mentioned where the aprons need to be expanded. Was it a case of – yes, please.

MR YOUNG: Pretty much had a standard view about traffic growth, but different views about how and where the terminal and the apron facilities should expand according to their own particular style of operation.

COMMISSIONER KING: So did it just all get too hard for the airport? That's sort of what I'm hearing.

MR YOUNG: No, not too hard. I mean we had a – we settled on a list of matters that we agreed to disagree on, and as a business, we had some other large issues that we had to resolve in terms of our international business, and we've moved on with that.

COMMISSIONER LINDWALL: Okay. You know that both BARA and the AAA have proposed effectively boilerplate contractual terms for airports and airlines to negotiate on. Do you think that would help your negotiation processes? Do you agree with that in principle?

MR COX: Yes. We've seen those proposals and spoken a lot with BARA about that, and actually the way that the AAA this morning characterised their desire to see those rolled out more is also what we've heard, in that when you're dealing with international counterparties that need approvals through multiple jurisdictions, I mean for us as an example, we're a very, very small part of their overall network, and even that would be the case in other ports around Australia.

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They're looking at ways to simplify those negotiations from their perspective, rather than having to have bespoke negotiations with each individual airport around international terms of access. They are looking to sort of simplify it, and now we're open to entertaining that debate and don't necessarily have a firm view either way on that, and that's something that we hadn't had to go down the path of in the past, but we're open to that discussion with BARA invigilating that discussion, I guess.

COMMISSIONER LINDWALL: That was Brenton speaking, I assume.

MR COX: Yes, correct.

COMMISSIONER LINDWALL: Okay. Now Adelaide Airport also suggests that the development of service quality indicators for ACCC monitoring should be agreed between airlines and monitored airports, with the ACCC to build on the work if necessary. Do you think that this should be coordinated between airports, so that each airport has the same set of indicators?

MR COX: Well we think that given the pretty bespoke or unique nature of each airline - airport and airlines relationship according to the, you know, the city that it serves, that service level standards and the monitoring of those should be something that the airports and the airlines operating to those airports should be agreeing and monitoring.

COMMISSIONER LINDWALL: Yes.

MR COX: It is also probably worth an opening comment in the sense that most of the time, airports and airlines already have service qualities that they are monitoring together, they're actually is a starting point and a useful constructive base and that would feel like the most appropriate place to start as opposed to a clean slate from an external party. That's just at a practical perspective but in many respects, it's not really our position to be judging on all of that. As an example, we have really quite bespoke existing arrangements in place and we sort of think that if we were being subject to additional service quality monitoring, you'd want to make sure that they were useful and that all the parties involved at least at the starting point, thought they were useful. There's nothing stopping layering on additional service quality levels above that, that are already being used but just as a starting point, that was just a practical matter we thought would be sensible.

COMMISSIONER LINDWALL: Fair enough. Could I now move on to jet fuel, unless you've got some other issues, Stephen. We will talk

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about jet fuel. You know that Melbourne Airport has moved to more of an open access scheme. Darwin is also buying back its joint facilities. Has Adelaide Airport considered changes to the current lease arrangements for the joint operated storage facility to improve competition of fuel supply to your airports?

MR YOUNG: Yeah, it is definitely a live subject and people often comment that if you strip away service quality, all you really need at an airport is a runway and jet fuel and at the moment, we're often in the situation where jet fuel access is held, controlled I guess, by a relatively concentrated group of people and that for competitors to access supply to an airport, they have to run through those competitors, so we sort of look at that and see the moves around the country and there is a sense that the previous system doesn't quite work and we are definitely interested and looking at opening up the access that we have at our airport. We are possibly in a slightly different situation to others in that we have no pipeline access but through our aeronautical agreements, the airport owns the (indistinct) so for us here, it's really the storage tanks that we're talking about that are held, what's really fuel companies. So there's a, I think, an acknowledgement that something does need to change there.

COMMISSIONER KING: Do you have enough supply certainty if you have expansions over time, to be confident that you won't have any outages or shortfalls?

MR YOUNG: No, that's part of the issue is that we only have two relatively small tanks. It's effectively (indistinct) only really a day-and-a-half of backup and then especially if there's supply issues down through the course and everything's coming by truck, they're really isn't much - we're definitely also in need of additional storage - at the moment it hasn't been coming because of some debates on tenure. So it's an area we need to improve on.

COMMISSIONER KING: Just to follow up on that, have you explored - given the need for additional storage, have you explored the possibility of bringing in a new fuel supplier to provide that storage?

MR YOUNG: We have - I mean the debate is a reasonable one here in that at the moment, because we're looking to explore different models, we haven't provided the existing fuel company incumbents with tenure and they, quite reasonably, desire tenure to invest in additional storage. So our focus at the moment has been to resolve that issue and what we're possibly looking at is, in collaboration with our airline customers, is taking responsibility for building that storage ourselves or through an expert. We have looked at alternatives for that.

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COMMISSIONER KING: Okay. I have got one more question and that's about your submission, describing the effects of Sydney Airport's regulatory constraints on Adelaide. How often did delays affect Adelaide Airport due to constraints at Sydney and how long do these delays typically last?

MR YOUNG: It's - I mean there's the old saying, "If Sydney sneezes the network catches the cold" and it really is relatively ad hoc and it's difficult to say how regular it might occur. It could be for all sorts of reasons that are occurring over in Sydney but when it does occur - and what typically happens is that our aircraft are pushing back on time but then having to sit and idle on the tarmac and that creates I guess at times, additional demand for apron and also taxiway space. It is very difficult to be specific about it and also very difficult to plan for it. What we were - when (indistinct words) I think and certainly others have, is that often it's a notion of that 80 movement cap is pretty blunt and it might be better done around scheduled movements, as opposed to flown movements and I mean even just had an example of last week and I was coming into Sydney from the US and on an A380 and we had this issue of where there were disruptions and the movement cap meant that the aircraft was kept in the sky and was circling over the Pacific for an additional half an hour. I was just thinking of 480 people wasting half an hour of time and all the jet fuel burning and it just seemed that that could be - and to really no benefit other than a blunt instrument - and it wasn't protecting people from noise because that aircraft eventually landed and it was just through that blunt instrument that you would have this huge cost.

In another context, if you could save that amount of time for that number of people on a regular basis, if that was a road, you'd be investing tens of millions of dollars but in this situation, by the stroke of pen and no obvious externalities - as in external parties suffering - you could relieve that congestion pretty quickly. So it just seemed like an opportunity to make some improvements and for us, it could reduce our need to invest in peak apron capacity to deal with where aircraft are being held on the ground in Adelaide because there's a disruption so no slots available in Sydney.

COMMISSIONER KING: Thank you, that's good, Stephen. So just one last area for me. You mentioned you don't charge for either public buses or the off airport car park drop-off buses, did I get that right?

MR YOUNG: Yes, that's correct.

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COMMISSIONER KING: I was wondering why you don't, everyone else - well most other large airports do and it's been put us they can get a return on capital. It has also been involved in setting up those slots, it's also been put to us that it's necessary for congestion management. Why don't you guys?

MR YOUNG: Well I think there's two considerations there. One is the congestion management and the other is the capital. A lot of our facilities are there and in place and for as long as it can be the case and we don't see the significant congestion issues or people taking advantage of the fact that there is no way for us to control the congestion like through pricing, we'll just keep doing what we're doing. But you know, there will come a time I would think, where continuing to be able to provide premium locations that are competing with all other sorts of ground transport just won't be able to be the case unless it is somehow priced and controlled through - controlling congestion that way. For us, it is as much about ensuring the efficient throughput of vehicles and people as much as anything. I'm not saying that we won't, at some point in the future, introduce some sort of access charge and that obviously will be designed around cost of capital - but presently, our system isn't clogging up to the extent where we think that that's necessary at the moment.

COMMISSIONER KING: But yes, I'm slightly confused, presumably there is investment in those locations, pick-up and drop-off locations, so there is capital. Currently in a sense you've made a commercial decision not to get a return on that capital. Why? You know, you could charge a price there and get a return on that capital. It is obviously not going to affect congestion. So congestion is off to one side here. Why have you decided not to get a return on that particular set of capital that you're investing?

MR YOUNG: We look at our ground transport assets and the capital invested in that really as a holistic system, and there are, you know, there are areas where we are not getting an adequate return on our capital. Those areas tend to relate to the public transport and those types of areas. There are some things that we accept that being an airport you're required to do, and one of them is to provide as much alternative in terms of ground transport as you possibly can. So the entire system we look at. We are earning a return but in some areas of that investment, it is significantly less than what you might regard as being a full commercial return.

COMMISSIONER LINDWALL: Okay. Well, I think will do us very nicely. Thank you very much Mark and Brenton for speaking with us today.

COMMISSIONER KING: Thank you.

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MR YOUNG: Thank you.

COMMISSIONER LINDWALL: Now, we move onto BARA. Is Barry around? Penny? If you could introduce yourselves and then give a statement as you see fit.

MR ABRAMS: We will. Okay. I am Barry Abrams, the executive director of the Board of Airline Representatives of Australia.

MS SWAIN: I am Penny Swain. I am a commercial lawyer who works with BARA and I would just make the observation that I'm not a competition lawyer, so my specialisation is infrastructure services agreements.

COMMISSIONER LINDWALL: Fair enough.

MR ABRAMS: That's what we do. Thank you. We will keep our opening remarks to about seven minutes, five to seven minutes. The Board of Airline Representatives of Australia does appreciate the opportunity to provide further comment on the Commission's draft report on the economic regulation of airports.

International airlines would like to convey three key messages in response to the Commission's draft report. First, international airlines were surprised that the Commission has downplayed their genuine and legitimate concerns over the provision of pricing of airport services. It isn't clear to us what evidence the Commission would need to see to take these concerns more seriously.

Second, international airlines do see a large gap between the performance outcomes deemed acceptable by the Commission in its draft report, and what they consider to be a reasonable standard for the prices charged. Airlines do remain concerned over problems in airport services that are reducing the efficiency of their operations.

Third, BARA working through multiple, unbalanced ambit claim airport service agreements is just simply wasting member resources. It need not be overly challenging or complicated to establish some appropriate accountabilities. What it actually takes is a willingness of an airport operator to accept that it must deliver its services to an appropriate standard for the prices charged.

In its submission to the draft report, BARA has presented empirical evidence covering on-time performance and baggage for international

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flights. International airlines do see plenty of room for improvement in airport services in supporting better outcomes for passengers and airlines, ones which could deliver an estimated 270 million in operating efficiencies over the next five years. So in a sense what we've just sought to do in our follow-up submission is just sort of re-package and re-present the first information to sort of say this is the magnitude of what we think we are dealing with here.

For us, we also believe such outcomes really do highlight the different incentive structures for the airport operators which we think goes to the heart of the differences in the service ratings the Commission has seen between international passengers and international airlines.

As we see it, the airport operators already have a commercial incentive to provide a quality of terminal services to international passengers that fits with maximising their discretionary retail spend in the terminal. As it's profit maximising to do so, airport operators are far more prepared to set benchmarks for international terminal services, and as long as those retail activities don't interfere with efficient airline operations, BARA has no issue with such incentives.

International airlines however, don't see the same positive incentives for airport operators in providing the core services needed to support efficient aircraft operations. These services include airfields, baggage systems, boarding areas, contact gates and airside bussing. It is here airlines report to BARA and the ACCC poor and highly unacceptable outcomes. It is also here where the performance benchmarks accepted by the airport operators in their airport services agreements, are weakest or often just simply non-existent.

These airport services underpin efficient aircraft operations and therefore we believe need to be evaluated on a stand-alone basis. We don't consider it is appropriate to effectively balance off deficiencies in these services against the quality of other services say going within the terminal, in reaching an overall performance assessment.

We would also say that the airport services agreements which are individual contracts between each international airline and the airport operator are also unfortunately proving ineffective in resolving problems in common use services that affect many airlines. This reflects, we think, the reality for an individual international airline operating to Australia in taking the commercial risk in speaking out and taking an airport operator to task over common use services.

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The Commission's draft conclusion is that the available evidence does not suggest the airport operators have systematically exercised their market power to the detriment of the community. It is also stated that overall the quality of service meets users' expectations. BARA disagrees with those conclusions unfortunately given its objective of supporting safe and efficient international aviation. International airlines would rate airport services below a reasonable standard in many areas. Identified problems include airside bussing services that regularly fail airline on time performance and aircraft turnaround targets. I could talk airside bussing for a long time.

Poorly performing baggage systems causing excessive rates of mishandled bags and we've presented further empirical evidence on that. The extensive foreign object debris around Sydney airport's international terminal which is impacting on the efficiency of aircraft operations, increasing airline costs and causing damage to their aircraft. Check-in facilities not balanced to airline demands causing congestion in some areas while other areas remain unused, and I would just note as BARA has always done in what its put in its airline views, what is published and is put to the Commission, when we've seen good outcomes and good efforts, we have always sought to recognise that.

BARA does note the Commission's draft report draws attention to the potential limitations and biases associated with airline surveys about airport services. International airlines have interpreted that, given it downplayed problems in airport services drawn from the BARA member survey, the Commission has discounted their evidence on the basis they might be seeking to gain the regulatory system.

International airlines which to make it clear they flatly reject any suggestion of regulatory gaining, rather they are doing their best to show where the regulatory regime is not delivering as intended. BARA does conclude that the airport's monitoring regime is currently not capable of supporting the delivery of airport services to a reasonable standard consistent with those prices being charged for those services. We don't see that revamping the monitoring report is going to improve matters because it is not going to change the underlying commercial accountabilities between the parties and the form of the agreement itself.

Unfortunately therefore, international airlines do not see a practical way left to address the problems they experience in airport services under the Commission's draft findings and recommendations. BARA has clearly articulated the commercial benchmarks that could deliver a reasonable standard of airport services for the prices paid and we detailed them in some detail in our first submission. They are based on principles for

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infrastructure services in both Australia and overseas drawing on people who have extensive experience in infrastructure service agreements and we've also sought to include a lot of information from the airport's council international themselves as a reasonable benchmark we should be working to.

We do consider that greater regulatory support in some form is required if the airport services agreements which ultimately underpin the delivery of the services and the pricing of outcomes are to be brought up to what we consider to be a reasonable standard. While the Commission has deemed regulatory options put forward by airlines as unwarranted, which is the negotiate-arbitrate model, I probably don't want to go into so much, it is still open to the Commission to propose reforms that would address the problems in airport services which BARA considers would better support safe and efficient international aviation in Australia.

COMMISIONER KING: Now, just to be clear BARA represents international airlines, some of which you would get new members at various times obviously, a carrier that's not in Australia now wants to come , they'd probably join BARA, is that basically right.

MR ABRAMS: Yes, we are a voluntary organisation. What I would often say about a new carrier is when they come they may form a view that look, you know, being part of the club might be a bit of a disadvantage and I'd like to go around and negotiate my own things and good on them, God bless them, they go and do what they need to do. Often once they get established, they see benefits in BARA which are much broader than just the negotiations of the agreement. So we provide details and updates as to where the industry is heading. Where these airports are going, security services. We have a pretty broad remit of activities that we get involved in and so it's for a range of reasons that an airline will see some value in BARA.

COMMISIONER KING: If I recollect, Sydney mentioned that – well, it has described to us that it is a very peaky operation and that a number of international carriers arrive pretty much at the same time. So the facilities are heavily, heavily used, baggage and so forth, for a very concentrated period. Then there's a long period where they're not much used at all. Is there anything that can be done in terms of timing to alleviate that, rather than new investments, because that comes at a cost obviously?

MR ABRAMS: It certainly does. I think when we look at this very critically in every case, we are trying to look at what are the sorts of incremental costs of expansion at these airports. I think, in coming at it from a couple of angles, one of the frustrations we find is it always just

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seems to be a big capital solution usually to a problem, rather than the airport operator going back and saying, "Okay, we seem to have some congestion and some issues here, how might we look at some of the scheduling? How might we look at towing? How might we look at coordination issues?", which is more OpEx type based. You need to have a very deep understanding of airfield operations to make that happen.

We are certainly supportive of any efforts by an airport operator that may induce a carrier to say they want to move out of that peak time, move more into the shoulder. But from BARA's perspective our job is to provide effectively a collective overarching view of the sorts of service outcomes and sorts of, what we might see as reasonably acceptable pricing outcomes, and then some of this then. And the role of the airport operator is then to take this on board and say, "Okay, based on everything I've seen here across all of these airlines, this is what I think will work".

COMMISIONER KING: Well, obviously the airports have said that they are trying to meet your services better over time and you are saying they are not.

MR ABRAMS: Yes.

COMMISIONER KING: Within the – I know what you have said about the monitoring regime, but if you were to continue the monitoring regime which is what we did recommend in our draft report, we might – and we did say that it needed to split out so more there's data and maybe change the quality of service indicators to some extent – can you think of good ways that that could be achieved that maybe would give an added incentive to airports to better meet the needs and requirements of the airlines?

MR ABRAMS: Here's probably a good example. And as we put in our second submission, we showed mishandled bag rates by airport. So in December 2018 for Sydney airport, so for directly checked-in bags by passengers in the international terminal, the rate of mishandled bags was almost six per 1,000. To put that into context, now, the system we have doesn't cover all flights, but I just extrapolated that over all flights, we were looking at nearly 6,000 mishandled bags through that system. Now, that's a lot of passengers who didn't get their bag.

The international airlines it probably has cost them about $1.8m reconnecting those bags to their passengers. For Sydney airport, it has meant precisely zero in terms of the revenues it receives from airlines for the provision of those poor baggage services in December 2018. So I certainly appreciate that providing more data and information can be useful, but from an airlines perspective, as I think Penny would agree, what

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airlines are after is the direct contractual ability to go and sort these problems out.

COMMISIONER KING: So you'd like to have an incentive in the contract - - -

MR ABRAMS: In the contract itself, yes. So what we would like to see is – and I suppose if I just come back to – and I've got to do this off my phone, just because it is from our first submission – what we made it clear was, we wanted some overarching principles that said airlines should be able to operate reasonably efficiently and not experience persistent significant delays as a result of unavailable or substandard airport services. And that airport operators should facilitate the safe and efficient journey of passengers through the airport.

So we would like those as overarching principles. We would then believe the airport operators actually have to have some financial skin in the game in meeting those objectives as we've agreed to measure them. At the moment unfortunately as we, I suppose, try to write a fair bit on these rebate schemes, they are not genuine financial incentives that hit the bottom lines of airports.

Now, what we've been able to do is at least try to get the airport to take some interest when these things go wrong, but until they actually have a bit of meaning and we've put in – written extensively in airline views around how you would look at caps and limitations and let's get – you know, we're not saying, "Well, we didn't get this service, therefore we're never paying anything". It has been around, how do you actually create some genuine commercial incentives to deliver better outcomes, rather than me having to wait for a monitoring report to then go wave it at the airport operator and say "Get on with it".

COMMISIONER KING: Monetary can be good for, you know, an average but for a particular day, if I was Sydney airport or something and they say "And I can handle three, seven A380s or whatever per hour" or whatever they handle, and suddenly because of weather events we get an extra one coming in, that would cause congestion, so how would you design incentives that – it's not really in the control of Sydney airport in that sense. Some of it is in their control and some of it is not.

MS SWAIN: All right. I would make the comment that it is unusual, in my view, to see a regime where a party negotiates around a rebate for services, effectively availability and performance, and there's a pool, let's say a pool just for argument sake, $100 and that gets added to the cost of the model and you're effectively paid in advance on the assumption that

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there is going to be breaches and that you're going to get the money back through the pool. That, to me, is a strange way of doing it, and it completely isolates the service provider from risk.

The rebates are quite modest and they are for very, very specific scenarios. The practical examples of people who have actually been to get money out of the system, as I understand it, it's a surprisingly low number, and also there is the individual airlines' reluctance to even push for that anyway. But there is no exposure to risk for providing poor service in a situation where you've got a sole remedy of a very small rebate. If there was ongoing, really poor quality performance, the suggestion, I'm sure from the airline would be "Well, that was your sole remedy. What are you going to do about it?"

I mean, that's the issue that the arrangement that has been put in place in a lot of these places, as has just been said, was simply to try and get management attention because just having no communication for them to even discuss these sorts of things makes it very difficult to get practical solutions which is what we have really focus on here.

And if you don't have any vehicle to discuss, even paying a couple of thousand dollars, people just aren't interested.

MR ABRAMS: And sorry, just touching on your point about how would you come up with these - - -

COMMISIONER KING: Well, yes, the risk sharing - - -

MR ABRAMS: Yes, the risk sharing, okay. What you sort of start with, a good way to do it is, you sit down and you work through some scenarios. So rather than first of all, trying to bash it out legally, you actually sit down and say, okay, what was the situation, and obviously we have many, many practical situations.

You can then into the agreement effectively just write the carve-out clauses. So the carve-out classes can be, you know, we have to agree that we're all going to apply some common sense here. So if an airline lodges and the airport operator comes back and says, "Well sorry, it was actually pouring down rain and the weather conditions were terrible," and you know, "we changed the runway modes," then that's the answer. We also have force majeure clauses and definitions, and they come in. Now just to be clear, we don't accept that the airport operator's own contractor's actions represent force majeure, so that's some of the things that have been pushed onto us that we think is highly unacceptable.

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But we do believe that with a bit of goodwill, it's actually pretty straightforward to sit down and work these things out, especially if you do it in – as we said, you're talking limited amounts, you're talking a cap. So ultimately, the airport's genuine financial accountability is limited to a cap. So you might say, "Maybe this might won't quite work in this situation or that situation." You just handle it at a high level. Let it run for an agreement, and then look to build on it and improve on it from there.

COMMISSIONER KING: Can I just follow up, so I guess my starting point is that these are issues of commercial negotiation. If for some reason they're not in the contracts working effectively from BARA's perspective, and maybe it's a matter of having the payments for failure to meet service larger, maybe making it easier to get those payments, maybe making it clearer when force majeure – I understand all of that.

I guess my question then is, you know, you've suggested the overarching principles, but is there any further role for government in here, or is it really that you want the commercial agreement facilitated in a better way? And if so, what do you see as being that better way?

MR ABRAMS: Very good question, and I appreciate it's difficult to answer fully. What I would say is at the moment, we were a bit taken aback to see comments in the draft report that said in terms of the commercial negotiations and outcomes, there was little cause for concern. Because we actually see many of the agreements to be, to be honest, rather basic and a bit backwards in terms of how we would view them against some reasonable standards.

There could be a lot of ways to go about this. What we're after, and I suppose what we did in our submission, was to say, there's the high level principle. Here is where we would see sensible service level arrangements existing. We would be more than happy to talk to the AAA and others around those high level principles. Our view is that though what we do within the aeronautical principles as one option, we make it very clear for each airport operator, these are important issues to be negotiated.

So you can no longer go to BARA and the airlines and say, "Sorry, if you want a rebate for equipment failures, you will need to prepay." There is some understanding that there will be some genuine financial skin in the game; that we will see some positive obligations to deliver the service. Perhaps we can even look at things like, you know, we will not see clauses that allow the airport operator to amend any clause at its own convenience."

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So as we would see it, we need to find a way of saying, one of the commercially sensible, good things that should be in agreement that clearly will align with dealing with the problems that we've raised, and somehow – so that could be, for argument's sake, given the commission has, I understand, reviewed the agreements from the airports – could that then not be part of the process and say, "Here are the things that we would expect to see in those agreements."

COMMISSIONER LINDWALL: Yes.

MR ABRAMS: Yes.

COMMISSIONER LINDWALL: So can I follow up though.

MR ABRAMS: Yes.

COMMISSIONER LINDWALL: Because BARA has also, together with AAA, have suggested a forum, for want of a better word, with government involvement to deal with what was put boilerplate contract issues.

MR ABRAMS: Yes.

COMMISSIONER LINDWALL: Do you see this as being part of that forum, or this as being separate to that forum?

MR ABRAMS: I think perhaps best just to talk to what BARA put forward first.

COMMISSIONER LINDWALL: Yes, please.

MR ABRAMS: Okay, which was a combination of, let's get the high level commercials right, because that's what's going to align you. We then had within every agreement this mundane, boring, but I suppose important from an infrastructure perspective, set of clauses around indemnities and insurance arrangements and the GST. And what we'd like to do is reach some sort of agreement or expectations about what they can just be. So as we would see it at the moment, it is a bit silly for Penny and I to be spending our time debating or commercially negotiating with an airport operator as to whether or not the international airlines should be indemnifying them for acts of their own negligence.

And we just sort of go, well this is just a stupid waste of everybody's time, but we do it all the time. So what we would like to see is some basis of people saying, you know, and we've developed many of these clauses

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already, that we then just shoot off to each airport operator and say, "Here is a standard set of clauses that have been deemed acceptable to the international airlines, because they've signed up to them. Please have a look at them, and if you think they're okay, just put them in." Don't give them, say for argument's sake, to your external lawyer to say, "How do I rework every clause to make in unfavourable for airlines?" These are the sorts of practical problems we're trying to get over so that we actually focus on the things that matter, rather than just this legal minefield we get into.

COMMISSIONER KING: Okay. So I understand that part of the complex.

MR ABRAMS: Yes.

COMMISSIONER KING: I'm trying to see then, is there any connection, is there any way for what you're solving in terms of the boilerplate clauses can also become a productive way of getting discussion going on the services and getting appropriate service levels and appropriate compensations or (indistinct).

MR ABRAMS: Yes, punishments, yes.

COMMISSIONER KING: Incentives, that's the word I'm after. Incentives in all those service levels.

MR ABRAMS: Yes. I think it comes down to a level of detail. So when it comes to boilerplate clauses and indemnities and the like, you can say – you can actually write the clause as we do and say, "There it is."

COMMISSIONER KING: You can't do that to services (indistinct).

MR ABRAMS: No, no, no. That's where you're just trying to agree that there will be general principles, because what BARA may want to negotiate with each airport might be quite different. There are no bussing services at Perth Airport. See, Kevin, I said I'd get Perth Airport in again. And so we wouldn't need or want to see any service type things around airside bussing. Airside bussing services are big and we think poorly performing services at major airports, so that's one where we'd like to see a lot of attention and detail. But we're trying to start from an understanding that the airport operator, he is going to be monitoring, measuring these things, and there are going to be some commercial consequences for what happens.

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COMMISSIONER KING: So that (indistinct) could, in your opinion, be – set those basic principles at least?

MR ABRAMS: Yes, yes. And then it's up to the parties to then go and negotiate.

COMMISSIONER KING: Yes.

MR ABRAMS: And then there needs to be, as we tried to put in our submission, and I get it that the AAA and that said, "Oh, is BARA looking for de facto type regulation here?" What we're trying to say is, if we've agreed that they are the things that matter and drive good outcomes, we should expect to see them in the agreement. It's then not good enough for an airport operator to say, "Well you know, the board and investors have thought about that, and we don't really want to go play ball on this," because that's what we see today.

COMMISSIONER KING: Are you concerned under – if there was a negotiate arbitrate framework, that it could be used by some domestic competitors to reduce investment and harm international airlines?

MR ABRAMS: That's a nice question to ask, given I have domestic carriers as BARA, though we only represent the international clause, obviously.

COMMISSIONER KING: (Indistinct words.)

MR ABRAMS: Yes, thank you. I think what I would say to that is in BARA's experience for the provision of international services, we have not experienced situations where we consider the ability to provide services to international airlines has been unfairly or impinged by what the domestics are seeking to achieve. Now these are obviously common use assets. As I would see it, every airport operator, as they keep saying, has an incentive to grow its international operations. In most cases, those services are separate to the domestic services anyway.

So we normally have our own domestic terminal, and then even where we find that terminal is integrated, like Mark Young was talking about with Adelaide. If they can't reach agreement with the domestics when we sort something out for the internationals. So I do struggle to see how it would happen in a practical sense. I mean one of the things that BARA does is, you know, we receive an offer from the airport operator. We then go to members to get, you know, sort of some high level feedback as to whether or not we think it's hitting the mark, and that's what we provide forward. So as part of that, and then obviously if BARA was part of that at all, all

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the experts sought any input from the international airlines, that's how we'd provide it in terms of the services we needed.

COMMISSIONER LINDWALL: But in case of say Perth Airport where there are effectively two domestic terminals; one occupied by our major Australian domestic carrier and the other one by all the other international carriers, one could argue that the former has a competitive advantage over the others.

MR ABRAMS: I think what I would say is that there's a lot of swings and roundabouts when it comes to airport capacity.

COMMISSIONER LINDWALL: It'd be (indistinct)

MR ABRAMS: Yes, I think that these things can, perhaps, be a little bit overstated.

COMMISSIONER LINDWALL: Yes.

MR ABRAMS: At the end of the day, no one ever said life always had to be fair and reasonable and an equal playing field for everybody in life and I think the Commission actually makes those sorts of types of statements in its report, which says, "Well, we don't expect all the parties at the table to have the same bargaining power." So the fact that there may be some differences in the services that you get and the efficiency of that, well, so what. That's life.

COMMISSIONER LINDWALL: Given the time, Barry, I think we better talk a bit about jet fuel which has always been a concern, now, after all of BARA.

MR ABRAMS: Yes, sure.

COMMISSIONER LINDWALL: We've identified a number of options in our draft report. I don't know what you think of them (indistinct) mentioning what (indistinct) for example, one was that the Minister for Infrastructure apply to the NCC for a declaration for jet fuel infrastructure sort of services. There was another option too, like under Part 7A and so on.

MR ABRAMS: Yes, I think as a general position from BARA is what we'd, in the first instance, would like to see is each of these infrastructure providers, you know, voluntarily just create a sensible and workable set of access arrangements that they could share with stakeholders for comment and, you know, that could be looked at and deemed reasonable.

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It was, then, I think, though BARA would support that if that doesn't prove to be the case, then, there is, then, a justification for some form of regulatory intervention as you've said there that, then, in effect, makes it happen in practise.

We see obviously Western Sydney Airport as a great opportunity. I think our only comment there was to say, "Don't call it JUHI," because we wouldn't expect it would be JUHI-type arrangements.

COMMISSIONER LINDWALL: Yes.

MR ABRAMS: And we also see a lot of advantage in the quality forum on the basis that – sorry, not the quality forum; the sort of coordination-type forum because we do need a way for the parties, for all the stakeholders to get their head around and understanding the type of arrangements going on there.

And I suppose if we're talking fuel, we've obviously provided our evidence and understanding of Sydney Airport's fuel throughput levy. We obviously don't see this as justified. I suppose this is my perspective; I wasn't particularly convinced by their arguments, but that's obviously something for the Commission to decide.

COMMISSIONER KING: I'm just wondering, is it worth them walking this through analysis or are we a bit out of time.

COMMISSIONER LINDWALL: We're a bit out of time. But if it's quick maybe or - - -

COMMISSIONER KING: Well, I'll ask them some slightly different questions because maybe that's one best done through correspondence. BARA obviously went for declaration of the Sydney JUHI; was unsuccessful. The reason put forward by the NCC related to the fact they simply, you know, because the way the legislation's worded, they couldn't be convinced that there was a problem that increased access would have a (indistinct) of benefit to competition in a market, other than the market for the service. Part of that just seemed to be that they just couldn't get the information from yourselves or from the - - -

MR ABRAMS: Yes, for BARA and it's the same for the Commission's inquiry as well, at the end of the day, we are down here in Australia and we have many international airlines who operate one or two flights a day and there's about 40 of them. So unfortunately you run into a problem that, in the big scheme of things, getting a large number of international

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airlines, the people here in Australia, to be able to convince their head offices to devote the resources to pull this information together to bring forward is unfortunately quite difficult.

What we have sought to do is through (indistinct) this time bring more information to the table and they've done that. So hopefully we find that to be satisfactory. But, yes, it is very difficult and I think it just reflects a practical reality of, you know, we are here in Australia, we're not a Singapore in terms of fuel consumption and in terms of these sorts of things. If we were, I'm sure there'd be a lot more stuff put forward.

I think importantly, though, that doesn't change the relative benefits that we could achieve here in Australia by getting reform that drove some outcomes where we had some competition on its merits.

COMMISSIONER KING: So one of our options we've put forward is either an ACCC Part 7A price inquiry or more formal monitoring and potentially with ACCC involvement, given the difficulties of getting that cost-base or the cost, the prices, the profits, all of that information which I've just mentioned, would those sort of things be beneficial so that, perhaps, the next time BARA or an airline goes to the NCC, the information's there.

MR ABRAMS: Certainly. More information has to be better and the more that we can shine a light on what is going on here. I suppose the way that we'd sort of come at it is try to give information on the number of bids as much as possible, so that we could get an understanding that, by and large, when an international airline turns up, what sort of competitive tension can it actually expect in its tenders.

Obviously, say through the coordination forum that's talked about, if there was a lot more information shared, and lodged and, then stored, then, that would provide everyone with a lot more information and understanding around the quality of the infrastructure, its capacity to actually facilitate entrance and the like. I mean I'm not surprised that somewhere like Melbourne at the moment, you can create some open access regimes and outcomes on the facilities there, but they're ultra-constrained at the moment in terms of, you know, you being a new competitor being able to come in and actually supply fuel into those facilities; all sorts of coordination issues and the like, I would understand.

You know, Melbourne JUHI can probably talk more about that than I ever could. But certainly you want a situation where the parties are comfortable that there's enough capacity there with some sensible access arrangements that would be broadly consistent with generating good

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outcomes. And that's always going to be a level of judgment call, but to do that we do need a fair amount of information.

COMMISSIONER LINDWALL: Well, Barry and Penny, I think we'll have to call it quits here. So thank you very much for coming.

MR ABRAMS: It's our pleasure.

COMMISSIONER LINDWALL: Thanks, Penny.

MS SWAIN: Thank you.

COMMISSIONER LINDWALL: So I might, now, invite Perth Airport if they're able to come forward. Usual thing, if you could introduce yourselves and then give a statement that you (indistinct) and apologies for eating into your lunch time.

MR PEREIRA: No pun intended.

COMMISSIONER LINDWALL: Yes, and no pun intended. Okay, so it's Brian Pereira and Kevin Brown, CEO of Perth Airport.

MR BROWN: Thank you, Commissioners. Perth Airport as a lessee operator of Perth Airport, welcomes the opportunity to appear before the Commission and to respond to questions that the Commission may have about Perth Airport-related matters arising out of our submission or about the Commission's draft report and to the economic regulation of airports.

Perth Airport has welcomed the Commission's inquiry into economic regulation of airports and through the course of the inquiry has provided extensive and transparent data and information, which illustrates that.

If I, first of all, just touch on investment and service levels. Under the light-handed regulation regime Perth Airport has made considerable aeronautical capital expenditure to address significant capacity constraints and service efficiencies which became particularly apparent at the commencement of the mining construction boom in 2009 and 2010.

Now, this investment has seen Perth Airport move from being one of the lowest rated airports on its Airport Service Quality Benchmark Panel through the earlier part of this data, to having, now, the highest overall quality of service rating in the past two ACCC monitoring reports.

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Now, as noted by the ACCC and its latest monitoring report, from an airline perspective, Perth Airport has significantly improved its performance over the past three years and was the only airport to receive a good rating from the airlines in 2017-18. Further investment to accommodate future growth and to provide the requisite capacity and level of service required by airline partners as planned. Information on these proposed investments has been provided to the Commission already.

I'll just touch in relation to the agreements with our airline partners — seven year price and service agreements with airlines operating at Perth Airport expired on 1 July, 2018. Perth Airport has since concluded new agreements with 23 of the 24 airline partners operating out of Perth Airport.

In 2017 and 18, Perth Airport's approach to negotiations for new agreements with their airlines partners was to conduct an open and transparent process where high quality, comprehensive and non-sensitive information was provided to all airlines, and indeed, any interested party through Perth Airport's publicly accessible website.

Contrary to the claims of one participant to this Inquiry, Perth Airport does use a building block methodology to assist in formulating agreements with the airlines, and does not make take-it or leave-it offers. Even a cursory examination of our publicly accessible website, the time taken to negotiate agreements and the content of those agreements will show the allegations of take-it or leave-it behaviour to be demonstrably false.

In fact, as part of our extensive negotiations over almost 18 months with that airline, we made several offers for longer term agreements, all of which involved prices lower than what was being paid under the previous contracts. The last of these offers was made before Christmas, and we are yet to receive a formal response to it. Despite offers of lower prices, that airline continues to underpay by up to 40 per cent.

As the Commission may be aware, legal proceedings are currently on foot in the WA Supreme Court, and it would be inappropriate for us to comment any further on the legal process, however, we do not want to have those comments made to the Commission earlier this week, to be unchallenged.

Both previous and current agreements with all airlines include risk-sharing mechanisms, incentives for passenger growth, and rebates recognising differential service offerings at Perth Airport. In collaboration with our international airline partners, Perth Airport is committed to exploring

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further the ability to link the risk-sharing arrangements to delivery of agreed service outcomes within the new agreements.

These, by necessity, see outcomes diverge from pure building block outcomes. This, and other evidence provided to the Commission, demonstrates our commitment to engaging in genuine, bona fide negotiations with all our airline partners on a bilateral basis. We endeavour to understand what is important and valuable to each of our airline partners, and work with them to find a win-win outcome.

In relation to the issues of market power: information Perth Airport has provided on Perth Airport's quality of service rankings, operating costs, capital efficiency, aeronautical prices and profitability has demonstrated that Perth Airport has not wielded market power through withholding supply, nor allowed quality to deteriorate, nor operating inefficiently, nor earning excess returns or imposing unreasonable prices and conditions.

In relation to ground transportation and carparking: Perth Airport has provided information which demonstrates that it participates in a competitive market for land transport services to Perth Airport. We have provided considerable evidence that consumers can choose between numerous land transport alternatives, and they exercise that choice.

Successive ACCC monitoring reports show that Perth Airport's carparking prices are the lowest of the monitored airports. There is no evidence from a decade and a half of monitoring to suggest that Perth Airport has engaged in any inappropriate conduct in relation to the pricing of its carpark products or the manner in which it has interacted with its competitors. There is considerable evidence to the contrary.

Perth Airport has not sought to restrict access to infrastructure in the vicinity of Perth Airport terminals, nor has it applied unreasonable price on non-price conditions of access. In contrast, Perth Airport has invested significantly to create fit-for-purpose, secure, and convenient parking facilities for the travelling public, and prices charged reflect the appropriate rate of return required to underpin the investment.

In light of the above, we now turn to the Commission's draft report. Perth Airport believes the draft report provides a considered position, based on thorough analysis and observable outcomes in the industry, and is not swayed by unsupported rhetoric. We note that the report's overall conclusions are in line with the submission of independent organisations and persons with expertise in the area of economic regulation, such as the National Competition Council, Mr David Starkey, former adviser on economic regulation to the United Kingdom Civil Aviation Authority, and

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Dr Harry Bush, former board member for economic regulation at the UK Civil Aviation Authority.

Perth Airport supports - with a few qualifications which are outlined in our submission in response to the draft report - the report's overall conclusions and recommendations, which effectively support the ongoing regime of light-handed regulation. Perth Airport believes the continuation of the light-handed regulation regime is critical to the ongoing support of investment in Australian aviation infrastructure, as outlined in the submission from groups such as the Australian Airport Investors Group, Infrastructure Partnerships Australia, and IFM Investors.

Detailed responses to each of the Commission's requests for further information are included in our public responses to the draft report. In addition, we will provide time-series data on utilisation rates of all at-terminal domestic carparks, which we are confident will rule out the exercise of market power in carparking at Perth Airport.

So, thank you, Commissioners. We're happy to answer any questions you may have of Perth Airport.

COMMISSIONER LINDWALL: Thank you very much for speaking with us today. Now, could I ask, given we just had BARA before, saying that there are some quality indicators that could be in contract with the international airlines, and they were talking about baggage handling and so on; is there anything you'd like to say about how you'd get the right incentives in place to service any international and domestic airlines, for that matter, in those type of products?

MR BROWN: No. With my engineering background, I love dashboards and looking at the trending of data, and we've been working very closely and extensively with Barry in BARA on this. Quite happy. Perth Airport; has some skin in the game already within the current agreements. I think there is a lot more scope to enhance a number of additional measures, and we've been doing a lot of work with our airline partners and BARA to actually scope-up what some of those measures would be.

For me, from the earlier questions, there are some common measures such as first-bag, last-bag, the availability of key plant and of equipment on the airport. But I think, let's look at this in a broader sense: an airport is made up of many different parties, whether it's the airline, the handling agents, the airport itself, but the border agencies as well; for us, one of the key issues we have is with the processing time for Border Force on arrival.

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So, I think having a holistic set of measures, and there's some of them - as Mark mentioned earlier - that may be more specific to the airport; there will be a core set, but there may be some specific to the airport. But we're certainly not shy of those measures, we're not shy of having skin in the game, and I'm certainly not shy of publishing them.

We have demonstrated throughout our pricing agreements over the last two years, an open and transparent publicly accessible website of the key data, and happy to do that on the basis of the operating performance of the airport.

COMMISSIONER LINDWALL: Now, I know you can't comment on the Supreme Court action, but A4ANZ earlier testified and said that - and I might be not exactly saying exactly what they're saying - but it possibly was that what you're achieving there is effectively what negotiate/arbitrate would be, but at a much higher cost. And wouldn't you be better to have negotiate/arbitrate as a policy and then you would be avoiding going to expensive Supreme Court actions?

MR BROWN: Well, I think from some of the discussion today, and leading up to today, it's obvious there's some ideas but they're not well-formed in terms of what that arbitration/negotiation model may actually look like.

My view is there's an already existing, well-defined regime in place, and that's exactly what we're following through at the courts in Western Australia. Why are we inefficiently talking about developing new regimes when there's existing regimes already in place? And that the courts, yes, offer an alternative independent umpire, and that is available to resolve disputes.

I think it's fair to say with the modern day case management techniques in place the courts, and I certainly consider the courts are actually faster, more cost effective in bringing that certainty to a conclusion, and they can certainly be well informed by expert witnesses to make sure that the full facts are in consideration in the determination of the outcome. So there's already well defined processes in place. That's what we're going through, and we know locally there are some significant cases through that arbitration model that have taken many years and considerable amount of money and are no closer to resolution. So I believe there's already models in place and it's normal for business parties who cannot agree on certain terms to use the courts to determine that and they have well developed models to resolve.

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COMMISSIONER LINDWALL: It does strike me, and maybe it's me, but it does strike me that a WA Supreme Court judge no matter how expert he or she is in matters of law, they aren't arbitrators, they're not airline or airport experts. Wouldn't it be better to have a system where you could go to an expert arbitrator with a background in airports and airlines who would be able to make these decisions rather than having to go through a very formalistic legal process with formal claims, formal issues of standing and so on. It does strike me, but I can see very few reasons why you wouldn't want the arbitrator type approach rather than a court approach.

MR PEREIRA: Yes. So if I can just answer that. So I think firstly I think the most cost effective and efficient way of actually reaching agreement is to negotiate. So I think that outcome for us, despite the fact that we're in the courts, that option is still open and we're continuing to reach out to Qantas to try and reach an agreement. The legal case that's before us is about a historical view, it's about what services have been provided and what prices should have been paid in the absence of an agreement. So it's not really about arbitrating what a going forward view of rates should be.

We still think negotiating should be the outcome, and then I think listening into the conversation earlier about a negotiate-arbitrate model - the negotiations are quite multi-dimensional and actually cover lots of different parties, as we heard earlier, and actually having an outcome on a very specific matter through a negotiate-arbitrate outcome could actually lead to some perverse outcomes for other users of common use assets at the airport, and I think some of the examples that we heard earlier are testament to the fact that it's very unwieldy, not very practical in terms of application.

COMMISSIONER KING: Probably if I go - sorry, I am just thinking of my question, I don't want to take it too far down the legal side, so I probably can't ask that. Sorry, Paul.

COMMISSIONER LINDWALL: Well, I mean obviously the court case is about a particular issue rather than a generalised one. The fact is at the moment you have two international terminals, (indistinct), as I mentioned earlier. Presumably that has an extra cost. Is there an extra cost to the taxpayer from this because the Border Force has to be in both places?

MR BROWN: Yes, Commissioner, there's a significant subsidy. I know Qantas often refers to a number of $25m. That's a very defined part of the project, of the build. There are additional costs on the project in addition to that, but as I am sure you can imagine duplicating facilities of Border

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Force agents, quarantine agents and Federal Police agents when there's already capacity in an existing facility and having to duplicate that, and doing that on a 24 hour basis, you know, it's maybe six to ten officers on duty at one time, but you need four or five times that to actually maintain that around the clock.

So, yes, a very considerable subsidy involved in duplicating facilities. It's extremely inefficient, and in addition to that you end up then having to duplicate security facilities, that you do not get the economies of scale, and the customers in the international terminal (T1), then having to pay a greater proportion of the costs of providing that security facility that's not being maximised in its utilisation for other flights who get a very significant subsidy.

COMMISSIONER LINDWALL: Do you have an estimate of that subsidy?

MR BROWN: I do.

COMMISSIONER LINDWALL: Are you able to share with us.

MR BROWN: I can't but it's a significant number; many, many, many millions of dollars.

COMMISSIONER LINDWALL: The monitoring report did say that Perth Airport costs per passenger are higher than other monitored airports. Could you describe why that might be the case?

MR BROWN: I will pass to Brian in a second, but that high level perspective there, Commissioner, you understand we had significant investment to do with the mining construction boom. Since then (indistinct) a million less passengers are passing through the airport. So, yes, when you look at the cost per passenger it does look disproportionately high. That has not been passed through to the airline partners during that deal. The forecasts and the development costs at the time were locked in. A million passengers have come off. That is a cost our shareholders have absorbed in the process. But as you will see, and it's been mentioned in the ACCC reports, those costs have actually continued to reduce over the last few years, Brian - - -

MR PEREIRA: That's right. So just to add to what Kevin just said the previous seven year agreements which started in 2011, obviously based on - informed by a building block model - had a trajectory of costs and a passenger forecast that underpinned that price.

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COMMISSIONER LINDWALL: During the peak of the mining boom.

MR PEREIRA: During the peak of - well, yes. I guess the cost base that was locked in there was what actually informed the price. So to the extent that Perth Airport incurred costs beyond that embedded costs in those agreements at the expense of the airport. So they were not passed on to the airline partners.

Then to add to Kevin's other point we have lost almost a million passengers since that mining construction boom. Again that's a passenger risk element that Perth Airport takes. Linking up into new agreements that we have just started from 1 July, and again 23 of our airline partners have got agreements, we have incorporated into those agreements efficiency dividends where we're actually locking in a CPI minus efficiency dividend to those prices to actually hold ourselves accountable to delivering more efficiencies of a time, because we do recognise, and certainly in the last two years we actually have taken costs out of the business, and we're not finished yet.

COMMISSIONER LINDWALL: What's the size of the efficiency dividend?

MR PEREIRA: We can't share that with you.

MR BROWN: I think is it fair to add, Brian, that the cost efficiencies that we have been working on are being passed through in terms of our most recent pricing. Our pricing has reduced significantly.

MR PEREIRA: Yes. So I think that's the other point. So every airline that has entered into agreement with us is now paying less than what they were previously paying under the previous agreements, anything between 11 per cent and 25 per cent less.

MR BROWN: I think, Commissioner, when you put that in the context our on-time performance is strong, our customer service ratings are strong from both our airline partners and the passengers and our costs are reducing. I think that's a good demonstration of running the business effectively and efficiently.

COMMISSIONER LINDWALL: Obviously mining booms are very difficult to predict. Governments were unable to, Reserve Bank unable to - in fact there was a long series of predictions that it would continue, mining investment (indistinct) for a lot longer than it did. Some people even said the terms of trade had become perpetually higher. Did that factor into your anticipation of the growth into your terminals and other

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activities, and perhaps you overestimated the growth that might have - obviously it's a million less now. Were you affected - I guess my question is going back in the other direction where there was a period before the mining boom when you were caught effectively by surprise with the growth of the passenger numbers because of the mining boom. Did that change your attitudes and you tended to overestimate a path of the mining boom? Is that a bit confusing what I just said?

COMMISSIONER KING: Did you make a mistake? I think that's what - - -

MR BROWN: I think if we look back at the terminals that were built, the terminal 2, the fly-in fly-out terminal, that was probably getting closer to its capacity during the boom, and it's a terminal that we're seeing a growth coming back again. So, no, I don't believe we made mistakes. We are facilitating the economic development of the state and it's important as the key infrastructure asset that we're able to do that, that the state is able to fully realise its economic worth. I think where we - and it's one of the reasons, and it's been in our master plan for some time, and that's why we are progressing bringing all our terminals together centrally is we really want to work with our partners, including Qantas, and we've had these discussions. We want to see common departure lounges. We actually want to see with domestic and international terminals are effectively one and the same as the terminals I was used to operating in the UK where you have no more deficient swing gate capability then that gate can be used for either or, because there are peaks in domestic and international at different parts of the day.

Your terminal doesn't have to be so big, you don't need as many gates, you don't need as much apron to park the aircraft. Then you don't need as much taxi way infrastructure to connect to the runaway. So, the whole philosophy of bringing our facilities together to make it easier for the passengers to transfer from one terminal to another and to do it more cost effectively and withdraw those – remove those subsidies at the border agencies, make the security at its optimum operational level and not duplicating, that's where the cost base can continue to reduce.

That's why we're confident that we will be able to continue to go over that cost base by bringing the airport operations together. And that will negate the need to build the standalone individual terminal. So with that existing infrastructure, enjoin that with what we're proposing allows us not to have to build this large infrastructure. But we're working closely with the government and our airline partners to make sure we can actually get that true common departure lounge capability which will be of significant benefit across the whole aviation sector in Australia.

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COMMISSIONER KING: So, the situation that you've gone through at Perth Airport, it's unfortunate from Perth Airport's perspective, but it is an interesting situation where you've had a significant drop in passenger numbers, and it was presumably unexpected. How did you see the airlines responding over time, so particular major domestic airlines. Did you see them relatively quickly reorganising their schedules, reorganising their fleet, perhaps not upgrading the fleet as they had intended to do for at least one of the carriers, how quickly did that occur or has that been a very slow process over a number of years, I mean, just from the airports perspective, what sort of flexibility did you see that the airlines perhaps had to – you can't get rid of your – well, maybe I would get rid of a terminal. Your capital source, how quickly could they adjust their capital?

MR BROWN: Well, within the same day. I mean, you just canceled the flight. You don't fly anymore as we heard earlier on today. I can't role up the runway and the terminals and move them to the east coast of Australia. The airlines, when I was working on the east coast of Australia, we saw flights coming out of there, coming here, they move with the market. As in, there's aircraft now coming back from the east coast to the west coast, because there is – there's an uplift in terms of that mining traffic again, it's starting to come back again. So the aircraft can be moved immediately.

The airlines have that maximum flexibility, we don't have that in our business. And that's where we take the risk on the passenger numbers. We're talking about seven year deals and working off forecast and they are challenged by our airlines partners. So, they're with us in looking at those numbers and then determining what's the capital spend in the infrastructure to support that growth. So, we're all putting our heads together and that's part of the negotiation process to understand what may be around the corner. But none of us have a crystal ball. But certainly the airlines have moved aircraft and east. They can also down gauge aircraft to go to smaller aircraft and they can reduce the frequency and we've seen all of that happen.

And I think we're starting to see some of that come back again. And just going back to Barry's point earlier, I mean, if you look at our cost base with that million passengers who are projected to be there, if you actually put that million passengers back in there, our operating costs are very similar and equivalent across the average of the other airports. But we can't rely on what it may be, that's why we continue to look to cut our costs accordingly and what we can do through the lean practitioners and our team, our continuous improvement ethos to improve what we do at the airport in terms of our cost base.

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But it's not just about cutting costs, it's the efficiency in the productivity and how can we serve our airlines customers better and make sure that the bags are delivered on time. The aircraft to depart on time, the customers do get a good experience, that the airport is clean, working, friendly, safe and secure. Those fundamentals can never be lost and that's certainly something very close to our team and I think the findings from the ACCC report and the independent customer satisfaction survey suggest that we do focus on those. And that's why for us working with Barry and BARA in developing these service standards is not an alien concept, we very much welcome Barry and his team on that, and I think together we'll actually develop a much superior outcome.

COMMISSIONER KING: I was going to go to land side - - -

COMMISSIONER LINDWALL: You go on to land side, yes.

COMMISSIONER KING: All right. How do – so the airport has charges, for example, for taxi pickups, for ride sharing pick-ups. Actually, do you have charges for off airport carpark buses picking up – so you don't have the charges there?

MR BROWN: No.

COMMISSIONER KING: All right. I'll put to you the same way that I put to Adelaide Airport, why not?

MR BROWN: Well there's a number of reasons – there's the key – well, there's the two key ones, public transport and its evolving in Perth, it's not quite where it should be but there is an inefficient – you know, there's an efficiency of people coming on the bus or coming on the train and the train will be connecting into Perth's central precinct by 2020, which will be very much welcome. Otherwise you have to keep lengthening your forecourt. It becomes very inefficient and what you do when you lengthen your forecourt, you make people walk further away, you're actually giving them an inferior service. I don't want to annoy my passengers and my customers, I actually want them to have a good experience. If they're in a good frame of mind, they will come and enjoy the experience, they might actually come sooner and they might actually spend more in the retail establishments.

So, there's a commercial perspective, you want to get your customers in and out of your facility smoothly. You don't want to congest them. And we certainly do not want to damage the fundamentals of our business which is the on-time departure of our airline partners' aircraft because passengers are not turning up or they're congested and can't get into the terminal through check-in, through security, embarkation control and on the aircraft.

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So, we're looking at this more holistically. So, it's more efficient to get people in and out, the airport operates more smoothly. And we are very much unique as an airport, we don't charge the off airport carpark operators, but we've actually got an off airport carpark operator who actually operates on airport. They're actually located within our carpark in both precincts. So, we're not shy of the competition and I think if you want to try and fight the shared economy that's evolving in our planet then I think you're on a hiding to nothing. So, you know, we're one of the first airports that encourages Uber and Ola to operate through the airport along with the taxis.

Yes, that does take business out of our carparks but that's part of the value in choice that our customers expect whether they want to use a free drop off and pick up or they want to use the bus or use the train. Or come on their bike on the bike paths, however it might be, we want to make sure we offer the full value in choice. And we're not scared of the competition that that brings with all these different mediums, the off airport or the on airport competition. That's healthy practice and we welcome that. Keeps us on our toes in terms of us commercially being focused on our pricing structure and our service standard. So, I don't think it does any harm.

COMMISSIONER KING: Yes, but following on that logic, you do charge the taxis and the ride share operators a pick up charge. Why do you charge them, on your logic, you should be saying well they don't get charged either?

MR BROWN: Yes, well you understand taxis typically would take one person away at a time. There's multiple taxis, we have holding areas for taxis, because there's literally hundreds of them. We then actually have to build the forecourt with dedicated lanes just for the taxis. The space one bus takes up, that takes 60, 70 people away, versus taking 60 to 70 cars in space, it actually takes up a lot of valuable space at the front of the airport.

But what we are very much focused on is that competitive neutrality in terms of what we charge all our Uber and taxis, it's all the same pricing, $3 per pick up, there's no cost for drop off. But they just take up a lot more space. As time goes on, we probably actually have to consider a multiple story car parks and actually having multiple layered forecourts to actually make sure that you're getting people with what they want as getting close to that front door and into your terminal. You can't keep extending forecourts. One of our longest forecourts in Perth Airport is in Terminal 2, the fly in, fly out terminal, its 220 metres long. It's one of the most congested because of its very peakiness of people dropping off and picking up. So, we're looking at different methodologies and controls to try and actually encourage people to use it for what it's made to be. It's not a

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carpark, it's there for the efficient movement in and out of vehicles of the forecourt. And that's why we offer an hours free parking in our long term carpark.

If you turn up too early, you can use our app and monitor where the aircraft is and park for free and then drive around when the person's ready to pick up. If you're closer in, you can have ten minutes free in the short term car park just behind the forecourt, if you want a bit more time to pick up. So, there's all of these different mediums coming together but its value and choice for our customers and – because not a lot of customers – you cannot provide a one-size fits all service for your customers. You have to provide the service to the full range of our customers and the 14 million passengers that use our airport each and every year.

COMMISSIONER KING: I think your submission, one of your submissions, you stated that – and I don't know which one unfortunately. I know it's on p.3 of one of them. In your submission you stated that for land side access operators, this is a quote,

> *PAPL does not therefore negotiate applicable access charges with any individual operators within any given mode.*

So, does that mean once you've got those access charges, you simply provide them to service providers, you know, as a take it or leave it offer, this is the charge, you pay it if you want to - - -

MR BROWN: I'm sure you can understand there's thousands of taxi drivers in and around each city and I think - - -

COMMISSIONER KING: But they're not the only providers - - -

MR BROWN: yes, there are of course many car hire operators. But the dispatch operators that the taxi operators work to, we work with them in terms of what options or service provisions there should be or what's working or what's not working and well and what the charge may be. But if you look at our taxi access charge, I think in the last 17 years, I think when it was first installed and it's only been changed once since then. So, it's not something that has changed on a regular basis. We're actually investing, I think it's $12m to provide a system for the whole airport that actually negates the need, that's more of a tolling system rather than the gold coins, and actually to speed up the movements of taxis and actually predict where the taxis are needed because they're tracked on site to make sure we get the right number of taxis in the right terminal at the right time.

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And that they're feeding through from the rank to be where the passenger meets them at the time that they need them. So we are investing in these systems to actually make a smoother operation and make it more efficient for the taxi operators and they can remotely determine if there's actually a need for them to come to the airport because the demand is about to spike or if it's a quiet period and there's no demand in which case they can go and make money somewhere else. So, it is adding value to the operators but we work through the dispatch companies to have those discussions.

COMMISSIONER KING: Okay. So that's going forward but the $3 that you've got in place. I assume there's no great science behind that. It's a coin based system, as I understand it, for the airport so it's presumably – it's got to be $2, $3 or it's got to be a multiple of gold coins going in there. Is that all the science that's behind it?

MR BROWN: Yes. It's a bit clunky and obviously it doesn't speed up the departure because someone getting the coins out and pushing them into the hopper this new system will eradicate that.

COMMISSIONER KING: Will that mean a significant increase in charges?---No.

COMMISSIONER LINDWALL: Will it lead to any increase?

MR PEREIRA: We're still modelling that but we're not expecting that to change radically.

COMMISSIONER LINDWALL: On jet fuel.

MR BROWN: Yes

COMMISSIONER LINDWALL: Could you describe what you think of what's happened in Melbourne, for example, the open access system, how are you happy about the security of supply in Perth and would you consider moving to more of an open access regime there?

MR BROWN: Most definitely and this is one of the key projects that BARA is driving and I think it's fair to say we very much share various principles on the fuel supply at the airport.

MR PEREIRA: So we are in the middle of negotiations. The current ground lease ends in three years' time. So all the discussions are around the key objectives that we're trying to achieve and one of them is security of supply and one of them is open access. So the key objective for us is to work with the JUHI operators on a new open access model. And so far the

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negotiations have been moving towards that and we're looking towards the Melbourne model as perhaps one model that could work but we're looking to get more transparency on that one to make sure that - - -

COMMISSIONER KING: Would you consider the Darwin model, for want of a better term where you actually own the infrastructure?

MR PEREIRA: No, we don't see that as our primary role to own that infrastructure. If we can facilitate the objectives of open access without actually owning the structure then that would be preferable.

COMMISSIONER KING: Okay, that's fair enough yes.

COMMISSIONER LINDWALL: Qantas in its submissions spoke about security costs and it said that it could – that many of the airports provide the same level of security at a much lower price. That's what they've said, what do you – you don't agree, obviously otherwise you'd get Qantas to provide the security.

MR PEREIRA: Yes, we recently took over Terminal 4 as part of the detailed transition piece and I can confirm that the security cost that we have applied going forward since transition is actually slightly lower than what Qantas are paying.

MR BROWN: And I think a fact of the contribution to that is the economy of scale of right of operating the security across the terminal, you need less management supervision. Whereas if you have a distinct company then it's got its own supervisions. So, we're extremely proud of our security standards which are important but the cost is important as well. But that is discussed and it's a straight pass through cost. And there's an annual wash up that returns any overrecovery, obviously more passengers come through and that's helping dilute the overhead, then that money is returned back to airline partners.

MR PEREIRA: And to that end, the transition involved taking over the existing same operator which is different to the operator at the rest of the airport. So for us, we believe that actually there's opportunities to further drive those costs down again once we get economies of scale, by providing a single operator cost on all the terminals.

COMMISSIONER LINDWALL: Do you have any more questions – you don't have any plans for a major new runway or something (indistinct)?

MR BROWN: We do. We have a parallel runway – we are - - -

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COMMISSIONER LINDWALL: So it's in your master plan?

MR BROWN: It is. It's being designed at the moment. We estimate it will be probably be required sometime between 2023 and 2028, that will depend on the passenger forecast. Currently, our movements are 132,000 a year. During the mining construction boom, we were up to 152,000 movements a year. Modelling the aircraft movements of the resource sector on its demands, actually , a new parallel runway will be required to serve 140,000 plus movements per annum. We actually need to have the parallel runway to maintain the on time departure, and that's' why we go back to the last mining construction boom and some of the congestion existed because it was over that threshold and we cannot allow that to happen again. So, that's why the design is in development at the moment and they're working with the airline partners to make sure that that's an efficient design.

MR PEREIRA: So, typically planning and environmental approvals and the like take several years.

MR BROWN: Of course.

MR PEREIRA: And I think during the mining boom, airlines were crying out for that second runway. So what we're doing is actually doing all the work now to make sure that project is effectively shovel-ready and the boom if and when it returns, will be ready.

MR BROWN: Well, that's a cost that we are bearing to develop that to have it ready. It's not an insignificant cost in terms of the design and development of the runway. It's possibly in the order of $50m to actually get it shelf-ready. So that's a cost we're wearing to make sure that we're able to make sure that our customers, our airline customers, are actually able to operate the business affectively as the passenger numbers increase.

COMMISSIONER KING: Now Sydney regulatory restrictions, I have asked this to other airports too, what type of (indistinct) on Perth and restrictions to Sydney's airspace?

MR BROWN: Well, I think we've heard earlier on, when there's a sneeze the others catch the cold because the aircraft are obviously coming across the country and there's a lot of flight movements into Sydney - - -

COMMISSIONER KING: But you've got the issue that you're further away, therefore there's less time that you have to be – the weather changes more rapidly - - -

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MR BROWN: And we do see that if aircraft don't get away in time or if there's weather issues or if there's any mechanical issues with aircraft unable to leave on time, and that can result in flight cancellations and they actually can't depart, they then have to cancel the flight and people get stood down and moved for the following day. So, yes, weather conditions have quite an impact on the network as well. Sydney is certainly prone to some significant storm weather.

COMMISSIONER KING: But you don't have the same issue as Adelaide with the extra tarmacs and the planes kept idling for long periods of time, half an hour or whatever they said.

MR BROWN: Well, potentially passengers can sit on the tarmac to be delayed because Air Services Australia will hold the aircraft and there's no point putting the aircraft into the air until they know that there's a slot to land at the other end. It's not good for the environment but equally the passengers get frustrated sitting on the ground for long periods of time and they just want to make their way on their journey.

COMMISSIONER KING: (Indistinct) final question in which case I think we've finished, thank you.

MR BROWN: Thank you.

COMMISSIONER KING: Thank you very much.

MR BROWN: Thank you.

MR PEREIRA: Thank you Commissioner.

COMMISSIONER KING: Thank you. It's time for lunch now. So we're due to resume at quarter past two with Cbus. So let's go and have a bite to eat.

LUNCHEON ADJOURNMENT **[1.08 pm]**

RESUMED **[1.48 pm]**

COMMISSIONER LINDWALL: Well, welcome back, everyone. I'd like to introduce and welcome Cbus, and if you've introduced yourselves, give a statement that you see fit.

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MS CALLEBAUT: Diana Callebaut, head of infrastructure at Cbus.

MR BRACKS: Okay. And Steve Bracks, the chair at Cbus; I've been the chair for the last 10 years. And obviously an asset owner, and it's that perspective I guess, I'm presenting here today. So, would you like me to proceed?

COMMISSIONER LINDWALL: Please, yes.

MR BRACKS: Well, first of all, could I thank the Commission for the opportunity to appear on behalf of Cbus Super. We are an industry superannuation fund; we represent about 750,000 members, about 150,000 employers. We have about $50 billion in funds under management; we're not the largest fund, but we're in the top quartile of the large funds in Australia.

At any one time, we would invest in the (indistinct), in property and infrastructure, probably about 25 per cent of that $50 billion; about half of that in infrastructure, about 12 and a half per cent. Or in our terms, something like about $6.2 billion we'd allocate to infrastructure, both in Australia and internationally, either directly or through other managers that we employ to undertake that.

At the moment, superannuation funds hold about 47 per cent of the equity in Australian privatised airports, so we're a significant player. We have, as Cbus, invested $5.5 billion, so we've got some capacity for further investment at the moment in global infrastructure assets, of which 22 per cent is committed to Australian airports; so a significant exposure. We're invested in all four airports currently monitored by the ACCC, as well as holding stakes in Adelaide, Launceston, Darwin, Alice Springs, Tennant Creek and Parafield.

As a not-for-profit member fund, we're certainly proud to be investing in Australian infrastructure assets that drive economic growth such as airports.
And whilst, as I mentioned at the start, I appear on behalf of Cbus, I can say with some certainty that other superannuation funds are equally as proud of the investment in our airports across the country.

Cbus has been investing in Australian airports since 1997, with look-through ownership of over 5 per cent, and 10 per cent in Melbourne, Launceston and Perth Airports, respectively. Over the years, a key pillar of the investment theses for Cbus investment in Australian airports has been the predictability of returns, which has been supported by the consistent application of the current light-handed regulatory approach. It

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is the consistency of process, as well as the predictability of outcomes that cannot be underestimated.

We are privileged to have the opportunity to invest in a range of infrastructure assets in different sectors and different geographies, however, as a result we are required to prioritise the allocation of capital, to maximise return for our members. From a portfolio perspective, a key pillar of the investment theses for the infrastructure asset class is predictability of returns; a reduction in that predictability for a certain sector therefore reduces the likelihood we will allocate capital to that sector in the future. And we have options, clearly, in investing in other infrastructure in other areas.

The benefits of a stable Australian airport regulatory framework are unambiguous: Over $15 billion has been invested in airport infrastructure since 2002, including $10 billion in aeronautical assets. There is an even greater task ahead, with an estimated $20 billion of infrastructure investment required over the next 20 years. We are keen, Cbus is keen, to support new runways being built in Melbourne and Perth, and the realisation of a range of other opportunities at regional airports.

The investments that make up this $20 billion in spending are vital to ensure both safety and amenity for domestic and international passengers alike; they are also investments that help foster competition in our skies, benefit passengers directly by lower airfares, and improve the competitiveness of our economy overall.

To ensure the continued availability of capital, and the benefits to the consumer and the economy overall that flow from this capital investment, it is critical that the current light-handed regulatory framework - which has been implemented so effectively over the last 15 years - is continued.

We've had some experience of more heavy-handed regulatory regimes in the energy and water sectors in Australia and the UK; we held some water assets in Thames Water - which we thankfully sold - those regimes involving explicitly setting out the allowed financial return for each business. This has presented a number of challenges for investors in these sub-sectors, including investment stress and significant caution regarding investment of future capital.

More broadly, the increase in regulation and uncertainty has increased volatility and sector-specific sovereign risk, with no change to return to offset that risk. And that is something that we would cost and identify, and we would expect compensatory increased returns if that was to be the case, which this asset class wouldn't give.

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Since the Commission recommended the removal of price controls in 2002, the problems that bedevil these industries, from both the perspective of investors and consumers, have been avoided in the Australian airport sector, and the benefits to the community are plain to see.

Cbus admits that regulatory stability is a key - if not the key - driver of new infrastructure investment, and in providing further capital to existing investments. We understand the complexity of balancing different stakeholder objectives. We are a responsible investor and we acknowledge the importance of having a social licence to operate, from the communities we interact with. We expect that the businesses we invest in - if they do possess an element of market power - will not use it to the detriment of the community and we're pleased that the draft report finds this in relation to the monitored airports.

We believe evidence supports the view that the current light-handed regulatory regime has successfully balanced airport, airline, community and other stakeholder objectives. It has enabled the owners of Australian airports such as our members, to generate sufficient returns to promote required investment, while not earning excessive profits, and this investment has contributed to the growth of the Australian state economies. The current light-handed regulatory approach has encouraged the negotiations that generate commercial outcomes and the innovation that comes with competitive markets, to benefit communities.

The light-handed regulatory approach should be maintained, in our view. And I'll stress again, that we do have options. If you look at the competing infrastructure investments that we undertake: ports; we own I think most of the ports in Australia, the Port of Brisbane, Botany, Port Kembla. Roads, the toll roads. These are predictable, certain, long-concession deeds.

There is less certainty and more volatility in airport ownership, and therefore, ensuring that we have the proper regulatory regime is going to be very important for our future investment in those. Otherwise, you know, clearly, that future capital requirement will not be able to be met for reinvestment and/or, we will look at looking at new investments in other areas.

COMMISSIONER LINDWALL: Okay, thanks very much. Could I start by asking about, if you could compare and contrast the ownership of a listed company like Sydney versus the other airports? And you're a passive investor, is that right, or - - -

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MR BRACKS: Yes.

COMMISSIONER LINDWALL: You do have this social licence to operate. Obviously, you expect of your investors, investments, but how do you manifest that and compare it and contrast the listed company versus the unlisted ones?

MR BRACKS: Yes. We largely invest through a vehicle, through IFM Services, which we're a shareholder in; one of the largest shareholders in it. And they bulk-up, if you like, the investments from several super funds: Australian Super, Hesta, Hostplus, Cbus. And they invest on our behalf, with our agreement and support, into these assets.

As a result, IFM Investors are able to nominate for the board; for example, I think there's one or two, I can't remember now. We also have another vehicle, Morrisons UTA, in which we have a significant investment through that infrastructure manager, in Perth Airport; I think something in Melbourne as well, from there as well, but certainly in Perth.

So we do it through those investment vehicles, and we have a stakeholder as a result of that, in the management of those airport facilities. So, that would be different to a listed company. Well, we're a shareholder in that as well, by the way.

COMMISSIONER LINDWALL: Yes.

MR BRACKS: I think superannuation funds, more broadly, have about 20 to 25 per cent of the Australian listed market at the moment. And with the funds under management growing and tripling in the next 10 to 15 years, we'll probably have about 30 to 40 per cent of the Australian listed market. So, we do have holdings there as well, but that's a much more passive investment from that point of view.

COMMISSIONER LINDWALL: You've implied before, or you said this before, but just to be clear: if the airports - as some participants have said - have been exercising their market power and earning excessive profits, would the claim be that you're happy about that because you're earning a lot of money for your superannuants and therefore, you can sit back with a lazy investment that's earning you a good return?

MR BRACKS: No, that's not true. I mean, we're not talking about excessive profits; we're talking about profits which are meeting a threshold which is required for that risk profile of that investment as a return to our members. And it's not excessive from that point of view; it is reasonable and adequate.

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But, it's on the edge, you know, it's very likely that if there was significant change that it might push it back over the edge and that we wouldn't be an investor. So it's not unreasonable; it's not dissimilar to the return of any infrastructure asset we hold.

COMMISSIONER LINDWALL: Do you want to add to that, Diana?

MS CALLEBAUT: Yes. I mean, we are a strong supporter of the current regulatory framework, and obviously there is always the credible threat of it becoming heavy-handed regulation. So it is not in our interest to actually earn excessive profit.

MR BRACKS: Because it could be manifested and - - -

MS CALLEBAUT: Because it would manifest and change the regime, and that presents increased risk for us and would be more challenging for us to invest more capital. So that's sort of just my additional - - -

MR BRACKS: I suppose the other thing is that we're long-term investors so we're not after – we're not listed, we don't have to mark-to-market regularly. And so as long-term investors we're looking for long-term sustainable returns. So that really obviates the need for any excessive profits - - -

MS CALLEBAUT: I would probably just add to that a structural comment, which I think is relevant. Is that as Steve previously indicated, we are invested through our two fund managers, both are open-ended funds. There's no exit. So often when there's an exit there is more pressure to increase profitability, but we are long-term investors, as Steve said, and we intend to remain invested, subject to the appropriate risk return profile of the investments.

COMMISSIONER KING: So, Steve, you did mention a threshold level of return that you would be looking for in an airport, are you able to say what that threshold is?

MR BRACKS: I think I was told not to. But it's probably not a great surprise that for the risk profile of infrastructure investments with the CPI plus 5 per cent type range, I think would be the – and that's commensurate with the sort of risk of that asset class.

MS CALLEBAUT: But it would also be fair to say the return is contingent on the maturity of the airport and obviously how long you've held it and the

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size. There's a number of factors, and as Steve said, we've got exposure to multiple airports, so they're actually different.

COMMISSIONER KING: Yes. And you did mention I think the volatility of airport ownership compared to say long-term or long concession toll roads, for example.

MR BRACKS: Yes.

COMMISSIONER KING: So would you expect a higher return or a higher threshold return for airports and for, say, long concession toll roads?

MR BRACKS: Yes, you would. Because clearly the revenue is different to a long concession deed, which is predictable rate of return each year for the next 25 years. It requires the economic activity of the airport, you know, landing fees, retail, car parking, all the rest of it, and that's really market driven. If it's market driven it's going to be less certain and less predictable. So yes, we would require a higher rate of returns as well.

For example, we know in purchasing a concession deed on a port that that port will largely operate in conjunction with the state gross product of the state in which it operates. It's largely sort of almost equivalent, whereas airports are not.

MS CALLEBAUT: There's a larger discretionary spend component in airports than there is….

COMMISSIONER KING: Just to follow up on that, does – because think of toll roads and ports, does the location of airports in that production chain of passenger transport, the fact that they are reliant on the airlines, unlike a toll road, it's directly – it's dealing with the end users. Does that change the way that you think about the risk of airports?

MR BRACKS: Well, yes.

MS CALLEBAUT: Yes, well location is obviously important, whether it's a toll road or an airport, and there's an illiquidity element to that the more remote it is. But, broadly, if you were looking in the same jurisdiction and you kept everything neutral, a toll road receives a lower return threshold than an airport.

COMMISSIONER KING: Okay.

COMMISSIONER LINDWALL: Obviously we've observed this inquiry and there's been a lot of, how would you say it, argy-bargy, for want of a

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better term, over the negotiate-arbitrate model and increasing regulation from its current level. Why do you think this has been manifested, obviously some participants think that or claim that the returns are excessive and a new model is needed to bring them down, you don't concur with that. Apart from what we've spoken about the implications of such a change in regulation, but why do you think it's being brought out in such a way now?

MR BRACKS: I'm surprised it is being, in a sense, because if you look at the last 15 years, there's really only been one case which has been brought before the courts for consideration, and that's in Perth, is my understanding. Otherwise, the market has operated, as it should. That is contractual agreements, commercial negotiations have been the key issues which have dominated, and we would see that as a material matter that was a move away from those matters of commercial arrangements and contract arrangements to an arbitrated system.

We would see that as a trigger to effectively say that there is heavy-handed regulation and probably therefore we have to account for that risk. And we would. I know in the work that Diana does, she would come back with a different return rate and risk profile that we would have to give to that asset class if that was the case, which would require a premium, a greater return.

COMMISSIONER LINDWALL: Presumably because there is a threat of regulation under the current system, which of course is – consists of annual monitoring and the five-yearly Productivity Commission review, that itself has a little bit of a risk element to it.

MR BRACKS: It has some, but it's predictable.

COMMISSIONER LINDWALL: Predictable, yes.

MR BRACKS: I think that's the key issue. And it's been accounted for. To interrupt that, to change that, I think would be a material matter which would have significant impact on investors. That is, would we look at re-investing $20 billion into the future? Well, yes, we might if you gave us a higher return and compensation for that.

COMMISSIONER LINDWALL: Yes, of course.

MR BRACKS: Basically. Because in the end, you know, we're serving our members and the best interests of members, and making sure we maximise the benefits for them in retirement is the key. So we want to make sure that we account for that.

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COMMISSIONER LINDWALL: How would you compare your investments in Australian airports compared to overseas airports and the regulatory structure, say, of those airports?

MR BRACKS: Similar.

MS CALLEBAUT: Yes, so they're obviously different structures. I think the critical aspect of it is that when you invest you invest along the assumption of the regulatory regime in place and how that's going to play out going forward. So it's all about being able to price in at that point of acquisition, what you expect going forward.

COMMISSIONER LINDWALL: And the reliability.

MS CALLEBAUT: Correct, and the reliability of that. So the challenge is once you're invested when there is a change, because that changes the risk profile once you're actually already invested. If it's already set at the beginning, it's a different evaluation.

COMMISSIONER LINDWALL: You took that into account.

MS CALLEBAUT: Correct, correct.

MR BRACKS: And we had the situation, not an airport, with – before your time – THAMES Water, which we were an investor in, and the regulation changed, heavy-handed Government regulation came in, we divested that asset, we didn't re-invest in it. That's an example, I guess, to a large extent.

COMMISSIONER LINDWALL: So are you able to expand on that? So was it – I mean, if it's a one shot change to a heavy-handed regulation - - -

MR BRACKS: It was price – controlled price regulation which the regulator was enforcing, which wasn't enforced previously, and that caused us to look at redeeming that asset, which it took us a couple of years, not easy to redeem an asset, but we did, and we redeemed it.

MS CALLEBAUT: But just building on that, it's also a signal about the certainty going forward, and so in the case of UK Water, there has been increasingly adverse regulatory determinations across time and we have actually other exposures there through funds, and it is – as often is the case, it's only in retrospect we can look back and say that divestment decision was the right decision, because subsequently on these other assets we've had come under a lot of stress.

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COMMISSIONER LINDWALL: Could you think about or postulate some – we've obviously outlined some changes to the current framework in our report, but I don't know if you want to comment on particular recommendations. But if you were to improve the current regulation of airports, where would you be looking?

MR BRACKS: I think we're happy with the direction that the Productivity Commission's going in, so we're happy and satisfied that what has been proposed in draft form today is where we would see significant benefit going forward.

COMMISSIONER LINDWALL: But you see an important role for five-yearly or so reviews?

MR BRACKS: Totally, yes. No question, yes. Public transparency and monitoring is very, very important and we would support that.

COMMISSIONER KING: One of the proposals that has been put up is a negotiate-arbitrate type approach put on the airports and the airlines, which I suspect their opponents would say that is an alternative light-handed approach to regulation, I don't think they'd characterise it as heavy-handed but they're obviously for themselves. What would be Cbus's, would Cbus think that is a useful way forward, would Cbus have concerns about that as a way forward?

MR BRACKS: Arbitration?

COMMISSIONER KING: A negotiate-arbitrate regime being - - -

MR BRACKS: We'd have concerns about it.

COMMISSIONER KING: Why?

MR BRACKS: The lack of predictability on outcome I think, in relation to the original undertakings that you had when you reinvested in the asset in the first place, which might disrupt therefore the effective return that we envisage. Without compensation - if there was compensation, if that was applied to investments (indistinct) okay, we could have a look at that.

COMMISSIONER KING: But the point is, it's an increase in risk and you want an increase in returns, not just - - -

MR BRACKS: And we're obliged if there is an increase in risk to identify it, cost that and it will be a factor in our thinking in the future.

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COMMISSIONER KING: I think we have probably exhausted everything we could ask here - there's lots of other subjects but in terms of airports, anyway.

MR BRACKS: Right thank you.

COMMISSIONER KING: Thank you very much.

COMMISSIONER LINDWALL: So now Frontier Economics, if they are here? Hello, I'm Paul Lindwall, good to see you. Again, if you wouldn't mind introducing yourselves and give us statement as you see fit?

DR WILLIAMS: I am Philip Williams, I work at Frontier Economics.

MS WILSON: Anna Wilson, also Frontier Economics.

MR DAVIS: And Warwick Davis, also from Frontier.

DR WILLIAMS: I thought I would open by talking a little bit about a couple of lessons for this inquiry, generated by the literature on multisided platforms. An airport is a multisided platform, like a shopping mall. Airports offer aeronautical services to airlines, pipeline services to suppliers of fuel, car hire concessions to car hire operators, retail concessions to retailers and on occasion, car part concessions to car park operators.

An airport does not necessarily determine the pricing and marketing of the services of the users of the platform. In the case of most Australian airports, the important exception to this is the operation of car parks. In Australia, airports tend to be vertically integrated into the operation of car parks, rather than offering these services as part of a multisided platform. There are a number of contributors to the literature on multisided platforms who observe that platforms sometimes choose whether or not to vertically integrate into one or other of their sides. There are positive network externalities among the various services produced by airports, however, like newspapers, these network externalities work predominantly in one direction. The greater the take-up of aeronautical services, the greater is the demand for the various non-aeronautical services.

Some multisided platforms tend to tip to monopoly; airports tend to tip to monopoly principally because of interconnectivity. Each airline wishes to land and take off from the airport used for other routes, so that passengers and freight can interconnect or particularly passengers. Only in large

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cities do we observe multi-homing by airlines. In a multisided platform controlled by a monopoly supplier, the platform owner is in a position to seize all the gains from interactions among the participants on the platform. That is a quote without acknowledgment.

My first proposition is this - or the first question I wish to address is this. Has the existing regime been effective in deterring potential abusers of market power by airport operators? The Commission has been asked to consider whether the existing regime is effective in appropriately deterring potential abusers of market power by airport operators. How should one assess the market power of an airport? The tendency to tip to monopoly does not necessarily mean that each airport has substantial market power. The ability of a monopoly to generate monopoly profits will depend on the demand for the various services that it produces. Indeed, even a single producer monopoly may have little market power if demand for its services is relatively low compared with the fixed costs it needs to recover.

When analysing the market power of a multisided platform, one should not treat each side as a separate market; one must acknowledge the externalities that exist between the various sides of the platform. Prices on one side of the platform need not reflect the cost of serving that side.

The operator of a platform will balance the participants on the many sides of the platform. For this reason, one cannot assess the monopoly power of an airport by comparing the price of one of its products with its long run average costs. In particular, if the externalities flow overwhelmingly in one direction, the price of the originator of the external benefit may be close to, or even below, marginal cost.

Examples of such strong one-way flows are from newspaper readers to advertisers or from airlines to purchasers of non-aeronautical services. This means that any attempt to assess the market power of an airport by examining its profit on aeronautical activities, is likely to seriously underestimate its degree of market power.

The extent to which a monopoly airport is able to exercise market power is its ability to generate profit over the sum of its operations. In many cases, this is often difficult to assess, for two reasons. In the first place, one generally lacks cash flow data for a period sufficiently long to enable inferences to be drawn. Secondly, even if one has cash flow data for a long period, one generally lacks evaluation of the airport at the beginning and end of the run of cash flow data.

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As we point out in our report assessing the profits of Australian airports, these problems are of little consequence in the particular case of the four Australian airports which report data to the ACCC.

Because of the theory of multisided platforms and because of the availability of a long run of cash flow data for the four reporting airports, the best way to assess the extent to which they are able to exercise market power is to use the available cash flow data over the sum of their operations. To assess the market power of an airport by looking at the prices or profits it generates from one particular source of revenue is to violate the lessons economists have learnt from the literature on multisided platforms.

The second question I'll address is whether the monitoring regime conducted by the ACCC has been effective. The Commission has been asked to consider the effectiveness of the monitoring regime conducted by the ACCC, including the methodology used and the adequacy of the information collected. In my opinion, the monitoring regime conducted by the ACCC produces a misleading picture. The principal reason for this is that it reports on one particular side of a multisided platform. The data contained in the most recent ACCC monitoring report illustrates the problem.

The ACCC monitors only aeronautical services, however in the case of Sydney Airport, non-aeronautical services generate 45 per cent of revenue but are allocated only 25 per cent of its costs. This results in a set of non-aeronautical activities which generate 45 per cent of the revenue being attributed with generating 60 per cent of EBITA. The ACCC's monitoring gives a distorted picture because it reports only one side of a multisided platform. That is all I wish to say by way of opening.

MS WILSON: I think we're happy to take questions.

COMMISSIONER LINDWALL: Okay.

MS WILSON: I mean, you guys would be aware that we've obviously been involved in supporting A4ANZ on this.

COMMISSIONER LINDWALL: Yes, yes.

MS WILSON: But also, AFIA and Qantas.

COMMISSIONER LINDWALL: In the terms of a multisided platform, where do you draw the line? So for example, an airport could own all the land that it currently occupies, plus it could own a lot of other operations

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well away from an airport; should that be included in the multisided platform?

DR WILLIAMS: No, one has to look at, in fact, whether this is a major problem or a small problem. If one actually looks at the cash flows at the airports, these amounts of money are trivial; in the cases of the Australian airports, the amount of revenue that they generate from things that are not related to the flying of passengers or freight is really trivial. But that could be removed, yes.

COMMISSIONER LINDWALL: So business parks, for example?

DR WILLIAMS: Yes, if they run a business park or something like that.

MS WILSON: Well, I think we'd add to that though, some caution in the sense that I think where we probably differ in some of what the Productivity Commission has said in the draft report; is that a lot of these non-aeronautical services, in a sense, are linked to the aeronautical services. Take, for example, a business park: most of the businesses that you would anticipate to be in a business park next to an airport would, in fact, be related to freight activities, logistics. I mean, that's a logical spot for them to house either their sort of back-office operations or any other aspect of that.

I think it's really (indistinct) that that's their preferred location, and therefore in some respects you have to ask whether that is passenger or freight-related, and therefore potentially within what you could argue is a reasonable till for an airport.

COMMISSIONER LINDWALL: Or freight, yes.

MS WILSON: Yes. I mean, sort of our preferred approach more generally is that you would adopt a sort of hybrid till which takes anything out that is clearly unrelated; and when I say clearly unrelated, say, you know, a wave park or a - - -

COMMISSIONER LINDWALL: DFO.

MS WILSON: A DFO. But as Philip mentioned, these things are trivial, particularly in the context of looking backwards. If you're looking at existing data for the past 20 years, this is not a thing that affects the outcome of the analysis.

COMMISSIONER KING: Can I come back to your two-sided market, or your two-sided platforms approach, or multisided platforms approach?

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So as I understand, you're saying that it's really the aero that drives the demand for things like carparking and - - -

DR WILLIAMS: Principally. There may be some other flows back the other way, but it seems to me that it's largely one directional, yes.

COMMISSIONER KING: Yes, and that's why you need to look over the entire platform for profits, to look at market power. But that same theory would say that if the aeronautical is creating the positive externalities, then you would expect aeronautical to be relatively under-priced, compared to the others. And to use your own example, consumers don't pay for the newspaper, and the newspapers make their money from the advertising.

Now, obviously the airlines pay something for the aeronautical, but on your analysis, the airlines are paying less for their aeronautical charges than if these other parts of the market – car parking and so on - weren't there.

DR WILLIAMS: No, not if they weren't there, but rather, if you say to allocate costs according to revenue, airlines would definitely be paying less than would a lot of the other non-aeronautical activities.

COMMISSIONER KING: Indeed, airlines may be paying below cost.

DR WILLIAMS: Well, that depends. I mean, I don't need to tell you, but what is meant by "cost" of aeronautical, or "cost" of non-aeronautical is not clearly defined at all. But if we were to think of some other way; I mean, costs are sometimes allocated by revenue. If you think of it that way of allocating costs, well then definitely, aeronautical would be paying less, as I pointed out with respect to the example of Sydney.

MR DAVIS: I think the point is, like, a monopoly platform will have the same price structure as a competitive-priced platform, it's just that all the monopoly prices will be higher.

MS WILSON: Yes. The question at hand is whether - - -

COMMISSIONER KING: Sorry, hang on, let's just explore that for a moment. So a monopoly newspaper that was not receiving advertising would not be distributing free to its customers, it would be charging those customers; I'm sure you agree with that.

MR DAVIS: As in price structure though. I'm saying if you're not competing, you know, paid for newspapers or something, they've got the

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same basic structure but the monopolist will have higher prices on both sides.

COMMISSIONER KING: But the simple facts of two-sided markets, where you have the direction moving from aero providing the positive externality to other services, the simple fact, as a matter of economics, is that aeronautical may be receiving prices, the charges for aeronautical may be below - they could be below operating costs.

MR DAVIS: They could be, in theory.

COMMISSIONER KING: In theory; I'm not saying they are.

MS WILSON: I mean, that's not the question at hand, at the end of the day; the question is whether that monopoly platform should, in fact, have prices that are lower overall, with the same price structure, not whether their price structure would change.

COMMISSIONER LINDWALL: Well, it could mean that the non-aeronautical prices should be lower and the aeronautical higher, but the overall level could be lower.

MS WILSON: But why would the price structure change?

DR WILLIAMS: What I was trying to tell you earlier had nothing to do with what ought to happen; rather, what I was saying: accept that in assessing market power, one ought, in the case of a multisided platform, to assess the cash flows over the whole range of the platform. Now, it's another question altogether what would be the optimal regulatory or legal set of arrangements to solve a problem if we found that there was significant exercise of market power by this monopoly platform. So, I think we have to keep these issues separate.

COMMISSIONER KING: Well, happy to keep them separate, but the pricing. As you said, prices will change in their balance because of the positive externalities - - -

DR WILLIAMS: Indeed.

COMMISSIONER KING: - - - in the favour - compared to a monopolist where these externalities didn't exist - in the favour of the airlines and against car parking, retail, and whatever else.

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DR WILLIAMS: I'm sorry. There was some confusion about what the comparator was. Of course, if there were no externalities, well then what you say is right: that both prices would be higher; that's the corner sort of - - -

COMMISSIONER KING: So to put it simply, the airlines gain a benefit from expensive carparks.

DR WILLIAMS: No. They gain a benefit from - - -

COMMISSIONER KING: (Indistinct) for once.

DR WILLIAMS: No, no. Most of the - - -

COMMISSIONER KING: Well, except that (indistinct) - - -

DR WILLIAMS: - - - externalities - - -

MS WILSON: Services, yes.

DR WILLIAMS: Most of the externality is in one direction, and I agree with the proposition that that means that the prices of aeronautical services will be relatively low, compared with the prices of other services. And that will be true whether there is say, overall revenue capped regulation or there's no revenue regulation. I agree with those - - -

COMMISSIONER KING: And if the externalities didn't exist, aeronautical prices would be higher and car parking prices would be lower for that monopolist.

DR WILLIAMS: Other things being equal, yes.

MS WILSON: Yes.

DR WILLIAMS: That's all I'm getting at.

COMMISSIONER KING: But I just wanted to verify - - -

COMMISSIONER LINDWALL: It's a matter of what we compare with what, yes?

MS WILSON: Yes.

COMMISSIONER LINDWALL: So Philip, would you also be suggesting that the monitoring regime which you say is inadequate

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because it excludes a lot of other services could be improved by adding these other aspects of an airport to that regime?

DR WILLIAMS: Indeed. It would give a much more truthful picture of the market power of airports.

MR DAVIS: Well, just to add to that. I mean, I think, you know, obviously the key difference between the work that we've done on profitability and the work that you've done on profitability, you know, we get results that are much higher returns and that simply comes - and we've both used, presumably, the same data: it's out of the ACCC monitoring.

The point is, with our data, we've used the revenue and costs on the non-aeronautical side as well. So in a sense, all we're saying is, that's what's explaining that difference. So you know - - -

COMMISSIONER KING: Fully understand that.

MR DAVIS: - - - if you're coming up with returns that are you know, 10 per cent on aeronautical and we're coming up with returns that are 20 per cent and it's non-aeronautical - or sorry, it's the total airport - the differences, obviously, are non-aeronautical. My point is, the monitoring regime already picks up some of this.

COMMISSIONER KING: Yes, true, true. Okay, so let's take perhaps, a non-platform approach about it. Let's imagine you had aeronautical was highly competitive and carparking was being abused ruthlessly by the monopoly, but there weren't any externalities going on in here, that could also explain why we would get a 10 per cent; let's say that's a market rate of return on aeronautical.

You get a 20 per cent overall because they're making it okay, and it's a 50 per cent return on carparking. That would be an equivalent explanation.

MR DAVIS: So in the - - -

COMMISSIONER KING: (Indistinct).

MR DAVIS: - - - (indistinct) yes. Yes.

COMMISSIONER KING: All right, one at a time.

DR WILLIAMS: I just want to be clear: are you saying that there are no complementarities on demand or supply, in costs or revenue, between - - -

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COMMISSIONER KING: I'm just asking an alternative way of understanding the differences of works presented. Yes, to make life very simple, let's imagine there were no externalities here, there aren't any complementarities, but you have no market power in aeronautical and you have a very significant amount of market power in car parking; that would also explain the difference in numbers.

In other words, one does not have to go to multisided markets to try and explain the difference in numbers between Frontier numbers and the PC numbers.

DR WILLIAMS: Well, one does, I think. I don't know what Warwick's answer to the question is, but one does. And for this reason: that what your question presupposes is that you can, in fact, separate-out, in a proper way, the costs of doing one function compared with the other.

COMMISSIONER KING: Well, what I'm trying to point out is that different degrees in competition on different sides of the market can explain the difference in your numbers and the PC's numbers. And in fact, if you got rid of the market altogether, it could be a complete explanation without having to go to complementarity.

So the claim that you've had is that you need to think about this in terms of overall market because it's a platform.

DR WILLIAMS: Yes.

COMMISSIONER KING: But actually, if you had different levels of competition on different sides of the platform, that would also explain the difference in your numbers, to our numbers.

MS WILSON: I mean, it would. But if we extended that from the sort of hypothetical question to saying, well, where is the actual difference, it would actually imply that you have no competition in the car parking side because there's high profits in that area, which is sort of contrary to what a lot of the PC report describes, in that there's a presumption of competition in some of those other services that an airport provides.

And, that you would have to have lots of competition on the aeronautical side, which is actually quite hard to describe why that would be, in the context of an airport.

COMMISSIONER KING: But it would be consistent, for example, if there was significant bargaining power or countervailing power from the

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airlines, so that the airports, whilst being in a situation of market power, were unable to exploit that market power on the aeronautical side because of that bargaining power. So, that would be consistent with the two sets of numbers.

DR WILLIAMS: Yes, it would be.

MS WILSON: Yes, it would. It wouldn't hamper the answer; assessing it on a whole of airport basis would still get you the right answer.

COMMISSIONER LINDWALL: But the question that, say, A4ANZ said, is that we should have a negotiate/arbitrate framework because of the profitability numbers that you've postulated. Surely, you could take from what Stephen has just said that if the aeronautical prices are actually lower than they would be because of the nature of the market, and the car parking, et cetera, should be lower because they're too high, then you should regulate the car parking directly and not have negotiate/arbitrate for the aeronautical services, which are actually under-priced, if anything.

DR WILLIAMS: No, because the question presupposes that you can assess the profitability of the airport independently of the profitability of the other sources of revenue from the platform.

COMMISSIONER LINDWALL: Well, I hear that.

DR WILLIAMS: Yes.

COMMISSIONER LINDWALL: But once you've assessed that, then you have to decide what type of regulatory structure is most efficient for that, and you might have different structures for different parts of the airport.

DR WILLIAMS: Indeed, but I think they're two quite separate issues if we come to regulation: one is what would be an optimal arrangement of the structure of prices? Another is what would be an optimal level of these prices? So it seems that any consideration of what would be an optimal regulatory or legal structure should think of these questions quite separately.

So, it would be possible - and this may not be at all what A4ANZ is advocating, so please don't attribute the views to A4ANZ - but it would be possible, for example, to have an aggregate revenue cap on what the airports are allowed to get, and let them decide how they structure their prices.

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COMMISSIONER KING: Can I come back? Because negotiate/arbitrate has been put to us as being a preferable approach. One of the questions we raised earlier on today actually related to the sort of externalities you were talking about, although looking at externalities between airlines in things like common user facilities. But a similar situation would hold in the externalities you're talking about, between carparks, retail, aeronautical and non-aeronautical.

Let's imagine that one of the domestic airlines brought a dispute before the arbitrator, with a particular airport; that arbitrator would need to think about the consequences of any price decision that arbitrator made, not just on the other aeronautical services, but also the consequences on the non-aeronautical services as well.

DR WILLIAMS: But this is presupposing that the arbitrator's job is to resolve disputes about prices for particular services. Now, I'm not sure that that is the optimal solution, I have to say.

COMMISSIONER KING: I'm not sure it's even feasible, if it's a two-sided market.

DR WILLIAMS: Exactly. That's why, in my opinion, it would be much more sensible for the arbitrator to decide, or somebody to decide, on an aggregate revenue cap, rather than to decide anything about a particular price or the structure of particular prices.

COMMISSIONER KING: So an aggregate revenue cap would require that there's a regulated rate of return - - -

DR WILLIAMS: Yes.

COMMISSIONER KING: - - - in there, so the airport would face a regulated rate of return under that sort of approach?

DR WILLIAMS: Well, if there were disputes, and undoubtedly there are likely to be disputes. So probably, it would have to face a regulated rate of return.

COMMISSIONER KING: So, we know from regulation in other areas that that can cause issues for airports where they may make investments and then seek to get a return on those investments from their customers; they then go to arbitration and the arbiter may say, "Well, that wasn't appropriate investment, or that was too big," or whatever.

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Under a revenue cap, would you see the arbiter having that role in, you know, ex-post, saying, "No, that was gold-plating. You were just trying to push up your asset base so that I'd set a higher price." I mean, would that be a role for the arbiter?

DR WILLIAMS: I think it would, yes.

COMMISSIONER KING: Okay. So in that situation again, we know from other areas of regulation that that risk on infrastructure means that usually, the infrastructure companies go and seek ex-ante approval for their investments. So, would you see ex-ante approval for investments as probably being a relevant part of the sort of method you're approaching?

DR WILLIAMS: Yes. Well, I should say, this is not something that we've written on.

COMMISSIONER KING: No, no, that's fine. I'm just - - -

DR WILLIAMS: But just talking off the top of my head - - -

COMMISSIONER KING: - - - exploring (indistinct) yes.

DR WILLIAMS: - - - yes, I think so, yes.

COMMISSIONER KING: Okay.

DR WILLIAMS: Just as it does in other regulatory models, yes.

MS WILSON: In a sense, I think Phil is pointing out the fact that you can give an arbiter a broader role than just determining on the specific matters at hand. But there's nothing stopping a negotiate/arbitrate process including that within it; I mean, there are plenty of negotiate/arbitrate arrangements that include an overlay. I mean, in a sense, Part IIIA does that as well: you come with a particular access dispute. But the ACCC can determine on far and wide matters. There's no reason any negotiate/arbitrate regime can't incorporate some aspect of you know - - -

COMMISSIONER KING: And the sort of things that Philip's been talking about?

MS WILSON: Yes, the sort of things that Philip's been talking about. I think you're presupposing a lot, that investment disputes will happen and they'll happen frequently.

DR WILLIAMS: Well, that might happen - - -

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MS WILSON: Which is not necessarily - - -

COMMISSIONER KING: It need not be frequent, but if I'm going to sink a couple of hundred million dollars into an airport infrastructure, I might like to know that the arbitrator isn't going to come along later on and say, "Well, sorry, that wasn't appropriate investment. You can't get a return on it."

MS WILSON: No, indeed. But I think there's an aspect to which you can overstate the significance of the problem, which is that by and large, if you're talking about specific investments at specific airports where airlines might not be that interested in making certain investments, it's going to be on certain aspects, not on the investment itself, because - - -

COMMISSIONER KING: Such as terminals?

DR WILLIAMS: Or the runways. I mean, there's - - -

MS WILSON: No, I would argue it might be on the design of the terminal, as opposed to whether or not to have the terminal.

DR WILLIAMS: Well, I'm not so sure about that.

MS WILSON: Because in a sense, airlines have an interest in having facilities for their passengers, in much the same way as the airport.

COMMISSIONER LINDWALL: Surely, you can use long-term contracts?

MS WILSON: Yes, I mean, that's what long-term contracts are here for.

COMMISSIONER KING: Were you here when Adelaide Airport was discussing its issues with terminal investment?

MS WILSON: No, no, but you could - - -

COMMISSIONER KING: Well, I'll let you read the transcript. But I think, if you had been here, I would've asked you questions.

COMMISSIONER LINDWALL: Well, I mean, they're the same type of issues. I mean, I would've heard it a number of times through this inquiry of hold-ups on runways and other major bits of infrastructure.

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I mean, Frontier in the UK did a study for Heathrow which said that the congestion at Heathrow produced rents - they went to airlines. So one could understand that airlines might rationally try to reduce - especially incumbent airlines - reduce investment to encourage the congestion, because they're going to earn rent themselves.

DR WILLIAMS: Airlines?

COMMISSIONER LINDWALL: Airlines, yes.

MS WILSON: Just to be - - -

DR WILLIAMS: It's not clear to me why an airline would benefit from congestion at the airport.

COMMISSIONER LINDWALL: Well, that Frontier study in the UK showed that congestion - - -

MS WILSON: They - - -

COMMISSIONER KING: I can give you a simple example: consider Sydney; Sydney has slots. Let's imagine there's an investment that would increase the capacity and increase the number of slots at Sydney Airport, and that those slots would be allocated to new entrants, as occurred post-Ansett collapse. I assume you would agree that incumbent airlines would prefer not to have more competition and would like that investment not to go ahead.

DR WILLIAMS: I understand. I think it would – I think it is important that any arbitrator or regulator have some overriding public interest concern. I definitely agree with that, and I can understand that it may be in the interests of the airlines or indeed the interests of the airports to act and perhaps even jointly contrary to the public interest. So I accept that, I agree with that.

COMMISSIONER KING: I'm just a bit wary of time because we had half hour slots this afternoon. Can I just understand because pass through was a key element of your work and the degree of pass through to the customers. There are, of course, too, you know, if you like, text book approaches to thinking about prices and pass through. On one side you have a single price setting, airport setting, landing charges to a single price setting airline, and then you get pass through according to the elasticity of demand and the percentage of the input and so on. So the sort of analysis that appears that Frontier undertook.

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Alternatively, you have a downstream firm that is able to engage in price discrimination. Let's for the sake of argument assume it's (indistinct) if not perfect price discrimination, in which case you would get a very different answer in terms of pass through of any increase in an upstream uniform price. In fact, in that situation there would be some change at the margin, but basically no change and no pass through of that cost for any passengers who continue to fly after that change had been made. I was wondering why you choose the first approach where you're essentially taking little, if any, price discrimination, rather than the second approach which assumes significant price discrimination by airlines, given that what appears to occur in practice is significant price discrimination by airlines.

MS WILSON: I can answer that question. I think I'd probably start by saying in some respects that analysis and evaluation of regulatory remedies has been a bit misunderstood and misrepresented, in the context that most of that report was actually about talking about whether you could get reforms that were cost effective, i.e. not looking at broader connectivity benefits. If you could in some way short circuit extensive and extended time unlimited negotiation processes, what would be the avoided cost of that and therefore would the reform be beneficial on a purely cost basis. So that was the main part and first part of the report.

COMMISSIONER LINDWALL: On the assumption that the outcome was identical in the short-circuited negotiation versus the traditional one?

MS WILSON: Indeed, - - -

COMMISSIONER LINDWALL: Which I don't think is a reasonable assumption.

MS WILSON: Well, you could say it could either way, but it was – but for the purposes of highlighting the fact that the current negotiation process is not costless. So then the second part was on, are there broader benefits that have thus far been largely ignored primarily I presume because they are complicated to assess which, as it turns out they are complicated, and they do require a lot of assumptions and they do introduce an element of uncertainty when you do it. So we presented that work quite separately to say, "Here are some benefits that come out as quite significant" you know, "up to – we're a bit uncertain about them, but they certainly – there are some wider benefits that probably need to be considered".

So on those wider benefits, what we were focused on was showing whether there would be connectivity impacts. In other words, would more routes be offered than are currently offered by virtue of a presumed fall in aeronautical charges, and I should say, we presumed all of the airports'

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charges would drop by a percentage, we didn't, sort of, take the non-aero profits and jam into aeronautical, that's not what we did. We reduced all of them evenly, and said, "Would that lead to more connectivity", and that was our focus.

So, sort of, in the context of that, thinking about cost pass through is actually a little bit of a distraction, because from an airline's perspective you can either have a reduction in aeronautical charges, that is cost, that is passed through to consumers that will result in lower airfares, that would lead to greater demand and therefore routes that were more or less marginal before, would then tip over into being routes that become profitable and therefore get offered. So that's one approach, assuming 100 per cent costs pass through which is what we did because it was largely a slim (indistinct) process in order to make the estimation.

The other is if they're not passed through what happens to them? In a sense it still makes from the airlines' perspective, it still makes those routes more profitable because it reduces their costs on those routes, which makes more routes tip into being less marginal or profitable, and so you get the same connectivity impacts essentially under either assumption. So the reason we adopted 100 per cent cost pass through, not identical but similar, was actually to – in order to actually make the estimation process.

COMMISSIONER LINDWALL: So did you – given that you made what seems to be a fairly important assumption but 100 per cent pass through.

MS WILSON: Yes.

COMMISSIONER LINDWALL: Did you do the analysis, an alternative of say perfect price discrimination and zero pass through to the customer so that we can see what the importance of price discrimination actually is to the modelling? And I don't want to try and guess whether it pushes one way or the other. It's just I would have thought it's important.

DR WILLIAMS: It is pretty easy to see, isn't it? If you think of say third-degree price discrimination, the answer is going to be about 50 per cent pass through. If you raise marginal costs for all the different services that you're providing – I know it depends on the slopes of the demand curve, but roughly you'll get about 50 per cent.

COMMISSIONER LINDWALL: Sorry, but to come back to Anna's bit about connectivity, so let's say what we're really worried about is what new services are going to be offered.

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DR WILLIAMS: Sure.

MS WILSON: Yes.

COMMISSIONER LINDWALL: That's not a pass through question, but the result will presumably still depend on what pass through has been assumed. It is purely – and you know, I'm not putting an argument that the airlines price discriminate or don't price discriminate. I don't think that's relevant, but I do think it is relevant just to make – it is a sensible test of your modelling if I can put it that way.

MS WILSON: You can put it that way. I mean, we were essentially time limited by your processes so no, is the short answer, but - - -

COMMISSIONER LINDWALL: We're time limited by the Government.

MS WILSON: Exactly. I mean, we were – our purpose was largely to say, "Were there benefits, could they be sizeable?" And I think the answer is yes, there are benefits and yes, they could be sizeable. But again, I come back to the fact that the costs, the reduced costs would have been passed through to an airline. They would definitely have gone through. So even if you took a 50 per cent pass through, you're still not accounting for those reductions in cost that an airline now has on some of its routes, which may lead it to increase its service frequency or increase the number of routes it offers. So by default through either route, you get a connectivity effect.

COMMISSIONER LINDWALL: Except if it also led to less investment and more congestion and higher fares.

MS WILSON: Again.

COMMISSIONER LINDWALL: We should touch on countervailing power - - -

COMMISSIONER KING: Yes, so just touch on countervailing - because it comes out of – you've done a report for Qantas and in there you have said, "We have indicated that assessment of countervailing power requires a case by a case assessment of each airline's position at each airport. Undertaking such an assessment would be difficult". So that's on p. 21 of Appendix 1. Should we read that as basically saying look, it just isn't practical to assess whether airlines have countervailing power in Australian airports. We're just trying to understand what sentence means.

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MS WILSON: I think it would be probably be more or less saying to determine that there is countervailing power at Australian airports as a generality would be challenging in the sense that you would actually need to assess it more rigorously at each airport.

COMMISSIONER LINDWALL: So if a PC had looked at, for example, Melbourne airport and looked at countervailing power and looked at Sydney power and countervailing power and looked at Adelaide airport – hang on I'll do more than one – Perth, and so on, if that's how the PC had done its analysis, then that would meet your requirements?

MS WILSON: Well, I guess that would be more rigorous, yes.

MR DAVIS: Well, I think perhaps what grated in our view in the report was just there was, you know, a selection of examples that seemed to have fairly limited, let's say broad applicability by picking on fairly small airports and you know, not major airlines. That was, in some sense – you know what I'm referring to.

COMMISSIONER LINDWALL: Yes, of course. Presume Rex and King Island.

MR DAVIS: That just didn't seem to be, you know, able to extrapolate that - - -

COMMISSIONER LINDWALL: I don't think we were trying to extrapolate that. I mean, for example, the newspaper said today that, if I'm not mistaken, that Qantas is withdrawing its planned route from Perth to Paris until Perth settles the dispute with Qantas. One could argue that's an exercise of countervailing power surely.

MS WILSON: One could also argue that the price has now go to the point where it makes that (indistinct).

COMMISSIONER LINDWALL: Well, has Perth reduced its prices as a result of that?

MS WILSON: That's the question.

MR DAVIS: Isn't that the question?

COMMISSIONER LINDWALL: It said it had. So anyway, - - -

MR DAVIS: I mean, that's the evidentiary point.

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COMMISSIONER LINDWALL: Of course. Thank you very much for coming to see us. Unfortunately we have run out of time. We've got to go and speak to Smithson and planning.

MR DAVIS: Thank you very much.

COMMISSIONER LINDWALL: So if I could invite Neil Smithson. He's on, that's right, the video. Good afternoon Neil, how are you.

MR SMITHSON: I'm very well.

COMMISSIONER LINDWALL: Would you like to give an introduction and a bit of a speech, or discussion?

MR SMITHSON: Yes, by all means. I'm assuming that Kenneth Baxter and Stephen King are both there with you?

COMMISSIONER LINDWALL: Stephen's here, yes. Stephen and Paul.

MR SMITHSON: Stephen and Paul, no worries, not Kenneth. Okay, my submission, and thank you for the opportunity to provide one, is probably a little bit different to most other people's. I'll just confirm, there's the actual covering submission which was published on the website, and then there were several attachments. One was a federal cabinet briefing statement, the other was a state cabinet briefing statement, and there were also two letters supporting, or otherwise (indistinct) from Dr Martin Parkinson and also Dr Peter Shergold, as former Secretaries of the Department of Prime Minister and Cabinet.

COMMISSIONER LINDWALL: Yes, I think we did receive (indistinct). We have received them, yes.

MR SMITHSON: Okay, that's fine.

COMMISSIONER LINDWALL: I think - no, go on.

MR SMITHSON: Basically, Smithson planning's core business is strategic regional development. Over my 35 year career, I've had a bit of a relationship with airports, and consequently, when I relocated from the eastern states back to Western Australia in 1997, I wrote a strategic regional plan for Albany and the Great Southern region - one of the core components thereof, was the establishment of a Albany Port Corporation. So, it wasn't just about airports. It was looking after the airports, and it was also looking after a ring road which was proposed to be a toll route.

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So that goes back to 1997, hence the two letters from the two DPM&C secretaries over that last 22 years.

The Commonwealth has consistently maintained the position that the things that we were trying to address were really the area of responsibility of state and regional governance and not the Commonwealth government. Yet here we are, today, 22 years on, and the Commonwealth has certainly embraced the Anzac Centenary commemorations, which were a huge success, but also in the next ten years, we'll have to negotiate the bicentennial celebrations for Western Australia, in which Albany, Fremantle, and Perth all play a significant part.

That was the - the gist of the 30 year plan, if you like, that it is actually a plan for strategic regional development in Australia, and not just Albany and the Great Southern, and consequently the relationship between public-private sector partnerships and airports, and a range of other facilities, intermix between local and regional and state and federal politics, and it all starts to get extremely interesting.

Anyway, along the way, my company was acting on behalf of a couple of international hospitality and tourism groups, and consequently, when I put together the plan for an Albany International Airport, embracing direct flights overseas, and tourism opportunities, one of the groups I briefed to along the way was the West Australian Airport Corporation, now Perth Airport.

At that time, I was of the opinion that their core business was investment in aviation in Western Australia, particularly through Perth Airport. But there was really no reason why they shouldn't also take an interest in every other strategic, regional airport in Western Australia.

One of the key factors there was, you'll be aware, all airports have to have an alternate destination. When I wrote the plan, Perth's alternate destinations were Learmonth and Adelaide, which is an awful long way to travel if you have to divert an aircraft. Several years ago, the State Minister for Transport, then, basically selected Kalgoorlie as the new alternate destination, but that could have easilt have been Albany or Geraldton, as two airports closer to Perth.

That's history now, and basically the two hotel groups I was representing, Taj and Versace, they wanted to establish five star hotels and they had direct aspirations for airport links, from Albany, straight into Asia, hobbing through Singapore, Jakarta, Bangkok and Kuala Lumpur, but ultimately through to India and China, and using airlines associated there with - we found out we had a lot of commercial interest. There was

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another individual who was looking after Accor Asia Pacific, in terms of their hotel group, which was related to their proposal for the Albany waterfront development (and LandCorp). But we'd had discussions with Air New Zealand and Qantas, and all the rest.

What transpired over 22 years is just a huge melee of public policy, particularly on regional airport development, and it's regrettable, depressing, unfortunate - whatever you want to call it, but it hasn't actually happened, and when you look at airports as trade portals, there is both inherent risk, and reward to having one major airport, being Perth Airport, servicing all of Western Australia. There have been numerous calls by regional airports to provide international access, particularly those in the north of the state, and what you can see is the interplay between state and federal politics, and we've got a lot of things coming into that equation.

Relative to Albany, we started off with a regional service airline, Skywest, and they eventually threw in the towel, and the State sought to procure another service provider for RPT travel between Albany and Perth, and as it turned out, also Esperance and Perth. Basically Virgin won that contract, and it was conditional on being a sole operator. Qantas would have liked the contract as well, but their offer was also conditional on being a sole operator, and as things transpired, even with the benefit of the hugely successful Anzac Centenary official launch in Albany, we still don't have five star hotels in Albany, and we still don't have, what I would call a quality airline. They've actually gone backwards.

We now have the service provider Rex, and you know, good for them. They're - they're building their business, and traveling into Western Australia, one would argue with support from various groups, politically. But, you know, the service is what the service is. From my own perspective, I think strategic regional development is so important to the future of regional airport, and seaport for that matter, and what I did was provide a particular interesting alternative way to think about the future of development opportunities, and then to follow the whole evolution of the strategy. So, we're just sitting back and watching it. Quite literally today for example, the Prime Minister, Scott Morrison has made an announcement regarding infrastructure development, and one of those announcements pertained to the funding for the $172m Albany Ring Road, albeit not a toll route.

Future funding and construction of the ARR is conditional on Infrastructure Australia approval, but we shall see what we actually get from the elected Government - and we'll also see where that goes in the future.

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Relative to other things that I've included in my submission, you can see the RPT aviation criteria in the various different categories and the international aviation specifications of how far different planes can go. You'll notice that some planes are moving in and out of favour, as a function of age, profitability and route application, and of course the airport has to basically be able to cater in terms of what they provide in the airside, and also the landside facilities to match up with what their customers are looking for.

I could say that there are other entities, all along the way, that are looking at the growth and development of Australia's cities, and you guys are focusing on four particular ones, with the major airports in Australia, which is fair enough. But, there are a lot of other strategic, regional airports capable of much greater things, if they had what I call a fair and open playing field, both in your regulatory system, and also the state that they're applicable to. Basically, in the briefing notes, particularly in the federal cabinet briefing notes, you can see there the pictures of the airports opposed. They were opposed over the last 22 years, those names have changed.

Basically, we've gone through seven Prime Ministers now, and five Premiers, and I can assure you I kept them all briefed all the way along. So, it's like talking to a brick wall, is the way to put it, both in Perth and also in Canberra. The tyranny of regional politics and multiple political jurisdictions, so getting things done in regional centres and opening up all of Australia for opportunity was quite challenging in a regulatory condition.

Coming back to the scope that you guys are working on, your key point, does this new airport regulation benefit the community and remain fit for purpose – I'd argue, yes. I think that is the overall situation. With four big airports that are not systematically exercising their market power, I disagree with that statement. I can't say I completely agree with other ones, but for a short while, I managed Mildura's airport and was aware of our relationship, then, in Sydney and Melbourne and Adelaide. Mildura is an interesting location, but Perth has definitely acted in its own self-interest which is, you know, fair enough. It's an international airport, now, a big corporation but that comes back to whether you see the bigger picture or whether you won't put forward the bigger picture.

There's no reason for airports to be complacent; 100 per cent agree with that statement, particularly on the future of fuel supply. I think that's a major factor in terms of aircraft movements, particularly with our extensive network in Western Australia, FIFO destinations and carrying mandatory fuel loads and getting fuel to the remote location. It's not

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going to be the easier or cheaper and, especially for more remote locations but, of course, it's a highly sensitive aspect and whenever you have a failure in your aircraft, well, people look for the reasons why and fuel contamination is not an uncommon cause.

It is perceived and commonplace to resent the cost of car parking. But, you know, it's a monopoly situation and if you were going out to the airport, there's only a couple of ways of getting there and different airports are being addressed. You know, you've got trains coming to Tullamarine, you got trains going to Perth, you got the western airport in Sydney with trains going there. The biggest improvement, you've got a different government moved (indistinct) on the nation.

I don't have enough information in relation to the kind of planes operating in relation to jet fuel supply. I think a lot of people are very nervous about the future of jet fuel supply. In the context of Western Australia, the state government and Colin Barnett – four years ago I think it was – renegotiated the contract for the BP refinery and at that point in time a big picture decision had to be made whether or not that refinery would remain in place or close and they elected to give BP another 50 year term, I think. So it's there for a while, as long as they get the raw materials for it, will they be able to manufacture jet fuel and then they had to basically distribute the fuels around the State by land transport.

In relation to government funding for infrastructure and regional airport; yes, by all means, but going back to the Albany ring road there were a lot of discussions and I know it got first proposed in 2007. They've called in Infrastructure Australia and they've tried to generate the business case for the $172 million road, but at the end of the day, the prime minister unilaterally made the decision yesterday without promising the business case and so – yep, that's going to get funded. So historically sometimes (indistinct) straight over the top. And as far as the things that I wanted to say, that'll pretty much do it I reckon. We can have a discussion.

COMMISSIONER LINDWALL: Well, thank you, Neil. Can I ask about Albany Airport which I am looking at the map of it at the moment? The runway is 1.8 kilometres long and 30 metres wide for runway 3214. I would've thought if it needed to be an international, it'd be about 2.4 kilometres long. Is the council proposing to extend the runway?

MR SMITHSON: The area is part of the problem. First of all, you could ask whether the City of Albany actually has some of these – like, is there a licensed aerodrome manager on staff. But anyway, the City of Albany as I understand it, they're not proposing to do anything for the airport. It

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hasn't done since the day my proposal was submitted for the Albany International Airport in 1997.

Relative to the picture you're looking at, the black tarmac with the original runway which is 1800 metres long, they did a little bit of recent work and realistically you can't extend the current runway out past 2,100 metres.

COMMISSIONER LINDWALL: Yes.

MR SMITHSON: Which is why I designed a parallel runway and the parallel runway over there is to full international standards; 3 kilometres.

COMMISSIONER LINDWALL: I see (indistinct)

MR SMITHSON: Now, that can be done. What you can't pick up from that aerial photo is the topography and quite literally the land drops off at both ends with the existing black runway. I might add that the brown runway, the cross runway has now been sealed and so that is – both runways are currently sealed. But neither is long enough for international traffic.

COMMISSIONER LINDWALL: Of course not, no.

MR SMITHSON: The whole intention was to basically build a whole new international airport in Albany, and part of the argument there is that just like – you can fly into Cairns, you can travel down all through Queensland and fly out to Brisbane or from Sydney I can fly out of Melbourne, but invariably it's better to have an entry port and an egress port relative to international tourism and for Western Australia, you know, I can argue that the south west is the most interesting part and the most attractive part and the most entertaining part and be able to fly in and out.

In the earlier submission I made to the inquiry in relation to Antarctic Territories, and I don't think there's any doubt that Albany's very well place in the future for actual travel to Antarctic Territory both for tourism and scientific and/or geological exploration .

COMMISSIONER LINDWALL: Well, thank you very much, Neil. Did you have any questions, Stephen?

COMMISSIONER KING: Yes, I guess just, Neil, I mean a parallel runway; that's going to be pretty expensive. You had the original investors; so the hotel investors and you had airlines interested. I mean, you know, well, how much were they willing to I guess put up front to be

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able to do that big investment that you needed, to be able to get this vision going?

MR SMITHSON: Put it this way, okay? I costed the entire exercise to seaport relocation and airport expansion at about $3 billion. At that point in time, and every financial adviser I've spoken to since, has said that if that product, being the Albany International Airport, the ring road and control route and also the seaport relocation and upgrade was offered to the market place, it would be oversubscribed. I would see that airlines and hotels and various other people send stakeholders, along with anybody in the community that wants to buy a share in the investment but most interest would be generated by superannuation and infrastructure funds. I never saw a problem in terms of raising the finances to deliver the outcome.

COMMISSIONER KING: Yes.

MR SMITHSON: The problem – and I had this response, again, in 2014 when I briefed both the Chinese and the Japanese consulates in Perth and for that matter, going back to 2009, when I'd briefed the diplomatic missions in Canberra every one of them said basically, "This is fabulous. What's the problem?" and I said, "It's just culture." And realistically it's about regional city development and government wants to grow that part of Albany. However, there's an awful lot of people in Albany who like Albany just the way it is right now and they don't want to see it grow. It's also the politics of Perth relative to Western Australia and that's both apparent in the airport as well as the seaport and you can see the discussions that are currently taking place in terms of relocation of Fremantle seaport down to Kwinana and also the discussions that have been place for Perth Airport in terms of the parallel runway. That's been an extraordinarily large decision commercially with the board and Western Australia Airports Corporation to (indistinct) going little bits and pieces along the way and I wish we would go into a discussion just where we form a frontier. You know, Qantas will negotiate as well as (indistinct) Perth Airport an introduction of air travel between Perth and Paris.

So, you know, why not, but you know, anything's possible if you want to make it happen and, yes, that plan is a very doable plan. After recent discussions I've had with other groups in politics as it were is that this plan's for Albany, but also the port relocation plans for Fremantle, and airport and Perth's (indistinct) region, you know, they represent the two largest urban redevelopment projects in Western Australia and the planning industry and the redevelopment of vacant industrial land goes a

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long way to helping to fund that exercise and of course they'll create taxing opportunity in their own right.

COMMISSIONER LINDWALL: Well, Neil, thank you very much for talking with us today. I think Albany is a lovely part of the country and hope to visit you sometime.

MR SMITHSON: No worries.

COMMISSIONER LINDWALL: So appreciate you having a chat and giving us your ideas and good luck with the project in the future. I think that having sensible infrastructure policy is something that the PC has always proposed.

MR SMITHSON: Thank you very much, Paul, thank you for your time.

COMMISSIONER LINDWALL: Bye. Could I suggest a five minute break and then we will have Qantas - Qantas Jetstar actually.

SHORT ADJOURNMENT **[3.10 pm]**

RESUMED **[3.12 pm]**

MR DAL PRA: We'll kick off. So good afternoon Commissioners Lindwall and King. My name is Mark Dal Pra and I'm the chief financial officer for Jetstar, and I'm joined here today by my colleagues Alan McIntyre, who's the executive manager of commercial planning for Jetstar, Carly Povey, who's the head of commercial operations improvement, but importantly for today she's our lead negotiator with airports and has been doing that for the last three and a half years. Also joined by Nick Brodribb who is the head of legal, and Moksha Watts, head of sustainability and industry affairs in support of legal and policy matters that might be common to Jetstar and Qantas.

COMMISSIONER LINDWALL: Before you go on when you speak separately given there's five of you could you just say your name for the record so it doesn't get confused.

MR DAL PRA: That's loud enough, close enough to the microphone.

COMMISSIONER LINDWALL: Purely for the transcript.

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MR DAL PRA: Okay, thank you. So I'd like to make an opening statement and begin with a background on Jetstar. So Jetstar has revolutionised air travel in Australia since we launched in 2004. Since we launched we've built up our Australian domestic operations to carry 14 million passengers a year. Over that same period the total domestic market has grown by 24 million passengers, which means we contributed to 60 per cent of the growth in domestic air travel.

We have grown in demand in existing markets and stimulated travel to new destinations. Places like Gold Coast, Ballina, Launceston, Newcastle, Ayers Rock and the Whitsundays have seen phenomenal growth since Jetstar arrived on the scene. This growth in travel would not have occurred but for Jetstar's competitive pricing structure. This has led to air travel becoming more affordable and accessible for price sensitive Australians.

As a low cost carrier the very nature of Jetstar's business model is reliant on maintaining reasonable fixed and variable costs so that travellers can fly from Sydney to Melbourne for as low as $45, from Sydney to Ballina for $56, and Brisbane to Sydney for $79.

The Commissioner's report is deeply disappointing for LCCs or low cost carriers like Jetstar whose business model is highly reliant on airports setting fair and reasonable prices through transparent negotiations. Excessive airport costs can significantly constrain Jetstar's ability to offer lowest possible fares to passengers. Jetstar is looking at its airport charges increasing by an alarming 7 per cent, including CPI, between this year and next, while our other costs will likely grow by less than 2 per cent, and it's worth saying that has also been experienced over the last few years.

After fuel, which is a cost we obviously can't control, except by trying to find efficiencies to reduce fuel burn, airport charges are our next biggest cost, and they are growing quickly. It's neither sustainable nor fair for low cost carriers or our passengers to continue to absorb these excessive monopoly charges.

Sydney Airport on Tuesday stated that an airfare from Sydney to Singapore is now more affordable than ever, and that it can be as cheap as $350 on a low cost carrier. That is true, and low fares are not only available during periodic sale events. If you feel like it you can fly up to Sydney for $68 one way with us this weekend, and that's actually cheaper than parking your car at either of those airports.

Jetstar continues to work hard to deliver affordable travel for Australians by keeping a laser focus on all aspects of our cost base. However, it's

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wrong and deliberately misleading for airports to claim that they have in any way contributed to these low fares. In reality they've done the opposite.

Over the last 12 months almost two-thirds of Jetstar's airfares sold for less than $100. Australian monopoly airports have done nothing but increase the cost of delivering those fares. Australian monopoly airports earned 25 per cent more revenue per passenger in real terms than a decade ago. Australian monopoly airport margins are more than double that of their international peers.

Efforts by the Commission to dismiss concerns about monopoly prices as a fight for revenue share are also misguided. More competitive airport charges have facilitated lower fares and passenger growth, which has positive flow-on effects to aviation jobs and also to tourism economies. As an example of this in 2015 Jetstar and Ayers Rock Airport negotiated a new more competitive pricing strategy. This contributed to a 150 per cent increase in Jetstar passenger numbers to the airport in the space of a year, and we continue to add capacity. Over the last three and a half years we've grown about 20 per cent more capacity into Ayers Rock.

We would also caution the Commission from suggesting that this is an example of the flexibility of low cost carriers to switch airports. In the case of Ayers Rock we knew there was latent travel demand, but more competitive pricing was needed to unlock it. But that's not the case with the vast majority of our network. Australia is the most urbanised continent in the world with a population concentrated in a handful of cities. In the four years prior to September 2018 Jetstar changed at most about 2 per cent of its capacity in association with new routes and route exits in any given year, even in the face of increasing airport charges and monopolistic airport behaviour.

Claims that low cost carriers can credibly withdraw or threaten to withdraw services from airports as some sort of negotiation tactic are also wrong. You only have to look at the work Frontier Economics have done on the myth of countervailing power. One of the scenarios they considered was the impact of Qantas threatening to withdraw a Newcastle Brisbane service. They found that Qantas stood to lose up to eight times more than Newcastle Airport if it carried out that threat. That's what they call cutting off your nose to spite your face.

We would also like to address the frankly false claims made to the Commission this week by Canberra Airport. Yes, Jetstar was in discussions with Canberra Airport to commence a Melbourne Canberra service. The reason Jetstar has not been able to start a service to Canberra

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is because the airport is simply too expensive. Canberra's prices can be nearly three times the prices of other monopoly airports across the domestic network. The short term incentives they offered would have meant that Canberra Airport was only twice as expensive in the first year rising back up to three-fold by the third year. The economics simply did not work for us, especially when you consider that two-thirds of our fares as I said before sell for less than $100.

Claims by the Commission that airports like Canberra Airport do not exercise market power because of the presence of modal substitution are also erroneous. We gave it a red hot go. We actually started a coach there with Murray's Coaches about two years ago, and we only managed to sell 2.3 seats a month between Canberra and Sydney on those coaches. I'd now like to hand over to Nick Brodribb to speak briefly about arbitration.

MR BRODRIBB: Thanks, Mark. Nick Brodribb, I'm head of Legal across Qantas and Jetstar. The importance of arbitration for airport negotiations is driven by a simple fact: the airports are a monopoly and the airport owners, not surprisingly, expect to get a monopoly return from their assets. The airlines want to see fair and reasonable price but those two things are fundamentally opposed. There is usually a gap between that cannot be breached. The key reason for driving to arbitration as a final outcome where negotiations fail, is that both parties now know where the negotiation is going to (indistinct). And both players are now driving towards an outcome that can be understood because it's what's fair and reasonable as set out in the arbitration methodology.

Without that as the end point, neither party is going to be able to concede their position because they are fundamentally different and the monopoly return is fundamentally different to a fair and reasonable price. Now, if you look at the reasons that have put up, over many years, as to why arbitration is such a terrible idea and if you look at them with some degree of analysis, you see that they really are hollow. The first one is this concept of the floodgates. The floodgates will be opened and every man and his dog is going to run an arbitration case. Well, it's in no commercial party's interests to give up their rights to negotiate to an independent third party. That doesn't serve anyone's purpose.

But secondly, the largest and most valuable airport in Australia was open to free arbitration for everybody for five years and not a single case was decided by arbitration. So the floodgates were wide open and not a drop came through. The concept of delay, to be honest I find extraordinary. I have been negotiating airport agreements since 1998 and the amount of time that has been spent in negotiations is unbelievable. The idea that somehow going to an arbitration model would create delay is a nonsense

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because the delay is already there. I think made the Perth that it would be "too complex", that an arbitration wouldn't be able to fathom the complexity of the decision which suggests to me that fair and reasonable can't be ascertained, it's an ascertainable concept. But that to me seems to be like a bit of a nonsense particularly when Perth Airport has sought that the Supreme Court determine what a fair and reasonable price is.

And then in terms of efficiency, as the Commissioner's rightly pointed out this morning, how efficient is it to go to the Supreme Court that deals with rape, murder, kidnap and ask it to determine a specific a specialist economic decision when you have a pre-existing regime that allows that to occur, albeit very difficult to access. So given that all those reasons for objecting to arbitration seem hollow and without basis or evidence, the question that is left is, "Well, then why is this dogged resistance to arbitration?" and the simple answer is: because arbitration will deliver a fair and reasonable outcome, and that's it. And if the Commissioner were to legislate such that access to arbitration that gave rise, obviously failed negotiations, but gave rise to a fair and reasonable outcome.

If that change were made and we're wrong, then you'll end up with some delays, which we've already got, and you'll end up with some complexity, which we've already got, and you might end up with the opening of floodgates, but the evidence strongly supports and suggests that's not the case, but ultimately you will end up with a fair and reasonable price and if we're right, which all of the historical evidence suggests, then it will be negotiated much more quickly because everyone's working towards the "same" outcome. Nothing will ever go to arbitration and you'll also end up with a fair and reasonable price. So our concern at Jetstar, and at Qantas indeed, is what is the fear of a fair and reasonable price? Why is the Commission, and certainly the airports, so terrified of a fair and reasonable price?

There's a couple of things I just want to touch on as well. Perth made some comments which I think the Commissioner repeated on the Frontier session which is that Qantas was somehow using countervailing power to threaten to withdraw from the Perth-Paris route. So I just want to point out, we don't operate Perth-Paris route. But Perth has been vocal in its criticism of the Perth-London route saying its loss-making and has been terrible for the airport and it's the protracted dispute about price that is preventing Qantas from being able to explore each of the routes because how can we operate a route when we don't even know what the airport charges are?

COMMISSIONER KING: But I thought the (indistinct) said that they were stopping discussions about all Perth-Paris, so.

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MR BRODRIBB: Yes, as I said, how can we continue to negotiate a route with an airport that can't even tell us what the price is and make economic decisions about whether it's going to be economically viable, whether there'll be demand, whether it can operate; without that transparency it would seem like a foolish, highly imprudent decision for an airline to make particularly when the airport is taking it to the Supreme Court to try and determine what price it's going to charge.

And the second issue was that Perth made a comment that the security charges that it was now passing down to Qantas were actually acknowledging what Qantas had been incurring which is in fact correct. Qantas is paying about 5 per cent more than it was paying previously. But there's a dearth of information provided making it very difficult to understand how they cover the prices in the first place?

COMMISSIONER KING: Well, that's two different statements about the security costs so only could be (indistinct) I suppose, but is there anything else?

MR BRODRIBB: No, that's the end of it.

COMMISSIONER LINDWALL: Could I go back to Canberra since that (indistinct) statement first.

MR BRODRIBB: Yes.

COMMISSIONER LINDWALL: Canberra Airport has told us that, because of what we said in our report, there's an anti-competitive contract clause; they can't offer Jetstar a lower price which they otherwise want to do so Canberra Airport, and I'm just telling you what they told us, says that they would like to offer Jetstar a much lower price to allow you to fly into Canberra but they're unable to through their contractual condition.

MR BRODRIBB: We don't know what clauses Canberra's got in its contracts with other carriers. If it's got a provision that prevents it from offering Jetstar a lower price than it offers to one of its competitors, then the simple question would be, "Why doesn't it offer a competitor a lower price as well?"

COMMISSIONER LINDWALL: Well, I guess it wants to price discriminate, doesn't it.

COMMISSIONER KING: Just on that. Would Jetstar be in favour of a Productivity Commission recommendation that most favoured customer

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clauses, to the degree that they exist in its services agreements, be removed from those air services agreements on the basis that they're anti-competitive?

MR BRODRIBB: Yes, so it's an interesting question. The ACCC's looked at the so-called provisions in relation to an airport back in 2002 and found that they weren't unreasonable, that they made no finding in relation to it and brought no proceedings in relation to it, so.

COMMISSIONER LINDWALL: There had been more recent cases, for example, the US in The Apple e-books case. The decision there was made that the most favoured customer clauses were from (indistinct) competitor.

MR BRODRIBB: Yes, in a completely different set of factual circumstances. So in relation to a scenario where you have an airline operating over a terminal that's being asked to effectively fund the majority of the costs if a different terminal, then it's reasonable you would say to that airline, "Well, I'm not going to charge you anti-competitive prices". So the operation of terms like this (indistinct) simply says to an airport, "You can't competitively discriminate against this airline".

COMMISSIONER LINDWALL: "You can't offer terms and conditions to airline A given the clause is in airline B's contract, you cannot offer terms and conditions to airline A preferable to those to B without also offering this to airline B" which for practical purposes it would mean airline A doesn't get offered the terms and conditions.

MR BRODRIBB: No, I don't agree with at all. The principle is that if you want to offer lower fares to an airline, you ought to offer them to all airlines and if you want to offer them on a basis that they are available to anyone of those airlines, for example, if you start a new route you can have a cheaper price. When the incumbent carrier's already operating that route, only the new airline will get the benefit of that. That's not difficult to operate.

COMMISSIONER KING: Your view would be then that somehow all airlines should be facing exactly the same sort of prices from the airport. One airline shouldn't be getting lower prices - I mean I'm just trying to push where you're going because your position quite frankly surprises given that these clauses it's been put to us; these contract clauses work against Jetstar's interest so I'm really quite interested in understanding what you would want then in terms of the airports?

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MS WATTS: I think, Commissioner, as we discussed Tuesday, we don't have as NCC said, we don't have any – an objection to the removal of these clauses as long as they're coupled with overall reform to how the system operates now. And we also face clauses where we are prevented from accessing declaration which we provided two examples of.

COMMISSIONER KING: Which we've also said are anticompetitive and should be removed - - -

MS WATTS: Absolutely. So for these clauses – the removal of these clauses is not – we don't object to them, we would much rather see a fairer negotiate arbitrate system which will take any incentive to have most of these clauses.

COMMISSIONER LINDWALL: Steve Bracks from Cbus appeared earlier. I don't know if you saw him and he said, that you did introduce negotiate, arbitrate they would basically sell off that asset unless the return went up significantly to cope with the additional risk. He also said that all of the things, the assets they invest in have to have a social licence to operate and he would not accept or they would not accept excess profits because they would see that their long term investors that if you could take short term profits eventually there would be extra regulation and it would be counter-productive so they just want normal returns (indistinct) returns. That's what he clearly told us just an hour ago or so.

MR BRODRIBB: Sure. I can answer that in two very simple answers. The first one is, the airports bought – sorry, the airport companies bought the airports in CPI-X, they were regulated. So, they made the decision at that time to purchase the airports with their obligations to invest infrastructure at that time. I can guarantee or I can't guarantee you but I think it is absolutely certain that if one of the airports sought to divest itself of its investment in the airport infrastructure in scenarios where it was guaranteed a fair and reasonable return, there would be a queue of investors, both domestic and foreign, who would take that up in a heartbeat.

But the second question is, Steve Brack's comment, as you repeated it, suggests that the only way infrastructure in Australia can be supported by the private sector is if its allowed to gouge with monopoly returns and that - - -

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COMMISSIONER LINDWALL: Well he doesn't say that he said it certainly isn't monopolies - - -

MR BRODRIBB: So, if that's right, if what he's saying is correct, then why would he would be fearful of going to an arbitrator that would give you a fair and reasonable price. If Steve's position is, he wants a fair and reasonable price, why would he be so fearful of an arbitrator that guarantees you a fair and reasonable price?

COMMISSIONER LINDWALL: Well, I didn't ask him that question but I don't know, how would - - -

MR BRODRIBB: I'm sorry it - - -

COMMISSIONER KING: Well, can I put back to you, do you believe that moving to a negotiate arbitrate model, would not lead to any change in risk from the airports perspective?

MR BRODRIBB: A change in risk?

MS WATTS: What sort of risk?

COMMISSIONER KING: The risk that they face from an investment perspective in the sense that they will clearly have less control over their future pricing strategies and so on - - -

MS WATTS: We would - - -

MR BRODRIBB: They'd be guaranteed a fair and reasonable return. Guaranteed a fair and reasonable return.

COMMISSIONER LINDWALL: They're guaranteed not that at all. They're guaranteed that an arbitrator will reach a decision, whether it's fair and reasonable that's – no one can guarantee that. What is fair and reasonable?

MR BRODRIBB: Okay, well if your argument is there's no such thing as fair and reasonable - - -

COMMISSIONER LINDWALL: Well, fair and reasonable will be in a purely competitive market, I suppose would be the competitive price - - -

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COMMISSIONER KING: Or fair and reasonable will be whatever is written down in terms of the rules of the arbitrator to work out what is fair and reasonable, so I mean - - -

MS WATTS: But that sounds eminently sensible. Surely, that's something that can be written down in terms of the arbitration frameworks that allows the arbitrator to determine what might be – how to determine a fair and reasonable price. I mean - - -

COMMISSIONER KING: But the arbitrator would never know as much as you on one side and the airport on the other side, no matter how good the arbitrator is. They're not going to be in full possession of the knowledge that comes to commercial contracts that - - -

MS WATTS: But they will have – they will have power. I mean, this is where I suppose we're trying to say that there isn't a credible threat that airports face at the moment. So, the information, asymmetry that exists now, is what enables them to charge high prices, or there's a lack of transparency in how those prices are calculated. If that power imbalance were to be corrected by having the threat of going to an arbitrator, we would submit that the negotiation process would be more disciplined as a result. I mean, it might be helpful if Carly Povey is able to elaborate some examples of the unreasonable infrastructure that we have been asked to pay for over the past few years.

COMMISSIONER KING: Just before we do that, just back on the fair and reasonable. So, you heard – well I'm not sure if you heard earlier today but earlier today but A4ANZ, said that you could include, for example, consumer interest in there and that would be part of a fair and reasonable, I would've thought. So, let's say that an arbitrator said, "Well, yes Canberra", just to pick on them because you said they were charging three times what the other monopoly airports were charging.

So let's say Canberra was under this regime and the arbitrator said, "Well, yes we think Canberra Airports prices should be significantly dropped to all airlines, subject to those price drops being passed through to customers." Would Jetstar be happy with that sort of outcome, which is clearly fair and reasonable to the customers, gets to what you believe will be closer to a fair and reasonable price, but also would require Jetstar not to see those as their own profit but to pass them through.

MR DAL PRA: I guess the starting point, with Canberra we don't operate there today, so it'll be hard to say - - -

COMMISSIONER KING: No - - -

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MR DAL PRA: But in terms of answering that question, I mean, we are a low cost carrier. Our (indistinct) and our business model is about offering low fares to customers, so we have only grown those 15 million customers because we have continued to drop fares and find ways to make our business more efficient - - -

COMMISSIONER KING: That's not answering my question though, would you be happy to make a guarantee to an arbiter, that yes, we will accept the lower price on the condition that it is passed – try again, passed through in full to the final consumers. And being a low cost carrier - - -

MR DAL PRA: I'm not sure I'd know what that would mean in practice, because we're not operating it today and - - -

COMMISSIONER KING: It's across - - -

MS WATTS: Would that apply to all airlines, I mean it's a - - -

COMMISSIONER KING: It applies to all airlines – what I'm trying to get at is you said fair and reasonable - - -

MR DAL PRA: If you look at pricing - - -

COMMISSIONER KING: - - - and example, I'm just trying to work out will you abide by the arbiter's decision?

MR DAL PRA: It's very difficult to answer that specifically because pricing varies for a whole bunch of different reasons in different times of the year, different days of the week. Is it a daylight flight, there are many things that determine price of an airline. But if you look at the aggregate prices over time, we've seen prices drop since 2003, the year before we launched by 40 per cent. So, it is in our best interest to stimulate demand through low prices and that is how we operate.

COMMISSIONER LINDWALL: But going back to Stephen's point, if the reduction in price was $5 per passenger, because it will be a fixed amount, that would in theory would mean you'd be cutting all your fares, no matter the higher price or the lower price by $5 each, would you do that?

MR DAL PRA: The difficulty is we are suggesting arbitration in a monopoly market. And you're now suggesting a cost pass through in a competitive market. So the prices in that market are set entirely by competitive forces. Because if - - -

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COMMISSIONER KING: And based on cost price presumably so as cost come down those prices will come down. I mean if you're competitive it should be a complete no brainer for you, you should say, "Yes, that will occur."

MR DAL PRA: Well it may or it may not. The pricing of an airline is incredibly complex because it's built not just – it's not built on inputs, it's built on what the market will bear.

COMMISSIONER LINDWALL: Okay, so can I come back then to a question that I put to A4ANZ, which is negotiate arbitrate, the consumer isn't directly there, you could try and set up some sort of consumer body as the AER has tried to do, I'm not sure how effective that is. But any arbitration that is going to provide a benefit not just for the airlines and potentially the airports, it could be of benefit to them, but for the consumers would have to have a requirement of pass through of some or all of a price drop to the customers and it appears that Jetstar would not consider that would be a reasonable or enforceable decision by the arbiter.

MR DAL PRA: No, I think your premise is flawed.

MS WATTS: I think you're misunderstanding us. What we're saying is that, if that is a model that the Commission would stomach and would be willing to recommend we would be very happy to look at it as soon as there were some practical details to consider it. But you're providing us with a hypothetical which is far divorced from how any airport negotiation has worked. So were we to have that model to consider, absolutely we'd consider it.

MR BRODRIBB: And very importantly, that arbitration model that exists now which is unfortunately defended by an almost impenetrable declaration, it has public interest tests in it, and it has public interest considerations in it, that the arbiter must take into account. So, it's already there, this is not new, I'm surprised Steve Brack's isn't aware of it - - -

COMMISSIONER LINDWALL: The NCC in its submission – the NCC in its submission to us didn't agree that it was impenetrable burden, by the way. It said that it considered the declaration test was quite appropriate and reasonable.

MR BRODRIBB: Well, I mean we probably (indistinct) that as - I mean, clearly any structure of (indistinct) discussing with A4ANZ, it's what we have to decide if we're to change from our draft recommendation is that where you've got the status quo, as we have with some modifications, we

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have to be convinced that there's a net benefit to the community to choose something else. Now, the actual implementation of a negotiate-arbitrate, if that were to be the model, is critical to that because it's not very good to say it's an impractical thing. The Commission's been criticised in the past for proposing things that are not practical to recommend so you really have to know exactly how you would implement something like that and there are going to be costs and benefits, let's face it.

COMMISSIONER KING: And it is important to understand the standard economic approach to cost benefits says that shifting a dollar from airport shareholders to Qantas' shareholders is not a community benefit. At the end of the day it has to go back to the customers and I'm trying to work out how it gets there.

MS WATTS: Well, what we say - well, it's competition.

COMMISSIONER KING: If you're - - -

MR BRODRIBB: (Indistinct).

MR McINTYRE: If you're reducing the costs of the airport, that's exactly the opportunity, in this of Canberra which allow Jetstar to operate, would allow Jetstar to pass on the benefits to the customer and in the way that Jetstar managed to reduce fares to a customer by 40 per cent over the last ten years or whatever it is, so that is exactly the opportunity. We obviously had to price at a lower level because we are a low cost customer.

COMMISSIONER KING: Of course you do.

MR McINTYRE: So that is the opportunity, if Canberra were to do that, to bring lower fares to the customer.

COMMISSIONER LINDWALL: But that seems to be the argument that if Canberra were to reduce its price, then you would be to enter the market but that's not the same as passing on that to a customer. That just means that you're now operating where you weren't before.

MS WATTS: But doesn't that go to the - - -

MR McINTYRE: But if we were to enter the market, there would be a dilution anyway because we would be extra seats onto the market anyway but the more capacity into the market and we cannot, because we are a low-cost carrier, charge the same as other carriers anyway because of who we are. Therefore we, by entering the market, we would be de facto

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passing on lower fares to the customer both through who we are and the fact that you would have more seats in the market.

Exactly. It's happened on all the other markets we've entered into and (indistinct) really.

MR McINTYRE: I mean, just by track record really. It's a fact of economics; you've got more supply. But the issue there is that there isn't the supply there because we can't afford it because it's a such large proportion of that total airfare because we're a low-cost carrier.

COMMISSIONER KING: Just as a matter of interest; Tiger operates out of Canberra and have done so for a number of years. Any thoughts on why they can do it you can't?

MR McINTYRE: Well, we talked about I don't know what incentives they've been offered.

COMMISSIONER KING: That's fine if you don't know.

MR DAL PRA: Well, they've got (indistinct) clauses but they only operated for a while.

COMMISSIONER LINDWALL: But I mean, surely whatever the costs of Canberra Airport, theoretically Jetstar could operate and yet your price might just be a bit higher than it might be other airports?

MR DAL PRA: Well, there's a point though, a price point, where people choose not to travel and that's the issue. We stimulate markets because the price points are low and there would be people who would choose to take a holiday because they can now afford to take a family of four on holiday to the Gold Coast, or wherever it may be, because the price is low. And if the price was higher they might just say, "Look, I'm not going to do that. I'll drive down the road for holidays." So we do stimulate demand through those low fares.

COMMISSIONER LINDWALL: I don't think there's no doubt about that, it's perfectly true. So, did you want to go - - -

COMMISSIONER LINDWALL: Do you have any more to say - - -

COMMISSIONER KING : Just understanding how Jetstar does it for commercial negotiation with airports; does Jetstar negotiate independently with airports? Does Qantas handle the group's negotiations? Do Qantas and Jetstar as a group negotiate - just to understand what's happening here.

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COMMISSIONER LINDWALL: Yes.

MR DAL PRA: I'll let Carly - - -

MS POVEY: Hi there, Carly Povey. It really depends. It depends on factors, including whether there are commonalities in what we're negotiating again. So, for example, in Melbourne T4, we have our own terminal therefore that agreement sits separately to a common group agreement but we've actually found particularly in recent years is that as we've become an adult, not a starter airline shall we say, we have less significant growth opportunity particularly because of cost and we also have more commonality in the kind of discussions we're having with airports and over time we've actually started to negotiate as a group.

To be frank, it would be totally unsustainable for us to manage the length of protracted negotiations if we didn't work that way. I'm a team of three. Jetstar alone flies to 39 ports. On average negotiations take four years which talk to the challenge that we have with the framework at the moment and from our perspective it's an efficient way of working. It actually allows the airport to have one conversation with one team about the same airport as opposed to two teams about the same discussions. Where there are services that differ by Qantas and Jetstar, then then become separate services. So, for example, Jetstar doesn't need a lounge, Qantas does. Those things do get separated but whether are commonalities, we take the most efficient course to what is a highly inefficient process, to be frank.

COMMISSIONER LINDWALL: Well, they're complex negotiations I'll agree on that. What about the other types of differences between Jetstar and Qantas? I mean, I take it buses versus, you know, gates is not so important in some ports where there's sufficient gates and others it would be more important where there are insufficient gates. I mean, logically speaking the operating cost, I would imagine, of a bus is more than a gate because a gate, once it's invested, it's just there. If it's vacant, there's no operational - you don't have to get security people to take people around, and so on, on a bus.

MS POVEY: It's actually not as simple as just comparing them like that. For example, when an aircraft comes up to an airport and it's on what you would call a "contact stand", often it has an air-bridge connected to it which is additional infrastructure that drives with it cost. A low-cost airline such as Jetstar, with very skinny margins, focuses its business in high utilisation of aircraft and turning those aircraft within 30 minutes.

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COMMISSIONER LINDWALL: Yes, yes.

MS POVEY: So where we do that, is one example, is dual door boarding so that would actually mean that for us a more efficient process is to have stairs which means we don't need as much airport infrastructure.

COMMISSIONER LINDWALL: Yes, but it's quicker.

MS POVEY: But it allows us to drive that very productivity that we need to drive costs down.

MR DAL PRA: So you save on the aerobridges.

COMMISSIONER LINDWALL: Yes.

MR DAL PRA: So you don't need to pass on that cost and you get better utilisation of your aircraft.

COMMISSIONER LINDWALL: Yes. Well, obviously negotiate-arbitrate talks about price but in terms of other things that airports provide to you as Jetstar, I mean in terms of the quality of the service and how innovative they are and how they respond to your needs. Can you talk to that perhaps, and what can be done to improve that?

MS POVEY: Yes, so look I've worked in similar roles in low-cost airlines for 17 years now. I've been in this role with Jetstar for three and a half years. In my whole time in this role I have never seen an airport proactively talk to me about their service levels. I would struggle to give you an example of where they've looked at innovative ways to increase service levels; I would struggle to give you any evidence of them proactively showing me how they meet those services levels; and I would say that there's a significant need for us to think about how we drive more robust frameworks moving forward. Because from our perspective, if the two come together in the right way, it's actually about driving efficiencies. But right now I would say there's a significant challenge there with how one gets clear line of sight, even with significant persuasion, to understand exactly what service levels have been met and - - -

COMMISSIONER LINDWALL: Because Melbourne Airport this morning, if I'm not mistaken, told us about the little bridge thing that you go out to the terminal.

MR DAL PRA: Yes, T4 Jetstar.

MS POVEY: Yes, yes.

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COMMISSIONER LINDWALL: And how they now wished that they had built the walkway to, whatever they call them, - - -

MR DAL PRA: Travelators.

COMMISSIONER LINDWALL: Travelators, which they didn't have an agreement with Jetstar and so they didn't build it and now apparently passengers walk along a very long corridor, I've done it myself, it's a very long corridor and people think that it's annoying and - - -

MS POVEY: Let me explain to you why we have that extra walk time. The reason why the terminal was designed the way it was, was to enable a first of a kind multi-lane taxiway that was critical for high utilisation of aircrafts so it would allow Jetstar's aircraft and other aircrafts to push back onto the taxiway at the same time which actually means you can drive better efficiency of aircraft and one's not waiting effectively in a queue behind the other. That was the premise of us moving to T4; that was the premise of the design that included that long walkway. We've been in T4 nearly two and a half years. That multi-lane taxiway is still not in operation. So that's, from our perspective, a bigger issue.

COMMISSIONER LINDWALL: Okay, yes. Well, obviously. I mean, I can fully understand that you want to have the airport provide services, baggage handling and so on, very efficiently and that's what they should do.

MS POVEY: Yes.

COMMISSIONER KING: Were you here when we were having the discussion with BARA about potentially having some sort of - sorry, let me step back. It's been put by BARA and I think the AAA and someone else, who I can't remember off the top of my head at this time of day, that an approach that would be desirable for boilerplate parts of clauses is to have the airports, airlines and government representatives sit down together and try and work out sort of contract templates. We were discussing this morning about whether such an approach could be useful to start getting service standards and to get service standard measurement and appropriate penalties or incentives for not meeting them. I'm not sure if any of you were present for that discussion so it's a bit unfair then to ask what you think of that type of approach but I'm going to ask it anyway. What do you think of that type of approach?

MS POVEY: Let me start with saying as the person who has the pleasure of many of these negotiations with airports, we'd welcome some

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independent direction particularly on the inputs of frameworks such as the building block model and what is a fair and reasonable return? I've been in this role three and a half years and we've signed two airport contracts in three and a half years. I spend every day on airport negotiations. That's a sign of, for everybody, a rather inefficient and unproductive process so we'd welcome some independent direction. Whether that also leads to your point on important factors such as once you've reached agreement, how you then think about how you drive efficient service levels and how you enhance customer outcomes; absolutely, that would be something we'd welcome but the initial challenge we have is even getting to that stage.

We see significant issues with - you know, I think the only thing we do agree to agree on is that we're misaligned on our view as to what is fair and reasonable and so some direction that would allow us to get to the crux of the issue and actually start to talk about things, like service levels, would be welcomed from my perspective.

COMMISSIONER KING: Why do other airlines seemingly less problems? I mean, a lot of the airports have told us that they've settled, you know, 30-odd agreements with airlines and only one's outstanding.

MS POVEY: So the example, I think, was Perth which said that it had agreements with 23 or 24 airlines. They said that today. We're the only airline that operates in the terminal that's in dispute so there are now 23 airlines in the terminals that are not subject to negotiations. It's a bit of a fallacy for Perth to suggest that, it's a little cute.

COMMISSIONER KING: Well, the other airlines have terminal agreements because they don't have the Qantas terminal. I mean, it's not like the airlines that have reached agreements are operating out of some tin shed or something. They're - - -

MS POVEY: But they're not apples and apples is our point.

COMMISSIONER KING: No, there is a dispute between Qantas and Perth Airport which relates to the airport which relates to the terminals, and we understand that. I don't think it's quite fair to say that, "Well, you can ignore the fact they've reached agreements with all the other airlines, that they are irrelevant because they're operating out of a different terminal?"

MS POVEY: We would suggest, firstly, that that's where you're boilerplate terms may be worthy of investigation because in our experience where we hold out and have more - are able to drive any

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additional efficiency in price or service, you know, we can't tell you if that is then passed on to the other airlines so effectively in those cases it's Qantas or Jetstar that end up doing that heavy lifting which others may benefit from. We don't have transparency around that.

COMMISSIONER LINDWALL: But doesn't that mean that you have countervailing powers and still do the heavy lifting?

MS POVEY: It seems odd to - - -

COMMISSIONER LINDWALL: I mean, it sounds like a countervailing power to me.

COMMISSIONER KING: She can bargain for a better result than everybody else so they free ride on (indistinct) and they say, "(Indistinct cost us?"

MS POVEY: Well, I would submit that's not a great regulatory outcome either.

COMMISSIONER KING: Quite possibly not the question that Paul asked is, "Doesn't that show that you have some degree of bargaining power that's more than the other airlines?"

MS WATTS: Can I just - - -

MS POVEY: It's just that it takes us longer to negotiate because we'd be going more complex, that's all it suggests.

MS WATTS: And just to talk to that as well I think, you know, if you look at the fact that our airport costs are rising more than 7 per cent actually before CPI every year. It takes on average more than four years to reach agreement. And even in airports where we have significant market share, we have been wholly ineffective quite frankly at reaching agreement. They don't suggest countervailing power to me. They actually suggested seriously challenging the process. We just do not feel that, you know, there is power to even do by, you know, putting together as a group. It's a wholly substantive process (indistinct).

MS POVEY: And I think just to add to what you were discussing there around why other airlines may agree and Jetstar, in this example, may not. I can't talk to why they do agree but I can talk to why it takes so long for us to reach a negotiation and I'll give you some examples of the kind of challenges we have without some form of framework to find pathways through negotiation. We've seen examples where airports will try to pass

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on aeronautical costs or its aeronautical cost. They include everything from moving security facilities to enable retail growth when those security facilities don't need to move and $6m being passed on to Jetstar. That same airport was proposing a design for a new terminal with a koala sanctuary in it and was adamant that it was not gold plating.

MS WATTS: And that it was aeronautical.

MS POVEY: Exactly. We've seen examples from airports where they have asked us to pay for CCTV for the security and car parks. We have seen multiple examples where they have asked us to pay double (indistinct) escalations. We have seen many examples where they have said that the whole reason that they are needing to invest in infrastructure is to drive aeronautical growth and to remove congestion in terminals. They are proposing to pass through 90 per cent of costs to airlines and 74 per cent growth in retail is part of that. So we just see so many different examples, with more time that we could talk to in more detail, while we really struggle to even see transparency inputs, never mind get to the stage where we can agree a fair and reasonable outcome.

COMMISSIONER LINDWALL: Well what about on the other side. I've heard testimonies, say from Perth, that they upgraded their ILS to Cat 3 and Qantas and Jetstar don't want to pay for that and don't pay for it and yet still land planes during conditions that require Cat 3 ILS landing.

MS POVEY: No, no - - -

COMMISSIONER LINDWALL: That's what they did say to me. So I mean, you know, you're saying one thing and the other side says the other thing.

MS WATTS: Indicates a system that needs reform.

COMMISSIONER LINDWALL: Not necessarily, not necessarily. It might but it may not.

COMMISSIONER KING: Can I ask whether Jetstar or Qantas, or the group, whether you think there should be a single till approach or the current dual till approach or a hybrid till similar to a single till; but in other words, should pricing relating to aeronautical be based on the return and the operations so that the entire airport, including car parking and so, all should, for pricing for aeronautical, just be based on aeronautical?

MS POVEY: We believe that single and hybrid till methods are worthy of additional consideration. We've provided some analysis in our

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submission on what would be the relevant merits of both of those systems. We don't have a definitive, a solution, to present to you but we do believe that they're worthy of further investigation by the Commission.

COMMISSIONER KING: Even though single till, by implication, means that yes, Qantas might be asked to or Jetstar might be asked through the aeronautical charges to pay for additions to car parks because that's where the airline has or the airport has determined that they will get the return rather than getting it on some other part of the single till. A single till means you are operating overall and you take the money from where you can so exactly the situation you said was unfair, could be possible under a single till.

MS POVEY: Well, it currently occurs under the dual till so we've been asked to pay for koala sanctuaries et cetera under the current system. The issue we have now is that there is no transparency of what airports regard as aeronautical infrastructure, there's very little transparency. We're not able to tell if there's retail added into that aeronautical price now. We do absolutely acknowledge that there would be some risks around a pure single till methodology, obviously that's why some jurisdictions have considered a hybrid till where you mitigate the risk to both airport and airline. Again, we would say that those are all worthy of consideration. Certainly, in our experience, there are a number of non-aeronautical assets or non-aeronautical services that reliant on passenger traffic which is why it's worthy of further consideration.

COMMISSIONER LINDWALL: Jetstar and other low-cost carriers; are they disproportionately or equally affected by the 15 minute of 80 movements an hour rolling cap at Sydney airport?

MS WATTS: Yes, it's a regime that we're all affected by, yes.

COMMISSIONER LINDWALL: But do you think LCCs are more affected than full cost carriers?

MR DAL PRA: Alan, this would be more a one for you really?

MR McINTYRE: I'm trying to think whether we're disproportionate. In fact, I think we're probably - - -

MS WATTS: Not materially obviously.

MR McINTYRE: I think we're kind of all affected by this. Sorry, what's behind your question?

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COMMISSIONER LINDWALL: I don't know, you've got that very tight - - -

MR McINTYRE: I agree absolutely.

COMMISSIONER LINDWALL: - - - margins, therefore fuel would be more important and timing - - -

MR McINTYRE: Congestion – I mean to go back to Carly's point, obviously anything that slows us down and doesn't allow us a 30 minute turn, but that's not specifically in relation to the rolling cap, it's a slightly different issue, so I think in terms of the - - -

COMMISSIONER LINDWALL: I suppose on the other hand - - -

MR McINTYRE: It's not regime, it's kind of affected together, I think.

COMMISSIONER LINDWALL: I suppose that's right and I mean, the person who pays the full price business class ticket on Qantas is going to be probably annoyed at being waiting five minutes more than someone who is paying $58 - - -

MR McINTYRE: I think everybody gets annoyed when - - -

MS WATTS: They definitely have loud voices

MR McINTYRE: It doesn't work that because you paid more you shout less or more.

COMMISSIONER LINDWALL: That's probably true. Do you have any more questions or – any other final points you want to make? Anything else you'd like to say because – anything we have missed?

MS WATTS: I think the only thing we would say is that our – just in terms of the price pass through question just as a concluding point. The record of – certainly Jetstar's record has been that wherever costs have lowered, those prices – those savings have been passed through to customers either through fare savings or through additional routes and additional seats, so that is certainly a track record that it has held for 14 years and the benefits that come through some of the reforms that A4ANZ and BARA have been advocating and (indistinct), we are absolutely confident they would have similar benefits for passengers. That's the record that Jetstar has stood on and it is certainly something - - -

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MR DAL PRA: I think it would be true of low cost carriers around the world.

MS WATTS: Absolutely.

MR DAL PRA: We are part of that and that's how the business model works.

MS WATTS: Yes.

MR DAL PRA: We stimulate demand, lower the costs, (indistinct) scales and you just continue to get that virtuous circle of reducing costs, passing it onto consumers, growing, it is a virtuous circle.

COMMISSIONER LINDWALL: Look, I applaud Jetstar, done a fantastic job. I should ask you finally, how do you find access to foreign airports that Jetstar services?

MR McINTYRE: How do you mean, how do we find them?

COMMISSIONER LINDWALL: I mean the cost, the access terms, the types of services you receive - - -

MR McINTYRE: It varies a lot. I mean we are seeing some concerning indications. Price increasing which is affecting us not well. Certain parts of Asia at the moment, and it's having – it is not having a good effect because for the very reason, as we've said, we run – we stimulate demand and airport charges are a considerable part of our costs. I mean, it is 20, sometimes more percent, of our costs, of the airport costs and so it means that we can't stimulate as we perhaps used to.

COMMISSIONER LINDWALL: And they're actually rises in airport charges rather than exchange rate effects or anything - - -

MR McINTYRE: Yes, rises in airport charges and material.

COMMISSIONER LINDWALL: All right. Well, I think - - -

MR McINTYRE: Thank you very much.

MR DAL PRA: Thank.

COMMISSIONER LINDWALL: An opening statement would be fantastic. Could I just have five seconds?

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MR ZANARINI: For the purpose of the transcript ,, Matteo Zanarini, Area Manager south-west Pacific representing the International Air Transport Association based out of Sydney.

MR RAFFO: Good afternoon. My name is Cesar Raffo. I am head of Airport Charges in IATA.

MR ZANARINI: So first, IATA appreciates the opportunity given to participate at this hearing, as well as hopefully provide commentary and clarifications as required, for consideration with the inquiry on the Economic Regulation of Airports and its draft report.

The International Airport Transport Association, IATA, is a trade association for the world airlines. We represent 290 airlines globally or 82 per cent of global air traffic. IATA member airlines include many that operate flights to Australia including Australian carriers Qantas and Virgin Australia. IATA supports many areas of aviation activity that helps formulate industry policy on critical aviation issues with the objective to drive safe secure and a sustainable environment for aviation to flourish.

Our views for consideration in our submission are from an international perspective based on global best practises which are relevant and applicable also for Australia. In the draft report, whilst the PC rightly identifies that the monitored airports possess market power, IATA is surprised and concerned regarding the PC's draft conclusion that these airports have not systematically exercised market power and therefore the existing light-handed regulatory framework remains sufficient.

Given that the purpose of this inquiry is to determine the effectiveness of the economic regulation of services provided by airport to airlines, passengers and the people and businesses that access the terminal precinct, our response respectfully encourages further assessment and for a balanced accord of the evidence presented by our members as well as A4ANZ and BARA.

Overall, we consider this matter too important for airlines, passengers, third party operators and airports, as well as for jobs, tourism and economic development within Australia. Our latest response to the draft report does not present again the details already provided in previous submissions, as we rely on the public hearing and our submissions to encourage the Productivity Commission to revisit the areas of concern or explain why they are not being considered.

Rather we have focused on areas where there should be some revision to the assessment methodology in order for the PC to seriously consider the

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need for an efficient and effective dispute resolution system as a meaningful and credible regulatory threat notably in the areas of additional scrutiny on the costs of the monitored airports, particularly capital expenditure efficiency and return on capital, and reassess its conclusion on airports exercising their market power.

A reassessment on whether scarcity rents exist based on the information provided in our submission, and also reconsider the much needed creation of guidelines on the minimum information to be provided at consultations. The PC is urged to investigate such implementations in other regions and to determine independent fact-based conclusions. Based on our experience across the globe, our view is that the progressive improvement would not be interventionist, nor lead to perverse incentives not to reach agreement during the consultations.

With me today, Cesar, has been, as he said, is responsible for airport charges and together with my colleagues, has been instrumental in formulating our submission. Our submission has three components; economic regulation of airports, Sydney regional access scheme and slots, and jet fuel supply. Cesar is here to help answer all your queries and requests for clarification on the economic regulation of airports.

Unfortunately, we were not able to also bring our subject matter experts all the way from Geneva as Cesar has come all this way - - -

MR RAFFO: I drew the short straw.

MR ZANARINI: **- - -** and he is holding up very well, I might say.

COMMISSIONER LINDWALL: When did you arrive?

MR RAFFO: The day before yesterday. I did the last two nights have been

COMMISSIONER LINDWALL: So your brain is telling you it is two in the morning - - -

MR RAFFO: I know, it's like – I woke up at 3 am and then it was impossible to sleep and so my apologies - - -

MR ZANARINI: So in short, I give Cesar the onus of taking the lead from this time on, but unfortunately we won't be able to respond to any request for comments on our slots and jet fuel submission, but we, of course, welcome the PC to provide any questions that you require and we can take them off line through normal communication. So thank you very much.

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COMMISSIONER LINDWALL: Well, maybe that's the best thing to do, we'll talk generally about things and we might send you separately some questions about fuel and slots. Yes, that might be the best way of handling it. Perhaps you could talk about – well, since IATA covers so many countries and so many airlines, different countries around the world and their regulatory approach in general, and how you compare Australia's regulatory approach to other countries of similar type of size.

COMMISIONER KING: Yes, so comparison say to the constructive engagement approach of the UK and any others.

MR RAFFO: Yes. So in the world you have the full spectrum. Now, the question is where you believe Australia – where Australia should be in that spectrum, you know. So, to go to the worse, is like you can have countries especially, let's say not that well developed, although that's not necessarily the case, where you have from one day to the other a decree saying "charges are going up twenty dollars", whatever, and then you start shouting like what's going on, you know. And it becomes more political than anything else at that point in time.

On the other side of the spectrum you have much more, let's call it, well developed regulatory regimes, let's call it with a proper independent regulator which defines what's the best regulatory framework given their statutory duties. Now, I guess that you will probably – well, and then you have many different versions in the middle, so in Europe for instance, you have some of these regimes but you also have what is called the – well, all the airports in the European Union what you have is what is called the Airport Charges Directive, so for instance, which is, first of all, a law all countries has to comply with.

COMMISSIONER LINDWALL: Except for the UK, is that right?

MR RAFFO: Well, once it leaves. Yes. If it leaves. No, there is – no, so there is a clause in the directive if the airport is deemed to be in competition then there could be alternative arrangements. So that's what the, for instance, that what has been applied for instance in some of the UK airports, you know. And then what you have in there is the designation, the designation, again, but this is the UK, you know.

But in Europe all airports above 5 million, competition or not, the ACD applies. And again, which provides for the basic ICAO principles, transparency, consultation, discrimination et cetera. And also provides a process on how – although not in detail which is one of our issues, provides a process and also most importantly, an appeals process.

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So if the airport makes a decision which the users are not – or believe is not fair enough, they have the opportunity to go to a – what they call is an independent supervisory authority, that is how it is called over there. Now, what does the ISA do? It depends on the countries and the ISA for instance some things that we are raising our hands and say well, it is not the best thing because in some countries the ISAs do have the right powers to deal with this type of issues. In some countries they don't. So which is why we are asking, currently asking the Commission, in public and everything, to have a review of the directive.

Let's say if the worse is on the left and the best is on the right, I would say and then you have the ACD in the middle, although I have to admit I am not involved in the negotiations here but we are in contact with our stakeholders here and we have experience elsewhere in the world. Australia's a little bit on the left because once again, you don't have at least, this opportunity to access an arbitrator, an authority that can solve matters, issues that happens between the users and the airport, especially when we are speaking about airports with market power, you know. If they were in competition well, that would be different, if they were.

But those that do have the power, is like not having a third party, then it just opens up the opportunity for – well, what you call so elegantly, exercising their market power, I would call it abuse, no. Maybe, I have expanded a lot but there's a lot to speak about here, you know. So that – that's – I don't know, it's no coincidence that our friends from some of the – let's call it airport associations, in the world favour very much what is happening in Australia as well. I wonder why, but yes, and I presume that is because you – it is much the situation is less stringent on the airport providers.

COMMISSIONER LINDWALL: I mean, it is interesting, I met a little while back the regulator for the Singapore airport because it has a very interesting situation because they have Singapore Airlines, of course.

MR RAFFO: Yes, CAAS.

COMMISSIONER LINDWALL: The national carrier. They've got - Singapore Airlines has no choice but to land at Singapore Airport, can't go to Malaysia. And so that symbiotic relationship gives a lot of power to Singapore Airport. So that would justify more regulation for - - -

MR RAFFO: And they are regulated by the CAAS.

COMMISSIONER LINDWALL: Sorry?

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MR RAFFO: There is an authority - - -

COMMISSIONER LINDWALL: Yes - - -

MR RAFFO: Interestingly – sorry, going a little bit in Asia, in Malaysia, MAVCOM has been created and actually does, with the economic regulation of airports, and currently they are consulting on how they should be setting the charges, it is a quite interesting approach. So it is not just a European thing, the UK , it is happening and people are realising the importance of having a reasonable level of charges.

COMMISSIONER KING: But when you look at Australia also, the other distinguishing feature is that individual airlines have contracts, individualised contracts with the airport, contracts to New Zealand where each – there's a common contract for Auckland airport and all carriers, and some would say, I think that, that a number of participants have said that that's a great advantage because those contracts can be tailored to the desires of each party. Do you agree with that?

MR RAFFO: It depends what are the differences in the sense if there are differences in the service levels maybe there could be some justification.

COMMISSIONER KING: That's a type of thing - - -

MR RAFFO: But then we'd have to quantify your differences. I think we have gotten to a stage about linking service and price and I think this is something that BARA has been mentioning all along, is like right now - - -

COMMISSIONER KING: Exactly.

MR RAFFO: We are paying something and we don't know what we are getting, so there needs to be a much better, how can I say this, relationship between all of these.

COMMISSIONER KING: So you were here, I think, for the earlier discussion with - - -

MR RAFFO: Yes.

COMMISSIONER KING: Where we discussed whether the sort of forum they had been thinking about for boilerplate type contracts could be extended to think about service levels and appropriate service levels and incentives

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So any thoughts on that?

MR RAFFO: Well, I can tell you how it works elsewhere.

COMMISSIONER KING: Well, it is.

MR RAFFO: And where it works properly the discussions are, I don't know how to call it, multilateral.

COMMISSIONER KING: It's multilateral between different (indistinct).

MR RAFFO: So it's the airline community.

COMMISSIONER KING: Yes that speaks with the airport.

MR RAFFO: Because something that you need to realise that happens very much, I think the airport negotiations is a divide and conquer thing, so it's quite important that the community is there - - -

COMMISSIONER KING: That occurs in Europe so you have the airlines that - - -

MR RAFFO: Well, you can't have everything. Sorry, the discussion in terms of service level?

COMMISSIONER KING: Yes.

MR RAFFO: Well I wouldn't say - I don't know, in every single airport, but in general it is at the community level. So for instance, I don't know in the case Heathrow, in the case of, if I'm not mistaken, in Manchester, an SLA is being discussed. In Dublin where you have regulated environment, you have KPIs for the airport which are then consulted with entire airline community. In Spain as well, same thing. You have service levels that are set in consultation with the airline community. I participate in those discussions. And so on, you know, it's

COMMISSIONER KING: And the European Commission doesn't have any competition concerns about them, I mean, you know, having all the airlines altogether in one room of the airport?

MR RAFFO: Well, the thing is - I'm not a competition lawyer.

COMMISSIONER KING: No, and I understand.

MR RAFFO: But first of all my - first of all my personal think is, you're leading a monopoly. So it's a kind of monopoly and then - but having the clients separated, that doesn't sound right. Again, divide and conquer.

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Secondly, this is - the type of discussions is not that, "Well, this is the price and if you don't accept it we don't fly" or anything, we don't enter into that. We discuss a level of charges based on, I would like to say, a reasonable discussion on the costs and the underlying costs of the charges and that's as far as it go. Now, depending on the regulatory regime, we as an association can appeal or individual airlines, again, it will vary depending on the country you're speaking about but it's not like - it's not seen that we - the words in Spanish are here but the - like, everyone going together against the airport, I think it's like that. It's - we need to try to level the playing field.

COMMISSIONER KING: Is there enough flexibility though in that sort of system? So let's say I'm starting a new low-cost carrier, so to be able to get my foot in the door to set up my network, I need to get special deals essentially from some airports. If I just go and say, well, you know, "Stephen King Airlines is starting up" but I got the same deals that all the airports that everyone has got then, you know, essentially I'm starting behind the baseline. You know, I've got all the extra costs of the start-up, of advertising, building up a network, dealing with the fact that I have low passenger numbers. So can you do special deals in that European type framework?

MR RAFFO: Well, rather than a special deal, what you have over there is what is called "incentives" which are published.

COMMISSIONER KING: Yes.

MR RAFFO: Now, whether you are ready or not with incentives that's a separate thing but they are available and they are available to everyone so it's not, "I'm dealing with you and I'm giving you this" so it's - - -

COMMISSIONER KING: But the incentives usually, unless it's different to other industries, but I guess, and I am guessing, they'd be that you get a lower charge the more volume you bring through an airport. So again they would operate against a new start-up who's starting from zero who would have to build up their volume at the airport so a new start-up could face higher charges not lower charges.

MR RAFFO: Well, the thing is what the airports do is that they offer incentives to help the airlines to develop their route. It's like, you don't have 100 per cent capacity utilisation from the first date so that is a type of incentive.

COMMISSIONER KING: So you can do that, okay. That's the bit I wasn't clear about.

MR RAFFO: Yes, my apologies.

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COMMISSIONER KING: No, no. Your English is a lot better than my Spanish.

COMMISSIONER LINDWALL: In your experience, Cesar, how would you describe Australian airports in general in terms of quality and price compared to say the United States, Europe, England, Asian - - -

MR RAFFO: I would need to defer to the airlines locally but again, as far as I understand, is the data on quality is not there so it's very difficult to compare. So it's only you have subjective surveys and to base your assessment on that is - no that's a no-go. No, you need to have quantitative data - how many minutes of queues on security or whatever, you know, and that is measured in the same way.

COMMISSIONER LINDWALL: Would IATA publish the types of standards that should be measured? Would we have guidance on this(indistinct)?

MR RAFFO: We do have guidance. This was included already in our first submission so you need to read it. We have a series of - well, first of all it's called a service level agreement, a paper.

COMMISSIONER LINDWALL: That's right.

MR RAFFO: And it does mention a number of indicators that could be used for measuring performance. Now, there needs to be a further discussion where in these particular circumstances those indicators, are they the apropriate ones or not, no?

COMMISSIONER LINDWALL: Yes.

MR RAFFO: That would be a starting point and it includes series of examples.

COMMISSIONER LINDWALL: And this is a type of thing that evolves over time I would imagine.

MR RAFFO: Absolutely.

COMMISSIONER LINDWALL: And do you collect the type of information from your member airlines, that 290, to say the types of things that value to them and perhaps help provide guidance to improve the standards over time? Because it's all very well having quality standards but as you know they're fixed in stone. You need to improve quality over time, don't you, in a number of areas and expectations change too.

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MR RAFFO: Well, yes and no. It depends on - because there's always a cost to it.

COMMISSIONER LINDWALL: Of course there is, yes.

MR RAFFO: You know, it's like when I was dealing with ATC, air traffic control is like - yes, ideally you would see no delays, no, but there is a cost to it as well.

COMMISSIONER LINDWALL: It's called gold plating.

MR RAFFO: Yes and so this is part of the conversation that you need to have at an airport level, you know, to see what are the requirements of the airlines behind there and then having a proper discussion on the cost related to it.

COMMISSIONER LINDWALL: Do you think there should be more transparency on pricing then?

MR RAFFO: Yes, for the record.

COMMISSIONER LINDWALL: Well, I know you said that before, so.

MR RAFFO: Well, there needs to be transparency and I'm going to take advantage of something if I may please.

COMMISSIONER LINDWALL: Yes, certainly.

MR RAFFO: In a way I'm - and my apologies how this is going to come out, it's like you sort of dismiss in the draft report the idea that there needs to be some sort of minimum requirements when you have consultations. It's like oh, it's like giving the hand to the airlines. Actually, it's not, it's levelling the field and again, from what I was hearing in some of the examples is, "Look, I cannot receive one pager for, I don't know, $100,000 investment and the same one pager for a $200 million investment. So there needs to be some sort of minimum principles, what is what needs to be provided, the type of justification that needs to be provided and then get on with it and have the consultation. It's like, at least with a proper transparency, we don't stay in the first - let's call it the first fight, and say, "Well, I cannot even have an informed opinion because I don't have a transparency", you know. At least we have the transparency and then we can have the proper discussion. Now, we all can agree, we cannot agree that - well, you would always have two things but at least we're not fighting on whether you gave me two lines or three lines or one line, you know, if that makes sense, so having those on the cost side but on the investment side some processes, as you were saying, the constructive engagement process.

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COMMISSIONER LINDWALL: Minimum information requirements.

MR RAFFO: Minimum information and if that could be actually through consultation, could be the ACCC, could be any other agency to have that discussion; what is the minimum necessary?

COMMISSIONER LINDWALL: So there's the monitoring information we get through the ACCC each year but - - -

MR RAFFO: But ex post.

COMMISSIONER LINDWALL: Exactly ex post. This is ex ante information

MR RAFFO: This is when you are having the discussion itself.

COMMISSIONER LINDWALL: That's right, yes.

MR RAFFO: So that you don't end up in a Turkey bazaar type of situation, you know.

COMMISSIONER LINDWALL: Yes.

MR RAFFO: No, it's like you have an appropriate level of costs and appropriate discussion and hopefully you reach some sort of agreement, you know, but if you can't because you don't think they are reasonable then you have an instance where you can escalate matters.

COMMISSIONER LINDWALL: The building block methodology used in Australia, was that traditionally used also?

MR RAFFO: That's ICAO. That's ICAO's policies, building blocks. That's the baseline for the calculation of charges. Key thing is not just using the building blocks, it is what goes into the building blocks.

COMMISSIONER LINDWALL: Of course.

MR RAFFO: If the operating costs are efficient, what are the depreciation accounting rules that you use, you know, if you're building a terminal or a runway that would last 50 years and you depreciate it on 15 then there's a problem. The WACC, obviously that's the typical discussion. The CapEx , is it the right scope, is it being delivered at the right time, at the right price, at the right cost. So it's all these things that are – ah, well, the discussion has already happened throughout the day, what do you do with the other part of the airport, that's like, on the non-commercial side? It's how you set the charges; if you treat the airport as a single thing or as separate businesses. So

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those are the key discussions. The building block is no problem, it's the other things, you know.

COMMISSIONER KING: And that's why discussion about the blocks correct?

MR RAFFO: Yes and having the right environment that will allow the right discussion about the blocks.

COMMISSIONER KING: So one of the things that has occurred in Australia because of issues of re-evaluation of assets, de facto - I think all the airports, or the monitored airports certainly, use a capital base in their building block calculations that actually took the value, I can't remember, a number of years, it might be ten years ago now, I'm not sure of the exact year, and then added on actual costs after that, so.

MR RAFFO: The line in the sand.

COMMISSIONER KING: Yes, the line in the sand approach. Do you think that sort of regulatory guidance, if I can put it that way, for things like the building block model that the airports use is useful?

MR RAFFO: Well, it certainly could be useful but again - well, it's difficult to deal with the past because it's - but again you need to know what goes in it, and this is something that we highlighted in our submission as well because you were looking at the return on assets but without really making an assessment or whether the assets were efficient or not. Now, looking at the past again it's quite difficult and for looking forward then probably something could be done, you know, so that only efficient assets or efficient costs are included.

COMMISSIONER LINDWALL: Yes, once you start going there, who chooses whether the assets are efficient or not, that would have to be done by an external party presumably?

MR RAFFO: If the negotiations fail probably you will need to go there into that direction. It depends on how the framework is set.

COMMISSIONER LINDWALL: And so is that done in any overseas countries because where it has occurred here in other industries, it's led to regulated businesses trying to seek ex-ante approval for assets so saying, "Well, we won't invest unless we know that the arbiter or the third party body is...", in this case it's a regulator usually, "Is not going to later on say 'No, no, we think that was excessive or inappropriate" or whatever.

MR RAFFO: Yes.

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COMMISSIONER LINDWALL: So you end up with this unfortunate situation where every investment is second guessed by a regulator and, you know, so we're not far off from the regulator saying, "Well, this is what you can build and this is what you can't".

MR RAFFO: But then what's the alternative? Let them build whatever they want at what cost. So it's - - -

COMMISSIONER LINDWALL: No, I'm asking has that been a result in the case of where - - -

MR RAFFO: Yes, obviously, and I was surprised to hear some of these comments today. yes, you need to have this type of discussion in advance. You know, it's like on that particular item I would agree with the person of Cbus, it's making changes expost is, it's - I will disagree with much of the other stuff like he said but

COMMISSIONER KING: It's got to be ex-ante.

COMMISSIONER LINDWALL: It has to be ex-ante.

MR RAFFO: Yes. Now, for example, the UKCA says, "Okay, I'm giving you ex-ante but I'm also doing a check ex post just to ensure that there's nothing - - -

COMMISSIONER KING: Which is standard among regulated assets in electricity and gas and elsewhere here in Australia.

MR RAFFO: Yes, so it would have to be ex-ante. The question is how?

COMMISSIONER KING: Devil is in the detail as it were.

COMMISSIONER KING: Now, it seems to me that there's going to be a fundamental change in the air market or the transport market over the next few years with the increased use of the long range white bodied aircrafts, you know, Qantas already is flying from Perth to London and I'm sure there'll be more of that. About 15 or 20 years ago, or more even, there were a lot of European carriers, Alitalia, Air France, Lufthansa and so on, coming to Australia. But now of course they tend to go to hubs, so we don't see much of that anymore. They go to Singapore, Dubai and so on.

MR RAFFO: Yes.

COMMISSIONER LINDWALL: I guess I'm wondering if you think that we'll see a lot more different carriers coming to Australia that haven't been coming to Australia for many years because of a growth of long range transports?

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MR RAFFO: I cannot answer that. My apologies.

COMMISSIONER LINDWALL: Can I ask for speculation?

COMMISSIONER KING: I'm just surprised (indistinct), do you ever fly Alitalia (indistinct), I'm just surprised you want them back.

COMMISSIONER LINDWALL: Alitalia, for the record - - -

MR RAFFO: I'm Italian, (indistinct words).

MR ZANARINI: I would hate to tell you who I used to work for.

COMMISSIONER LINDWALL: The very first 747 to land at Canberra Airport was in 1972 and was an Alitalia plane and it was diverted from Sydney Airport and at the time the runway was nowhere near long enough for a 747, but anyway, so yes I was just speculating that's all. I don't think I've got any more questions.

COMMISSIONER KING: No, I'm fine.

COMMISSIONER LINDWALL: There's a lot of questions we've got on jet fuel and slots and so on but maybe more things that you'd like to talk to us about, you know, before we finish our conversation?

MR RAFFO: Yes, well I'm just repeating what has already been said, you know, it's like we were a little bit surprised with the report especially with analysis. We thought it was, again apologies, a little bit light touch, in the sense that no, it's like, okay with the indicators that you saw, analysed, and then determined that the market power was not systematically exercised and therefore we - and again, especially in light of all what has been said in these hearings, I think there is merit in going back and have a further look at some of these things and further analyse them. Maybe there is - well, I mean in our view there is enough evidence to propose a change in the way the regulatory system works here.

Now, I heard at the beginning of the day you were asking, "Okay, how exactly do you see this happening?" I'm not sure if we need to - well, I'm not sure if you need to say this at this point in time in the report. In my view the report needs to say, "Is there a problem? Yes or no," and if there is a problem then what can be solved. A4ANZ was mentioning, "Well, what are the options?", you know, it's like in a way, again from me looking at things from 41 thousand feet it's like saying, "it looks like these guys are trying to shoot down the final offer arbitration,", or whatever, you know, but if, for instance, If you believe that there is a problem (we believe that there is a problem) and you think that something needs to be done. Maybe the next step will be to

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have some sort of follow-on consultation on, "Okay, we know that something needs to be done. Okay, let's discuss all the options, pros and cons in much more detail, let's all think here how this thing will work," and then get a solution out of it. You know, instead of in June saying, "this is the solution," if that makes sense.

COMMISSIONER LINDWALL: Yes, I understand that.

MR RAFFO: You know, it's - okay, I don't know if it's within your remit but it will be a recommendation to the government, for the government to then send it back to the PC, I don't know, but as a follow up, no?

COMMISSIONER LINDWALL: When we're convinced, and say this was a draft report, that there needs to be a change to something, we would usually investigate different alternatives and then we would try and judge ones against the other.

COMMISSIONER KING: Yes and I mean, I think what you're seeing is that some parties have put forward a particular solution and we're just trying to work out if it's practical so you are seeing one solution being debated more but, for example, Dr Williams mentioned an alternative which would be a sort of single till price capped which is more of a sort of approach that was used in other industries in the UK and it's certainly one I'm familiar with and there's a long history of that in other industries and it's got merits and it's got - but, no one in a sense has put that up other than Dr Williams at the moment so we haven't been really trying to explore it in depth.

MR RAFFO: Well, probably I think it would be good to explore all options to show that you have been exhaustive in the different options, you know, and not just say, suggestion again, you know, "This is what we have received, this is what we have analysed" and then yes or no and then that's it. So maybe again, if you think there is a problem, maybe yourself come up with a solution, I don't know. But it's this analysis of different ways of solving a problem that will hopefully be competent. Thank you.

COMMISSIONER KING: Thank you.

COMMISSIONER LINDWALL: Thank you very much. Well, everyone, there's always an opportunity for anyone who wants to come and have a say and either rebut or agree to something that's been said through the day so does anyone want to take another opportunity? Please, Graeme.

PROF SAMUEL: Do I come up here?

COMMISSIONER LINDWALL: Yes and you better say your name again for the record.

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PROF SAMUEL: Now, I promise you, Commissioners, this won't take longer than an hour and a half so - - -

PROF SAMUEL: We'll keep it short for you guys.

PROF SAMUEL: I will be short, I promise. I just wanted to cover on a few things that have come up through the day and can I say to you that personally I found this a really constructive day. It's been very helpful indeed and I think you will detect an approach made for ANZ that is much closer to the approach of our Spanish friends, or Spanish friend from IATA, which is, We'll apologise for, you know, suggesting that things are a bad light, in terms of the investigations you've done or whatever it might be but we'll still be pretty firm as to the approach we're going to adopt. I just wanted to correct a couple of things for the record. First of all, arbitration is not just about price, it's about everything, it's about the whole thing including terms - because if you take the standard aeronautical service agreement, the ASA, it covers the whole process of the provision of aeronautical services and land side services as well and that's probably one of the reasons why Dr William's approach of a price cap is not going to work because - and I might say that's not an A4ANZ approach, it is framed this way too.

COMMISSIONER LINDWALL: No, no, understand that. He said that.

PROF SAMUEL: He said it, yes, but when you talk about a price cap, you talk about a price cap in return for something and that's very easy - well, I say easy to do when you're talking about, you know, pumping electricity down a transmission line or pumping gas down a gas pipeline, a lot harder to do when you're talking about all the various elements of the 70 page aeronautical services agreement so I respectfully put aside the concept of a price cap. So we are dealing with services as well. The problem that the airlines have, and as you are aware, most of the airlines that used to manage or own their own terminals are gradually transferring them to the airports.

That's where service becomes a very relevant factor because, for example, at the Melbourne terminal Virgin manages its main terminal, I think it's terminal 3. Qantas at the moment manages its terminal 1. But the terminal is branded a Virgin terminal and if you, dare I say it, use the conveniences there, the toilets, and they're dirty, as they have been twice for me, then I think, "Well, I'll ring Virgin and find out what's going on," and they'd say, 'It's not us, it's the Melbourne Airport" and they have no way of actually controlling that so elements that would be involved in the negotiations/arbitration will involve potentially penalties for a failure to meet the various service standards that are required if they can be negotiated. So that was item one.

Item two, you did raise the issue of pass through - actually I've done two because there was the price cap issue. You did raise the issue of pass through and the response I think I'd have given is this: If the arbitrator cannot be

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convinced that the normal process of competition such as, for example, exists between Jetstar and Tiger Air as two low-cost airlines, will result in the lowest possible airfares relative to costs and the like, then clear that the arbitrator's going to then, in the context of the public interest that he would have to apply or she would have to apply, will then say, "Well, maybe I want to have some form of pass through." But we shouldn't underestimate the very complex aspects of "passing through," if you like. It's quite complex indeed. It has, by the way, the aeronautical charge for the low-cost airlines can form a very significant part of the total airfare as you'd be aware.

The third thing I'd say is this, and it follows on from something that our friends from IATA commented upon just at the conclusion when they said, "If you were of a mind to even consider the issue of negotiate-arbitrate", and we've talked about all that this morning and following the discussion that Commissioner King and I had about the details of it, it seems to me, and what we will undertake (indistinct words) is give you a detailed submission on the way that the arbitration might be conducted with, you know, appropriate references particularly to the Vertigan analysis and the like. But if you're of a mind to be pursuing that, may I respectfully suggest that you follow-up the suggestion made by IATA which is that we get a round-table together and you actually say, "Well, what about this? What about “if the airline and the airports don't agree on a travelator?” but the arbitrator thinks the travelator ought to be there, how would you deal with it, right?

The reason I suggest that is this: that if we put something forward, we could put through a list of criteria that ought to be examined or ought to be part of the directions for an arbitrator, but if we put in too much then I can well hear Commissioner King say, "But hold on, the government's getting too involved". If we put in too little then you'll say, "Yes, but what about this? What about that?" and I think the way that you develop that is we'll give you a draft template, if you like, but we think there'd be a lot of benefit in having a round-table where we actually talk about, between us, the sort of things that you might say, "You've forgotten this" or "Why do you want that?" or whatever it might be and we'd be very happy to participate in that as I think IATA themselves has said is a sensible way of taking that forward otherwise they think we'll end up with a problem.

We do think that the three fundamental issues are public interest, competition and efficient investment. The efficient investment is a really interesting one and I know Commissioner King has actually discussed this a bit in terms of the ex-ante approval, if you like, of investment. I'm not sure that necessarily happens. What happens is two things: first of all in the negotiations a lot of the investment is agreed upon. There will tend to be three fundamental problems or disagreements. The first is: is the investment proposed efficient? That is, it is being done at an efficient cost? And so often the airlines will say to the airports, "Your cost is not efficient. We can do it more efficiently," and can demonstrate just that. That indicates to the airlines that what's

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happening is that the airports have less concern about efficiency because they pass through the costs in terms of charges to their various users of services.

The second thing that happens is this: is that, you asked the issue about the most favoured party clause and things of that nature, and I can tell you exactly what occurs. With the exception of the major operator Qantas, and this is not a countervailing power issue but with the exception of that the rest are either much smaller players or they are, in the case of Virgin, the challenger and they can be - I don't want to put it in terms that this is what happens, but it is very easy to actually settle terms with a challenger that says, "You are very keen to have a lounge put in place. We'll pay for the lounge or we'll put it in place for you. We know you need it quickly because that's part of the challenge process to get in the domestic area," and then the challenger will say, "Well, that's fine but you can't do a deal that's better than the one you're offering us to any other party."

And essentially they hang up the cloak with coat tails of the larger player and the larger player says, "Well, look we can just sort of sit there and we can do one of three things. We can reach an agreement", which doesn't happen, "We get to an intractable no-deal," like a no-deal Brexit and then you know what happens there, and then thirdly they simply say, "We're not going to pay" and "What are you going to do about it?" because, you know - and the airport says, "Well, in the end we'll sue." And that's what's happening at Perth Airport.

And that's where we then get into this problem that we had that we discussed before which is litigation arbitration, and I think Commissioner King has actually said on a few occasions there in the questions he's asked, "Well, is that really sensible having an inexpert judge do these sort of things with the various constraints of litigation" or you've got Part IIIA access declaration.

Yes, if you've got enough years to wait for that process of the NCC. I should just emphasise the NCC has no position of arbitration. It's only position, as we all know, is to determine whether or not there's a declaration so we go through an eight year process of court appeals to determine whether declaration occurs or the simplest and most efficient is say, "Why don't we just have a commercial arbitrator that can be called upon by any one of the parties experts subject to criteria, ones that mention competition, public interest, the efficient investment, and all the others that were put up to you and yes, that's the way that we see it going. So they're the primary things I just wanted to raise. It's just to deal with a couple of the corrections of, you know, some things that we heard just through the day.

COMMISSIONER KING: All right. On that Virgin toilet issue, did you say that was Melbourne?

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PROF SAMUEL: No, one was Melbourne and one was Sydney and I lost two pairs of shoes as a result. I had to throw them out.

COMMISSIONER KING: I will say that because you've raised this before and maybe we're both elderly gentlemen - - -

PROF SAMUEL: I'm prepared to concede I am, but go on.

COMMISSIONER KING: I went into the Virgin toilets and found them comparable to the ones in the Qantas terminal.

PROF SAMUEL: Yes, yes. I can't think of any - are you talking about in Sydney or in Melbourne?

COMMISSIONER KING: No, Melbourne.

PROF SAMUEL: Melbourne, yes and that may well be the case but you could take that up - you see, Qantas then bears the responsibility for that until they handover the terminal to Melbourne Airport. Virgin bears the responsibility because their toilets are branded Virgin - they're actually branded male and female but they're actually there in the Virgin terminal.

COMMISSIONER KING: Yes, I didn't have to throw my shoes away.

PROF SAMUEL: Yes, I did.

COMMISSIONER LINDWALL: Well, it must be getting close to the end when we're talking about toilets.

PROF SAMUEL: But that is the - - -

COMMISSIONER LINDWALL: (Indistinct words) arbitration.

PROF SAMUEL: Yes. But it is the issue of quality and of course what we do find is that the areas where they get (indistinct), if you go into the Virgin terminal, the large retail area, superbly glossy and fresh and everything else. You go into the non (indistinct) areas, if you like, then you have a totally different standard.

COMMISSIONER LINDWALL: Well, thank you, Graeme. I should ask does anyone else want to come and have a chat?

MR LYON: I'm an observer, I'm not - - -

COMMISSIONER KING: No, that's fine. That's in fact what's meant to be for so.

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COMMISSIONER LINDWALL: You'll just have to introduce yourself.

MR LYON: Yes, okay. Yes, I'd just make one point - I'm David Lyon from RMIT University. I'm in the School of Engineering. It hasn't been discussed today but I'd just like you to take into account the fact that the competitive model for airports in Australia is changing over time. Just to talk about the two biggest cities, so Sydney and Melbourne, Sydney first. So when the Sydney Airport was leased by the Federal Government to Sydney Airport, they were given the first right to operate any other airport within 100 kilometres of that airport. The government then put the pressure on them for the West Sydney Airport to see whether they wanted to exercise that right, they chose not to do so.

In choosing not to do so the Federal Government and, I think, the New South Wales Government, developing that airport which will then either be operated by the current owners or it will then be leased off to another airport party so therefore there will be competition in the Greater Sydney area within 2026 and that airport's already under construction or (indistinct). So there's going to be more competition there, so that's something. And in terms of Melbourne, we have two airports that are operating internationally now already, so - - -

COMMISSIONER LINDWALL: And Avalon as well, yes.

MR LYON: Yes. So since December last year AirAsia moved their operations from Melbourne to Avalon and Jetstar operate from there. Jetstar before were arguing about the pricing issues that they have but they actually - their operations from Avalon are subsidised by the airport, by discounting, and also by the Victorian Government. So I guess the only point I'd make is in the life of the next - in a relatively short term, the two largest cities in Australia are going to have airports which then airlines could choose to operate out of.

So already Jetstar is operating from Sydney and Melbourne and could choose to operate - the other major airlines could operate certain airports in Sydney. Some of my students, we did a project and we looked at the third runway for Melbourne and concluded that, you know - and Melbourne have actually delayed their third runway because it's a major infrastructure, and you can actually model it as if you're saying, "Well, a third runway for Melbourne has already been built, it just happens to be at Avalon," and airlines need to make a choice as to whether they exercise where they want to operate from and they will have two independent airport companies that they can then negotiate with.

COMMISSIONER LINDWALL: And of course Brisbane's got the Gold Coast and the Sunshine Cost.

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MR LYON: Yes, that's - - -

COMMISSIONER LINDWALL: They're so different I suppose.

MR LYON: Yes, well I think that's owned by the same company.

COMMISSIONER LINDWALL: Yes, that's the trouble, yes.

MR LYON: So there's not the same competitive level. I think Coolangatta is - - -

COMMISSIONER KING: I'm pretty sure Brisbane Airport and - - -

COMMISSIONER LINDWALL: Brisbane and Gold Coast are not the same.

MR LYON: Sorry, yes. So just in terms of there being a more competitive airport market, I think that that is starting to occur.

COMMISSIONER KING: And we might start looking a bit more like Europe. Just on Avalon though, Avalon and competition from Avalon has been coming for an awfully long time.

MR LYON: Yes.

COMMISSIONER KING: Any thoughts on why it has been so unsuccessful in being a second airport in Melbourne?

MR LYON: The distance to Avalon is a problem. The CEO of Avalon Airport is advocating that there be another railway station just further past Lara so that you would actually go to - you would catch a train out to the station, which will be called Airport or Avalon, and then you would check-in at the airport - sorry, at the railway station. They have a master plan like all the other airports and they have the two runways. They've just invested a large amount of money to attract AirAsia there and they've built the 5 thousand metre, so yes. As the growth of Melbourne is going to towards the west, you've also got perhaps tourism operators looking at the Great Ocean Road and other attractions and yes, so it will come into its own over time.

COMMISSIONER LINDWALL: All right. With the fights over the fast rail - fights, I shouldn't say that, the various - you can smell an election in the air when you suddenly have fast rail projects coming up. Have any of those actually - because I just haven't looked at the detail and it really is something I should have thought of, have any of those actually taken into account Avalon?

MR LYON: Any of those?

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COMMISSIONER KING: Taken into account Avalon Airport, so Geelong Airport, probably Sunshine would be next.

MR LYON: Well, the CEO of Avalon Airport is trying to do that because he could pull-off that rail link to his airport where as the rail link to Tullamarine Airport is way in the distance. It witness actually make a competitive advantage for Avalon over Tullamarine.

COMMISSIONER LINDWALL: Okay.

COMMISSIONER KING: Yes, okay.

MR LYON: Thank you very much.

COMMISSIONER LINDWALL: All right, thank you very much, David. Anyone else want to come and have a - - -

MR RAFFO: Just to follow-up on this.

COMMISSIONER LINDWALL: Yes, please.

COMMISSIONER KING: You'll have to do it up here for the microphone

MR RAFFO: All right, just a quick one and - - -

COMMISSIONER LINDWALL: You better say your name again, Cesar.

MR RAFFO: Cesar Raffo. I probably have to say this so that it doesn't stay unanswered. The existence of two airports doesn't mean that there is going to be a competition. We need to understand what are the market dynamics, that people travel from the airport that is closest to them and this type of things so again I would suggest extra care before jumping- making any conclusions.

COMMISSIONER LINDWALL: We mention this in our report, yes.

MR RAFFO: Okay, thank you.

COMMISSIONER LINDWALL: Thank you, Cesar. Anyone else? In which case I'll adjourn the hearing until tomorrow. What time do we start tomorrow? 9 am tomorrow. Thank you all for attending.

MATTER ADJOURNED AT 4.57 pm
UNTIL FRIDAY 29 MARCH 2019

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Australian Government
Productivity Commission

PRODUCTIVITY COMMISSION

ECONOMIC REGULATION OF AIRPORTS

MR P LINDWALL Commissioner
DR S KING, Commissioner

TRANSCRIPT OF PROCEEDINGS

AT PC OFFICES, LEVEL 12, 530 COLLINS STREET, MELBOURNE ON FRIDAY 29 MARCH 2019 AT 8.56 AM

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COMMISSIONER LINDWALL: Good morning. Welcome to the public hearings of the Productivity Commission inquiry into the economic regulation of airports. I am Paul Lindwall the Presiding Commissioner of the inquiry and my fellow Commissioner is Stephen King. I would like to acknowledge the Wurundjeri people of the Kulin Nation.

The inquiry started with a reference from the Australian Government in June 2018. The purpose of the inquiry is to investigate whether the economic regulation of airport services promotes the efficient operation of airports and related industries. We released an issues paper in July 2018 and have talked to a range of organisations and individuals with an interest in the economic regulation of airports.

This has included representatives from the Australian State and Territory Governments, airports, airlines, industry representative bodies, academics, researchers and individuals with an interest in the issues throughout the inquiry. We held focused public hearings on competition in the market for jet fuel in Sydney and Melbourne in late November 2018 and following the release of our draft report in February 2019, the Commission has called for further submissions and is undertaking consultations along with these public hearings. We have received 88 submissions prior to the release of our draft report and about 30 since then and they're still growing since its release.

We are grateful to all of the organisations and individuals who have taken the time to prepare submissions and appear at these hearings. This is the fourth and final public hearing for the inquiry. We will then be working towards completing a final report after considering the evidence presented at the hearings, in submissions, and during other informal discussions. The final report will be submitted to the Australian Government in June. Participants and those registering their interest in the inquiry will be advised of the final reports released by the government which may be up to 25 parliamentary sitting days after completion.

The purpose of these hearings is to provide an opportunity for participants to provide comments and feedback on the draft report. We like to conduct all hearings in a reasonably informal manner but I remind participants that a full transcript is being taken. For this reason comments from the floor cannot be taken but at the end of the day's proceedings I will provide an opportunity for anyone who wish to do so to make a brief presentation.

You are not required to take an oath but are required under the Productivity Commission Act to be truthful in your remarks. Participants are welcome to comment on the issues raised in other submissions and by other participants. The transcript will be made published on our website in due

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course and submissions are also on our website. For any media representatives attending today, some general rules apply. Please see one of our staff for a handout which explains those rules.

To comply with the requirements of the Commonwealth Occupational Health and Safety legislation, you are advised that in the unlikely event of an emergency requiring the evacuation of this building, please listen for instructions over the P.A. Follow the exit signs to the nearest stairwell. Lifts are not to be used. Please follow the instructions of floor wardens at all times. If you believe you would be unable to walk down the stairs, it's important that you advise the wardens who will make alternative arrangements for you.

Participants are invited to make some opening remarks of not more than five minutes. Keeping the opening remarks brief will allow us the opportunity to discuss matters in participant's submissions in greater detail. I'd now like to welcome the Australian Institute of Petroleum. I think it is Paul Barrett. Is he on the line at the moment? Paul?

MR BARRETT: Yes I am.

COMMISSIONER LINDWALL: Hello, Paul, how are you?

MR BARRETT: I'm very well, thank you.

COMMISSIONER LINDWALL: Can you hear us clearly?

MR BARRETT: I can hear you very clearly, thank you.

COMMISSIONER LINDWALL: Excellent. All right, would you like to introduce yourself, Paul, and make an opening statement.

MR BARRETT: Yes, please. So thank you and good morning, Commissioners. Thank you also for the opportunity to appear at today's hearings and have another exchange with you. My name is Paul Barrett and I'm the CEO of the Australian Institute of Petroleum, AIP, and I'm also joined in here this morning by a fellow, Nathan Dickens, who is the AIP Deputy CEO. We apologise for not appearing in person but we've had a number of pressing matters that we've been finalising including the national framework for fuel standards for petrol and diesel.

So I am here to represent the views of four member companies who are BP Australia, Caltex Australia, Mobil Oil Australia and Viva Energy Australia. These four companies have decades of operational experience in Australia and Asia delivering high quality fuel, including jet fuel, to their respective

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customers and have very significant investments in infrastructure around Australia throughout the supply chain. We've invested over $10 billion in the last decade in refineries and other supply infrastructure and with the finalisation of these fuel standards we anticipate investing a considerable amount more in excess of $1 billion over the next ten years.

These four companies, as well as the JUHI JV's operating at Australia's (indistinct) have made a significant contribution to this PC inquiry to support the delivery of a robust final report to government. These parties are the only ones that could really assist the PC with the information sought as most of the matters of interest relate to commercial incompetence and contractual arrangement relevant to each party. As an industry association, AIP does not get involved in commercial matters as appropriate. The major contribution of these parties is outlined in AIP's submission to this process which has included a range of detailed submissions from companies and JUHI JV's, 14 (indistinct) and submissions in total detailed by lateral discussions between the PC and each company to share commercial incompetence information (indistinct) emotional sensitivities and attend at public PC hearings.

AIP member companies and JUHI JV's have focused on, to the greatest extent possible and in a public way, the PC's information request (indistinct) related to jet fuel infrastructure owners and jet fuel suppliers. The additional priority information request identified by the particular in discussions with AIP and other claims, conclusions and (indistinct) made in the draft PC report which we've addressed, in our submission, or have been extensively addressed in the JUHI JV or company submissions. AIP's most recent submission summarises key evidence and conclusions from this information and there are four key conclusions. The first that the JUHI JV's are operators of an infrastructure. They are not sellers or suppliers of jet fuel.

The second: third party access to JUHI JV's is readily available on commercial terms and most importantly the nature of the operations of the JUHIs is evolving and will continue to evolve. The third: that airport lease tenure impacts on access by third parties and infrastructure investments at the airport. The fourth: jet fuel prices in Australia are competitive and reflect market prices (indistinct). Our detailed (indistinct) information has been provided to support these conclusions and AIP member companies are willing to share additionally incompetent information where commercial sensitivity and legal constraints are involved. These four conclusions are inconsistent with the PC's drafting finding 8.1 which was strongly rejected by AIP member companies and as a result they see no clear or strong case to justify consideration of any heavy handed (indistinct) options canvassed in the draft PC report. Instead AIP does agree with and supports the PC's

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overarching conclusion that the benefits from measures to improve the conditions of competition should be carefully weighed against the potential cost such as changes to incentives for infrastructure invested.

Even if the benefits of industry specific regulation are greater than the cost, there may not be a need (indistinct) to facilitate access (indistinct) your infrastructure. This position is underpinned by clear market developments and evident that access models and arrangements are evolving naturally on commercial terms and at predictable times such as (indistinct) negotiation with leases without government intervention. In addition, AIP and the companies do support the PC's draft recommendation 8.1, open access to JUHI at Western Sydney Airport for the reason that (indistinct) submissions. Primarily, the industry can make (indistinct) and investment plans with a clear knowledge of a future operating environment on this basis.

Our AIP member companies also support, in principle, the PC's draft recommendation 8.2; establishment of infrastructure consultations forums. If there is a clearly defined role focusing on the discussion of the master planning and coordination of infrastructure invested at the airport and involving infrastructure owners and operators. These positions are explained in the AIP member company and JUHI JV submissions. I welcome any questions from the Commissioners.

COMMISSIONER LINDWALL: Thank you, Paul and thank you Nathan too. In submissions and during meetings we heard that the operations and marketing of jet fuel are separated by information barriers in the business. Are you able to just describe how those barriers function in practice?

MR BARRETT: Okay, I missed a little bit of that but I (indistinct) question of barriers.

MR DICKENS: Sorry, Paul, we lost you.

COMMISSIONER LINDWALL: Sorry about that. I was saying that - I'll repeat it. In submissions and during meetings, we heard that the operations and marketing of jet fuel are separated by information barriers in the business. How do the barriers function in practice?

MR DICKENS: I think, Paul, that's a question best directed to any of the JUHI JVs or indeed to the member companies that are appearing today. We have no visibility of those arrangements.

COMMISSIONER LINDWALL: Okay that's fine, Nathan. A common theme in the JV and fuel supplier submissions is the operation of JUHIs are

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separate from the business of fuel suppliers. In practice are you able to describe how they maintain those clear lines or is that something that I should ask the fuel companies?

MR DICKENS: Again, that's a question that you should be directing at the JUHI JV's fuel suppliers. There's no - we don't have any visibility in the inner workings of those arrangements.

COMMISSIONER LINDWALL: I'll get Stephen to ask a question now then.

COMMISSIONER KING: I want to ask one but it's slightly - again, you might not be able to answer this one but just looking back through the discussions yesterday, the issue of fuel throughput levies came up. What's your view on fuel throughput levies? We've had different views put to us by different parties. What's your organisation's view of the role of these levies?

MR BARRETT: Was that you, Stephen?

COMMISSIONER KING: Yes, it was.

MR DICKENS: Yes, thank you, Stephen. Look, I note that we didn't address that matter specifically in the AIP's submission recently tendered to you. We did identify throughput levies in the generic price build (indistinct) I think on page 6 of our submission. We didn't specifically address or articulate an AIP view on throughput levies but I note that a few of our member companies via their company submissions rather than JUHI JV submissions, expressed a view in relation to it. We didn't have or seek a consensus view on that issue across the AIP membership but I note some of our members expressed a view that it's a levy or fee without economic or efficiency basis and they're charging it and passing it straight through to the airlines effectively as a charge from the airport.

COMMISSIONER KING: All right, so various claims that are made. Is it best that I put them to the individual fuel companies and perhaps get their views? Is that probably better than asking yourselves?

MR BARRETT: Well, I was just making the point where it (indistinct) organisation and we didn't seek or consensus on that issue.

COMMISSIONER KING: No, that's fine.

MR BARRETT: But some of the member companies have been very clear in their positions in relation to that issue.

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COMMISSIONER KING: Yes. Perhaps just a factual question, and again I'm happy if you say this is better for the individual companies, but there are claims that have been made by airports that these fuel throughout levies are simply part of the negotiation with JUHIs over lease terms and conditions. A simply factual question: do you know if fuel put levies have been either introduced or changed outside negotiations over JUHIs?

MR BARRETT: Stephen, again that's a question - - -

COMMISSIONER KING: Fine.

MR BARRETT: As we've indicated we don't have any physical (indistinct) appropriate into the internal individual workings of each of the JUHIs, so.

COMMISSIONER KING: No, that's all right. Could I ask - - -

MR BARRETT: (Indistinct) sorry.

COMMISSIONER KING: That's fine. No, I understand. In your submissions and in your comments just earlier in your introductory statement, Paul, you said that AIP supports open access at Western Sydney Airport. Could I imply from that that you would support open access at other airports if the access tariff was priced to reflect sunk investments made by the JUHI members?

MR BARRETT: I think that one of our key points that we really wanted to get onto the record today is that a lot of the JUHI arrangements around Australia have evolved out of past practice and as they've evolved, they've moved, as Melbourne Airport has for example, has moved to open access arrangements. Now, in Western Sydney initially because of the (indistinct) will be involved it will be trust supplied. That will (indistinct) self, more naturally into open access arrangements. Our view is that these arrangements will continue to evolve towards an open access arrangement at different places and you've seen that occur at Melbourne, in particular, but you'll also see that happen in Western Sydney as another example.

COMMISSIONER KING: Yes, okay. Now, in your submission you noted that AIP and its members support, in principle, the establishment of jet fuel infrastructure consultation forum, and you mention that in your opening remarks too, could you tell me - and you said as long it was restricted to certain types of activities, can you think of any topics or matters that shouldn't be discussed at such a forum or that should be restricted from the forum?

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MR BARRETT: Well, I think every commercial arrangements, any sort of lease or other charging arrangements, I think it would (indistinct) Western Sydney because clearly being a greenfield site, it's pretty much an open book. I think there could be some very conversations around, and there have been, around potential pipeline routes, potential volumes that the airport considers it will require, which goes then again to trucking routes that will be required in the interim. So it's really a logistic space rather (indistinct).

COMMISSIONER LINDWALL: Yes.

MR BARRETT: (Indistinct) the efficiency of the jet fuel supply into that (indistinct).

COMMISSIONER LINDWALL: All right, yes.

MR DICKENS: And just to add to Paul's comments, Commissioners, look we'd be more than happy to consult with the member companies and develop or assist the Commission with the development of the terms so (indistinct) a forum on appropriate terms. I think what we did note in our submission is that what we see to be the underlying objective of the forum has occurred and will occur quite naturally in the negotiation of new leases and you've seen that and I understand you've heard directly from companies who were privy to those negotiations but there are now clear and effective planning arrangements and triggers for investment as part of - triggers for investment in upgraded infrastructures as part of the new lease arrangements.

COMMISSIONER LINDWALL: Do you think it could address investment, coordination and planning issues that have been raised as concerns of underinvestment at Melbourne and Sydney airports?

MR BARRETT: Yes, potentially it could assist each of the companies coming up with better collective information and by companies, I mean, all participants involved so there's an agreed set of facts on the table about what potential demands there's going to be out of the airport and how individual companies can align their - not align, can decide their individual investment profile so that there is no underinvestment, as you rightly pointed out, at Melbourne.

COMMISSIONER LINDWALL: Okay.

MR DICKENS: And I think it's important, Paul, just to – I think it's important to understand that I think impressions and conclusions that have

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been reached that investment in Melbourne Airport was unlocked as result of the forum that was established there I think is flawed. I think it is very clear, and I'm sure you can test this with others, that the unlocking of investment occurred when security of lease tenure was secured. All their member companies can tell you the planned investments that were on the table awaiting finalisation of the lease negotiations can move forward, and once that occurred they've all been in play and progressed at speed.

COMMISSIONER KING: So the lease tenure, can you just expand on the importance of lease tenure and investment and do you see any role for the consultation forum in dealing with that issue or is it really just an airport by airport issue?

MR BARRETT: I'd consider that airport by airport issue but clearly underpinning those negotiations are an agreed set of facts around and it's particularly a demand equation too. In part the growth of Melbourne (indistinct) was quite substantial and I don't really – the airport itself more, the company, has really anticipated it would be as significant as it was and a forum like the consultation forum would be valuable – since then would be valuable to assist in having an agreed set of facts on the table between all parties.

COMMISSIONER KING: So to be clear - - -

MR BARRETT: (Indistinct) just - - -

COMMISSIONER KING: Go on please.

MR DICKENS: Just coming to your point, Stephen, about the link between lease tenure and investment, it's very clear that you're not going to spend the tens, indeed hundreds of millions in infrastructure investment, particularly on airport, for example in Melbourne Airport, without (indistinct) lease tenure. Now I note that most leases are 15 or 20 years in comparison to airport leases which are 99 years. So obviously you're not going to invest that sort of capital in new storage tanks, in truck unloading facilities, in pipeline augmentation without the certainty of – that'll you'll be able to earn a reasonable return on such investment.

COMMISSIONER KING: I just wonder if that's a fundamental flaw in the – and understand that historically JUHIs and the fuel system into airports has risen for historic reasons and so taking that on board I just wonder from what you've said then is it a system that in a sense is now not fit for purpose because with all the goodwill and consultation and leases end, and leases may not be renewed, you will always have issues of

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investment as leases come up and this is not unique to the fuel industry it's anywhere where you have long term investment.

Would it be actually better going forward to think about a different ownership structure of the JUHIs, so for example the system where the airport takes back control of those because that would get over this issue of investment coordination, uncertainty for the JUHI investors, you know, so is there a better way, is what I'm saying?

MR BARRETT: The first point I'd make is I wouldn't characterise it as flawed. I'd characterise it as transitioning and you'll see that emerge over time, I believe, as we've seen at Melbourne and as I think we'll see at Sydney because certainly in some of the consultations I've been involved in with New South Wales transport that has been a recognition of the need for coordination, particularly around the pipeline corridor that potentially could be put through what is, you know, heavily urbanised areas. In terms of the ownership, I don't believe the issues that you've identified – and this is me just putting my economist hat on, I don't think the issues that you've identified really warrant that.

COMMISSIONER KING: All right I think - - -

MR DICKENS: I think - - -

COMMISSIONER KING: Go on.

MR DICKENS: I think it's an airport by airport proposition, Stephen. At the end of the day most of the submissions from AIPs and JUHI JVs, and indeed from the airports themselves, have identified the JV and the JUHI arrangements as being fit for purpose and delivering reliable efficient fuel supply to quality standards into their facility. But quite naturally in all investment in this industry and throughout the supply chain tends to be lumpy, it tends to be reliant on, you know, long term government approvals, environmental approvals, lease tenure arrangements, town planning, there's just natural constraints.

And in some instances justifiably so to the expansion of (indistinct) fuels supply infrastructure. They're the challenges we face day to day and not just for jet fuel, across ground fuels as well. So I think if there is a better way then that would be something I would naturally assume would be under active consideration as part of any renegotiation of a lease between infrastructure owners.

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COMMISSIONER LINDWALL: Okay. Well Paul and Nathan I think that's great and on behalf of the Commission, thank you very much for your submission and your commentary today and have a good weekend.

MR BARRETT: Thank you very much for our opportunity to appear and have a great day.

MR DICKENS: Thanks.

COMMISSIONER LINDWALL: Now we might invite Viva Energy. I'm Paul. Come over here if you don't mind, I'll just turn this volume down. If you'd both like to introduce yourself for the record and an opening statement as you see fit and thanks for coming to help.

MR RIDGWAY: Good morning, thank you. I'm Daniel Ridgway, I'm the Chief Operating Officer of Viva Energy Australia.

MR ADAMS: And I'm Nick Adams, I'm the Viva Energy Aviation Business Manager.

MR RIDGWAY: I've got a few opening remarks, I'll try and keep it fairly snappy. So thanks for the opportunity to appear today. We'll just kind of outline a little about who Viva is and what we do, for you, and then clarify or kind of rephrase a few of our key points from our submission. So we are the operator of both the Sydney and the Brisbane JUHIs and we're also a participant in the jet fuel business as a marketer and supplier and infrastructure owner. So today we're appearing here as Viva Energy the company, but we also can make some statements as the JUHI operator in line with our submissions for Sydney and Brisbane but not outside of those submissions.

So general background, we're listed in Australia. We're an Australian company in the ASX 200. We were originally formed when Shell Australia sold its business in Australia to a private consortium in 2014. But the business in itself has been operating in Australia since 1907. So 112 years and we're very proud of that. The business covers commercial B2B fuel sales, retail fuel sales under the Shell brand, our refinery in Geelong and the aviation business which we purchased from Shell in 2017. Moving on to kind of how the fuel business works and I guess our role in it, so obviously being in the industry for a long time we've built up quite a lot of fuel supply infrastructure.

So we hold pipelines, we hold import terminals, we're participants in a number of JUHIs around the country. Since the closure of several refineries in Australia, which has been well documented, we've gone from eight

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refineries down to four in the last decade and a half. Australia is a large net importer of petroleum products and that includes jet fuel as well. So whilst we manufacture some jet fuel at Geelong Refinery, we import around 40 per cent of our jet needs. The results of that, along with the other participants in the industry importing jet fuel, is that jet fuel is priced closely in line with international pricing benchmarks.

So the reference price is the import parity price, which is what we refer to as a Singapore Platts price or sometimes referred to as Mean of Platts or MOPS price. As we outline in our submission, adding on that Platts price plus transport, those two elements are about 95 per cent of the end user price for jet fuel, typically in Australia and the remain covers infrastructure, insurance, (indistinct) into-plane services and any marketing marginal return on capital.

So in terms of the marketing business for jet fuel and Australia. We place competitive bids in tenders, which the airline air operators put out periodically. Businesses typically tender for contracts of between one and three years, depending on the operator and what they're looking for and that market, we believe, is very competitive.

In general, the fuel jet marketing business in Australia is characterised with low margins, driven by the need for high volumes to drive efficiency of scale in a fairly high, kind of, fixed cost investment environment. Price is an important factor in negotiations to sell jet fuel in Australia, but there are other important factors in particular, track record around supply reliability. And product quality. Product quality being a very key issue in the jet industry as you can imagine.

In terms of supply security, we invest heavily the supply chain to ensure that and that's an ongoing discussion with our customers both as an upstream operator/ marketer and as a JUHI participant. And obviously airlines are looking for supplies that can guarantee them reliable supply at the airport. We believe that the track record of the industry in supplying jet fuel reliably in Australia is exceptionally good as evidenced by the lack of disruptions due to fuel supply issues. And we have a number of major investments which we've made in the last decade and we have a number more that we're progressing at the moment.

You've briefly touched on it in the last session with AIP, we have seen the issue at Melbourne Airport recently in terms of a hindering of investment. We agree with the view that that's largely being driven by lease uncertainty in terms of the tenure going forward and that the new arrangements have unlocked that issue and there are significant plans for investment now underway.

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Another area of focus of your draft report, which we covered in our submission is that access to JUHI infrastructure in Australia is available on appropriate commercial terms and those terms, we believe, reflect the past investment that have been made by participants in those JUHIs.

There have been several (indistinct) applicants to enter JUHI, particularly in Sydney over the last 10 years. And for those who chose not to go ahead with those applications, the number 1 reason was lack of tenure on the outstanding lease in Sydney.

And so finally, in respect of our participation in the supply of jet fuel and as a supply partner to Australian and International Airlines, we are concerned by any recommendation by the Commission to introduce regulations which might limit our ability to operate efficiently or that might provide supplies not currently invested in the supply chain with an unfair competitive advantage.

But with respect to the recommendation specifically in the draft report, around open access for Western Sydney, and the jet fuel coordination forms, Viva Energy is supportive of those recommendations. Thank you.

COMMISSIONER LINDWALL: Thank you very much (indistinct words). If I can ask about the lease terms. Not the terms but (indistinct) duration. How many years do you think is the minimum to make a lease for investment in a major Australian Airport viable from an investment perspective?

MR RIDGWAY: It is a little bit difficult to judge that generically because it would depend a little bit where you are in the investment cycle. So if you've just built a brand new airport with infrastructure that might be quite fit for purpose, I don't think you necessarily need as longer tenure. But you might, I guess, generically consider that you don't want to end up being quickly always in a cycle of coming up towards wanting to renegotiate terms. So I think from our perspective, 10 years plus makes sense in terms of tenures and maybe longer if you're facing a very significant investment at the commencement of the lease.

COMMISSIONER LINDWALL: So when you've made a – say it's a 15 year lease, as you're coming up to them near the end, that must make you quite uncertain because you're getting quite close to the end and you don't know what the airport owner wants to do after that. How far in advance of the end should negotiations commence for what might happen after this and - - -

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MR RIDGEWAY: I think it depends a little bit on the terms of the actual lease and what is documented in terms of what happens at the lease. As you might imagine, some of the past JUHI leases were written a very long time ago and may have different arrangements for how the lease is wrapped up and, indeed, what compensation, if any, the JUHI receives for the lease terminating. So it's kind of – again, not wanting to be unhelpful, but it probably does kind of vary based on that, but I think in general, there usually is a good shared understanding by the airport and the JUHIs of the need to try and negotiate years prior to the end of the lease. And that only tends to not work effectively if there's, you know, a disagreement on either the high level direction, the new lease should take in terms of roles and responsibilities or the terms.

COMMISSIONER LINDWALL: So if say, hypothetically, a lease is expiring in two years and the airport operator wishes to buy it out, you strike a price for it, right, and then you would continue operating until the end of that two year period. There wouldn't be any incentive to run it down or something, over that period, do you think?

MR RIDGWAY: Yes, so it might be the case that a JUHI agreement already has those terms in it that says if it expires, the airport will buy the assets at this kind of valuation but it wouldn't usually be a fixed dollar number. It might be a number relating to book value or written down values or whatever and so that may still provide incentives right up until the end or it may not, depending on how it's phased.

COMMISSIONER LINDWALL: But when you were saying earlier in your comments that some participants, particularly in Sydney, have tried to enter the market, but they were – they were put off, if you like, because the expiry of the lease or the lease term remaining was too short. In a way, that's a bit odd, because all they're doing is providing supply into an infrastructure. The infrastructure, presumably, will still exist and the price at which they would enter surely would reflect that there's only a short period of tenure remaining. It wouldn't be a high price, surely, for a long period, which when there's only a couple of years to run - - -

MR RIDGWAY: Yes, I don't think I can tell you the actual terms on which the current JUHI agreement in Sydney allows new participants to enter. But I think you can assume from the actions of the people looking to enter that it's clearly not commercially attractive to buy in if you only have a short period of time to kind of make that investment back.

COMMISSIONER KING: Okay. So just I guess to follow up on that point. Do you know if in Sydney, JUHI arrangement, the previous one, or the existing one (indistinct words).

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MR RIDGWAY: No, existing one.

COMMISSIONER KING: In the existing one. What the buyback arrangements are if a new agreement isn't reached? So on what basis Sydney Airport will buy the facility back?

MR RIDGWAY: Yeah, I don't think I'm able on behalf of the JUHI to disclose what those commercial terms are.

COMMISSIONER KING: Okay. Okay.

COMMISSIONER LINDWALL: What about putting it another way then. I'm a potential – I want to supply fuel to Sydney (indistinct) operator, what can you tell me a bit about the process that I would have to go through to – you don't have to tell about a particular terms obviously, but what kind of process would I have to do and what would you want to do to verify that I'm a bona fide (indistinct) entrant?

MR RIDGWAY: You'll have to forgive me, because I'm fairly high level, given my role, but in high level terms, you would have to write and express your interest to want to join. You would have to meet the requirements in terms of capability to be a participant from a technical and financial perspective and then you would have to pay to but your share on the agreed or the documented kind of formula for buying a share in the JUHI.

COMMISSIONER LINDWALL: Where did the – again, I'm a potential new entrant to supply fuel. It would be difficult for me, presumably to go to, you know, Qantas or Virgin and agree a price when I don't already have access. So I presume that the sequence would be that I have to, first, do that and then bid for Qantas business or Virgin business.

MR RIDGWAY: Yes and no. It might be one that Nick can expand on a little bit more but, you know, it's probably not correct to fixate that you have to be a JUHI member to sell fuel in any of the airports in Australia.

So in Sydney for instance there are participants who are selling to airlines without being a member of the JUHI. Maybe you can speak a bit about that, Nick.

MR ADAMS: Well, and you're right. Working back from the customer, I mean one could put an agreement in place with an airline to sell them fuel. But there are a number of other aspects of a competent supply chain which would need to be established and recognising there's a focus on the JUHI.

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The genuine new entrants would also need to establish a hydrocarbon supply chain, they would need to land that product, come across a wharf into storage. They'd then need to have a physical route into the airport as well. And those agreements, be they ownership or through a third party arrangement also have a term. So having confidence at each step is actually what builds up into a supply chain.

So it might not be that it's purely around the JUHI, but if you can have a longer term arrangement at that step that opens up your confidence to build your supply chain.

MR RIDGWAY: But if you think about it from a Sydney perspective, and there is a player doing just this, as well as our import terminal and Caltex import terminal, you have the Vopak which is an independent tankage terminal. You can rent space in a tank at Vopak; Caltex's path line system to the airport auctions off pipelines space periodically, and then one of the JUHI participants is Qantas.

So if you wanted to go to Qantas and say, "I'm open to supplying you at the airport," you could, in theory, throughput through Qantas' JUHI ownership.

COMMISSIONER KING: Of course. That's right, yes.

MR RIDGWAY: There's, then, an into-plane service company which is pooled among multiple players and, again, Qantas is one of those players. So really all you would need to do is go to Vopak, get a price, buy some time on the pipeline and do a deal with Qantas.

COMMISSIONER LINDWALL: Now, Western Sydney Airport is due to open in 2026, initially, at first, I imagine that there will be trucking in fuel. How much volume do you think you need to justify building a pipeline roughly speaking?

MR ADAMS: It's difficult to say. I mean I think the evolution of most airports and even some quite mature airports can rely quite well on trucking.

COMMISSIONER LINDWALL: Yes.

MR ADAMS: There might also be public policy inputs which detract from wanting to truck, taking trucks of the road for example. But it's a bit of an intuitive process and we'd need to - you know, I think the Western Sydney Airport program which I think was a very good program in terms of consultation and so on recognising needs, would need to select a route and the pipeline price would need to be established and kind of work back from that.

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But typically many hundreds of millions of litres would be normal and, of course, it's quite a way away from the coast so the pipeline would be relatively expensive compared to the current arrangement.

So difficult to answer and it's not necessarily purely economic inputs in to the decision and even - - -

COMMISSIONER LINDWALL: Yes, there could be such (indistinct).

MR ADAMS: And the planning can take a considerable amount of time as well. So in discussions around tenure, the real estate arrangements around a pipeline can also be quite complicated because it's an asset that can't be repurposed very easily.

So I mean we do some modelling of course. We don't believe there'll be need for a pipeline initially, but because the time lead to develop it means that you might actually be planning from the outset anyway. So I think it will just be a case that eventually it will need one, it's more maybe driven by the planning process to when that gets kicked off.

COMMISSIONER LINDWALL: And environmental concerns, yes.

COMMISSIONER KING: So on Western Sydney you've said you're supportive of open access at Western Sydney. Well, there's different models for open access. Which model of open access do you think should be introduced at Sydney? So if we were to make a recommendation, not just that there should be open access, but there should be open access of the following form, what would you like to see us do?

MR RIDGWAY: I think without getting too much into the details, we believe that what's important in open access is that there's still an incentive for people to invest in infrastructure because new entrants coming after investments have been made to pay their share of that investment. Establishing kind of what that return rate is is kind of probably the bit that needs quite some detail that we couldn't necessarily land today.

We also think that it's important that that open access involves some kind of qualifier around the technical capability of the participants and their financial standing as well. But mostly of the technical capability, especially with respect to product quality which is a massively important safety issue in the industry.

COMMISSIONER LINDWALL: On quality, does that imply - I would've thought – maybe you can correct me here – that all of the fuel

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suppliers that you can imagine that would be in Australia would have the same type of quality standards, wouldn't they or are there potential new entrants that don't meet those quality standards?

MR RIDGWAY: Well, I guess I'm just imagining for the avoidance of doubt.

COMMISSIONER LINDWALL: Yes.

MR RIDGWAY: I mean if you think about say the terminal gate legislation in Australia, it pretty much just says you have to sell to anyone who rocks up in a terminal gate if they want to buy petrol and diesel, I think that you wouldn't want to have such a broad regime and then participants should have to comply with a recognised quality standard.

COMMISSIONER LINDWALL: Quality standard, yes, fair enough.

COMMISSIONER KING: The sort of investment issues that you've raised seem to be because of the ownership of the JUHIs. So we have that separation between the airport and the JUHI ownership. So there's always going to be a lease ending where there's always going to be issues about lease tenure and so on.

Would a better system for Western Sydney be that the JUHI infrastructure is owned by the airport and the actual investments are then made by the airports, with fuel companies having access to that infrastructure?

MR RIDGWAY: Just, firstly, I would say that, although we've kind of highlighted that the Melbourne lease and the Sydney lease endings have created some challenges in terms of continuous investments at the airports, I would also say that if you do look at Melbourne, we've maintained a pretty effective supply chain during that period and now are investing for the future and have already put some new assets into the airport. So I wouldn't characterise it as like entirely unsuccessful regime in terms of making sure that we supply our customers.

In terms of say a brand new airport and whether it would make sense to have its fuel assets owned by the airport, I think that is a possible model that can work depending on how it's done. I think there's probably a couple of challenges that need to be overcome.

One, is often the airports themselves lack the technical capability to design and operate specific jet fuel infrastructure. So even some of the airports that have looked to own the infrastructure, are then looking for a partner to kind of help them design and operate. So that's kind of our experience in

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any case save for the capability and core business kind of question for the airports.

And then the second thing that needs to be managed I guess is how the airport then prices access and the return from that asset and ensuring that remains competitive for the end customers.

COMMISSIONER LINDWALL: I've been told a few times that there's been a strict separation between operations of JUHI and the actual supply through the JUHI. How, in practise, is the separation managed and ensured?

MR RIDGWAY: I can probably only speak for VIVA in that case.

COMMISSIONER LINDWALL: Yes, of course.

MR RIDGWAY: But we do operate two of the major JUHIs. So, organisationally, we're set up with a - market organisation, under a general manager for marketing, and then Nick, who heads up our sales team within the marketing organisation, kind of sits under that organisation, and that reporting line goes up through the GM of marketing to the CEO of our organisation, and then within my team, I have a supply chain team, and within that team I have a - a jet supply chain group, which is headed up with a person who oversees our JUHI operating role, and so it is one of the things that the industry has, I think, quite good discipline on, in the fact that, say, that person will be very clear on saying, for instance, our submissions to your commission, through - they would have been pulled together by our representative in that team.

They haven't been shared with Nick prior to being submitted. If he wanted to see them, he would have had to download them from your website, and - and minutes of those JUHI meetings, all those kind of things, the information is shared, kind of, equally across all the members. But it's not shared in any special way back into Viva's marketing team.

COMMISSIONER LINDWALL: Now, when an airport, say Sydney, wants to build new tarmac and parking lots for planes, and hybrid facilities to those new parts, and the JUHI's got, say, four - four members, and three of them agree and one of them disagrees, how do you break a deadlock like that?

MR RIDGWAY: Yes, I mean, it is something that, usually, the - if it's a simple of case, of, "All right, we need to move from here to here," and, you know, "This is how the airport wants to do it, and when they want to do it." I think it's unusual that different members would see that differently, right, because the incentives are usually reasonably well primed, and even on new

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investments, I haven't particularly seen is as being a problem, but I'm not involved in the - in the day to day, but I don't - I don't think it's usually that problematic to get alignment within JUHI memberships.

And probably a little bit of that is the way the commercials tend to work, in that it's the users of the JUHIs who paid it - who pay the price. So, if you're not using it, then you get - typically, don't pay.

COMMISSIONER LINDWALL: But you might be asked to make some new investments as a member, though. (Indistinct).

MR RIDGWAY: But then you get - you'll usually get some return on that for the people who are using the investment.

COMMISSIONER LINDWALL: You'd expect so, yes. Sorry, Stephen.

COMMISSIONER KING: Just coming back to the structure of the JUHIs, where you do have competitors participating together, in the JUHI. Even where there's Chinese walls, competition regulators tend to get very nervous about competitors having joint ventures. The potential for conversations around a board table, or in meetings, can perhaps stray in to areas that would raise competition concerns. Now I'm not - now, I want to make it very clear, I'm not suggesting that any of that happens. But what I would like to know is why should we be assuaged that this joint venture doesn't raise competition concerns?

MR RIDGWAY: Yes, I guess I'm kind of struggling to see how it - how it could. I mean, typically the people involved are operational people, in the supply chain, with, kind of, no roles to play in the selling or marketing of fuel, and the JUHI's not involved in that side of the business at all, and secondly, if you look at the way the - the airlines buy fuel in any case, it's a pretty, kind of, aggressive tendering process, with sealed bids, and so, I just - I kind of don't know how it would be a problem.

COMMISSIONER KING: Okay. The Airlines have actually suggested on the tendering side that they find it very difficult to actually get competitive tenders, that often they'll have only one or two companies tendering, but often the tenders won't be for the full amount of the fuel required by the airline at a particular airport, so why are we getting - you've said it's a very competitive process. The airlines have said, well, they don't see that. Why that difference?

MR RIDGWAY: I might leave that one for Nick.

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MR ADAMS: Well, there's quite a broad spread of how tenders are placed. So, I mean, there's an international side to it, there's a domestic side also to be worked with the airlines who are based in Australia. But, sometimes an airline will want to split their volume. So, a tender might be - you might see the whole tender. Other times, we have to submit a supply cover request. So, can we actually accommodate additional volume throughout infrastructure at that point in time.

So there's a number of reasons why a supplier might not tender in that way, and of course putting the product into wing, on the airport, there might be nuances between - it's sometimes off a hydrant, which is quite a vanilla way of delivering fuel. Sometimes it's a bit more specialised, so it's away - it's a stand, which is away from the hydrant, it's a truck delivering, the truck availability, rather than investing in trucks.

So there are a number of reasons why a tender might not cover the full volume. But as far as competitive terms are concerned, I mean, business does change hands a lot. So, we might supply, let's say typically, for an international tender, we're supplying fuel, take Sydney for example, to a customer. It might be for 12 months, maybe for longer, and then there's another tender, and we lose it. So, volume is always moving around as well.

So there is evidence to show that there is competition in that space, and an into-plane - there are also different in inteo-plane, in terms of what service levels that the companies will provide. So there might be some more interaction with the aircrew, which is of value to the airlines as well. So there's a few pieces which come into play there.

But on the point about how the JUHIs work, as well, anybody who's worked in a JUHI, and is then coming out - so, if it's a Viva employee who's working there, and is then coming out of that organisation, to go back into a Viva role, they have restrictions around what they can do, as well. So there is a- it's within the fabric of a JUHI employment structure, that folks coming out of those organisations do have restrictions on what they can do inside Viva going forward.

COMMISSIONER LINDWALL: So when there's, say, four operators - sorry, four owners of the JUHI, and one of them's the operator, how is the operator - how do you determine who the operator will be?

MR RIDGWAY: That's determined by the members, but it - - -

COMMISSIONER LINDWALL: Does that change much?

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MR RIDGWAY: It doesn't usually change, but it could change, if - and I think it's probably more driven around, kind of, technical and operating competence than any other factor. So, I think to drive a change, it would probably need the members to agree that there was someone else who was better placed to operate the - the asset.

COMMISSIONER LINDWALL: But there's a - - -

MR RIDGWAY: And some members will - will have no interest in being the operator, because it just brings some kind of operational complexity and distraction, when things go wrong. There's not really any - any commercial reason to be an operator.

COMMISSIONER LINDWALL: So, no competitive advantage for - as a supplier, to be the operator?

MR RIDGWAY: Not particularly, no, and that's why typically most members are happy for the status quo.

COMMISSIONER KING: Just two things - - -

MR RIDGWAY: Sorry, and that - probably that probably relates a little bit to even what I was saying before, where an airport wants to own the asset, or have a single operator of the asset, typically other - other players are still happy to participate under that arrangement, and there's not really any commercial benefit in that, either.

COMMISSIONER KING: So, just two quick things I wanted to cover off, because I'm aware of the time, and apologies, because I cannot remember exactly who's given us which information, but as you mentioned, there's churn in terms of the contracts. Have you been able to provide us with that from Viva's perspective, their contracts going, contracts lose information? Presumably I mean it's confidential, but - - -

MR RIDGWAY: Well, we haven't - we certainly haven't done that. It is super market sensitive, I mean, that's the sort of stuff. But we've given a synthesis, if you like, of the cost build up, and, you know, what's built it, it's in words and the pictorial form. That's as far as we have gone with that.

COMMISSIONER KING: Are you able to able to provide us some sort of churn information, even - you know, it doesn't need to be names of airlines or anything like that. You don't need to say, because you may not know, who you won it off and who it went to but just, you know, "Airline A at Airport X; won contract this volume; lost contract a year later", that sort of thing, to show us that (indistinct) with - - -

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MR RIDGWAY: I think - can we just take that on notice as we might be able to do that in the (indistinct).

COMMISSIONER LINDWALL: Thank you. And the other thing: you presumably heard me comment on the fuel throughput levies and it is an area that we're trying to work out because there do seem to be very different opinions, your view on fuel throughput levies?

MR RIDGWAY: So again my understanding is reasonably high level but, as I understand it, those are levies charged to the JUHI for five year airports and the JUHI typically passes those costs on to the fuel marketers and whilst I'm not able to tell you whether they are ever changed or introduced with lease periods, my understanding is they're more or less static within leases but I'm not 100 per cent sure if that's always the case.

COMMISSIONER LINDWALL: When a new entrant tries to say enter Brisbane JUHI and you go through that process of bona fides and checking on setting the price law for the rest of that, are they buying someone else's equity share or they become - say if there is four, they became one fifth of the owners now; is that how (indistinct) happened?

MR RIDGWAY: Yes, it depends on the agreements and because some of them are quite old they might be more or less having different arrangements but, to be clear, they would get a new share as opposed to having to buy someone out.

COMMISSIONER LINDWALL: Yes, okay. Now, BARA yesterday suggested that its preferences of workable access arrangements, they were commercially determined rather than set by a regulator, and that airlines and airports are given consultation (indistinct) or what do you think of that type of comment that BARA made?

MR RIDGWAY: So in what context? Workable access to what?

COMMISSIONER LINDWALL: To the JUHI's access, as far as I'm aware, do you remember exactly what they said?

MR RIDGWAY: Sorry, not off the top of my head.

COMMISSIONER LINDWALL: No, we might have to - - -

MR RIDGWAY: I'll probably reiterate our point which is by and large we're happy to exist in either an open access arrangement or some of the existing legacy JUHI arrangements, we think both of them generally

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provide significant competition and access for new players, as the Sydney JUHI has shown where you have people throughputting off other people's shares so the boundary condition for us is really that if there is an open access arrangement or there is airport operated assets, there's still the right incentives for making the investment and getting a capital return which is neither excessive, in the case that it's been passed on to customers, or too low (indistinct) investment.

COMMISSIONER LINDWALL: Could I just confirm that if any of the airport's views to (indistinct) open access that has been (indistinct) request of Sydney, that Viva would actually consider that there's no problem with you actually bidding for business there?

MR RIDGWAY: On the basis that I've just outlined, yes.

COMMISSIONER LINDWALL: Obviously you're got to get the right price.

MR RIDGWAY: Yes.

COMMISSIONER LINDWALL: I think that's great, thank you very much.

MR RIDGWAY: Thank you. Thank you for having me.

COMMISSIONER LINDWALL: Could I invite BARNZ, Justin Tighe- Umbers to the table.

MR TIGHE-UMBERS: Hello, good morning.

COMMISSIONER LINDWALL: If you wouldn't mind, Justin, just introducing yourself for the record and an opening statement will be fine.

MR TIGHE-UMBERS: Good morning. I am Justin Tighe-Umbers, the executive director for BARNZ, The Board of Airline Representatives New Zealand. Firstly, I'd like to thank the Productivity Commission for the opportunity to present at the hearing this morning. I'd like to make an opening statement for about ten minutes and then we can move on to any questions you may have. I'll start off by giving a little context on our organisation and why BARNZ is here presenting today. We represented 29 airlines that fly from New Zealand, which is virtually all of the major airlines, including Air New Zealand and Qantas and pricing consultations with airports and capital plan negotiations, BARNZ represents the 27 international airline members while Air New Zealand and Qantas group represent themselves directly.

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One of my roles is to negotiate with Auckland Airport, their capital planning forum which is tasked with agreeing requirements for the current $1.8b capital plan as well. So why is BARNZ here today? Simply put, the Australian approach to infrastructure regulation matters for New Zealand. It is a fact that New Zealand policy makers and regulators look closely at Australian examples and innovations and this is just as true for airport regulation as other sectors. Equally I appreciate that the Productivity Commission is interested in what it can learn from New Zealand as evidenced by your visit last year, Paul. Listening to the hearings yesterday, it's clear that the exact same challenges exist on both sides of the Tasman. The recent New Zealand experience of airport regulation has direct relevance to the Productivity Commission draft report and I think challenges some of the conclusions in that report and I'd like to go through some of those examples today.

I'm sharing this experience not because I believe that New Zealand is somehow a shining exemplar of airport regulation, but rather to illustrate how New Zealand's limitations and failings, and improvements, could be used to enhance airport regulation in Australia for the benefit of travellers in the airlines, and I'd argue ultimately for airports themselves as well. I'm here today because a positive outcome in the Productivity Commission report can assist the development of better regulation for airlines and travellers on our side of the Tasman. At this point I'd like to note that my comments today are in the context of the three major airports, that they can account for the vast majority of airport revenue and are most relevant to the big four Australian airports so they don't apply directly to the regional airport situation.

I'll talk briefly about the airport regulatory settings in New Zealand and then the lessons that can be drawn for the Australian contexts in relation to the draft report's findings. As you are aware New Zealand has an information disclosure regime for airports. That involves the airport publishing detailed cost revenue and capital return information at each five yearly pricing decision. That's then reviewed by the regulator against predetermined benchmarks and, in particular, a reasonable rate of return and the regulator then publishes its report. Airports are free to decide whether, and if so how, to change their prices in response to the regulator's reports. In the New Zealand system there are four levels of regulation that can be applied. At the lightest end information disclosure, which is what we have today, and then through to the tightest end which is price regulation and my background comes from working as a regulatory manager in telecommunications which is price controlled, which I can assure you is a very heavy-handed form of regulation from that experience.

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Negotiate-arbitrate is actually only the second rung on that ladder. It's built into our Commerce Act - so specific measure there in the regulator's toolbox. It's by no means considered heavy-handed regulation by the Commerce Commission as it's at the lower end of the options available and in fact the next one up the rung from where we are today. The Productivity Commission's draft report does not recommend the adoption of the New Zealand approach or, in particular, the benchmarking approach in Australia and I think this would be a missed opportunity.

The setting of benchmark returns in New Zealand has had a positive effect in reducing the magnitude of supernormal returns by airports though I note there is still some way to go. Over time we have seen a trend of the benchmark returns reducing. In 2012 airports were trying to set the returns at the 75th percentile of the WACC range and in some cases even higher. Today, after some years of legal and regulatory debates, the airports' targeted returns are much lower saving your travellers a great deal of money.

So in the latest pricing round that we've just completed with Auckland Airport, they initially sought to recover a 65th percentile return on the invested capital and following strong criticisms from airlines, Commercial Commission and the Commerce Minister himself, they returned this to the 55th percentile. Christchurch Airport sought a return close to the regulator's benchmark and the regulator decided that that was reasonable.

So I take you through this brief history to highlight how having a benchmark rate of return has been instrumental and resulted in better outcomes for the travelling community. It serves to contain disputes into a tight scope and provide an agreed reference point for parties to work from.

The Productivity Commission rightly notes establishing a benchmark return regime is complex. In New Zealand's experience, we found that after the very robust contesting of the initial methodology and decision, subsequent decisions by the Commission have not been challenged. So there was a religious war around how to actually establish WACC and all of the machinations there. Once that methodology was agreed, the debate then moves on to whether a departure from the midpoint for an airport is actually justified or not. So it's a much more contained practical discussion, rather than getting into the intricacies of WACC.

The result has delivered significant consumer benefit; $66 million has been, or will soon be, returned to airlines and travellers as a direct result of the benchmark return process and I believe the mere fact that a benchmark even exists is instrumental in driving better airport pricing decisions from the

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outset and pushing them to set prices that are more reasonable there or even before the regulator holds their review.

The reductions in excess of returns by airports couldn't have been achieved without the comprehensive reviews and benchmark and by the regulator. That said, the benchmarking process is inefficient. It has involved over a year of wrangling between the airlines and the airports and a good deal of submissions and cross-submissions, back and forth to the Commerce Commission and this is also after the fact that the prices are set and the airlines and passengers are paying those rates. It is far more efficient to negotiate on an equal footing and to work to an outcome that is acceptable to all, with recourse to arbitration if needed.

Airlines don't have countervailing power to drive better outcomes from airports; I haven't seen any evidence of this at play in New Zealand. At the international airports, Auckland enjoys very similar geographic monopoly position to Sydney Airport, as you know. There's simply no other way to get to the upper north island. Travellers wanting to go to Auckland don't have any realistic alternatives. International airlines can't just simply withdraw services to take them to another airport in New Zealand, as they face a far greater challenge actually filling the aircraft from the smaller catchment areas. So typically, in that instance what they'll do is just withdraw service from New Zealand altogether.

We have actually seen two airlines this year pull out - AirAsia X and Hong Kong Airlines - do that rather than move anywhere else. This, of course, harms competition and I'm aware of some of the dynamics seen at the major Australian airports as well.

Like many of my industry colleagues, I am very surprised that the Productivity Commission draft report concluded there is no evidence that airports in Australia systematically exercise their market power to the detriment of the community. I beg to differ and I just point to the evidence that has been presented through A4ANZ and Air New Zealand's submissions, that were acknowledged in the report by the Commission.

There can be many ways that a monopoly can abuse their market power, some subtle, some less subtle. I will give two contrasting examples from New Zealand that I think help illustrate this point. Auckland Airport has some of the highest profit margins in the world and over an extended period, they've maintained their policy to return 100 per cent of net profit after tax through to their shareholders, while deferring some major capital investments - to the detriment of consumers.

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The reductions in the cost of capital that I mentioned before are welcome but have done nothing to change this dynamic of market power. In Wellington, ironically, we've got the exact opposite problem, which is one of over-investment. Wellington Airport proceeding with preliminary work to invest in a $300 million runway extension, in a bid to turn it into a long haul destination that none of its airline customers, that I'm aware of, want. So we've got two quite contrasting - - -

COMMISSIONER LINDWALL: Isn't it the council that wants that?

MR TIGHE-UMBERS: The council?

COMMISSIONER LINDWALL: The council, the local council of Wellington, I think that's what - I had the impression – sorry I'm interrupting you.

MR TIGHE-UMBERS: No, that's all right.

COMMISSIONER LINDWALL: I had the impression that it was a governmental thing, rather than the airport itself wanting to do that.

MR TIGHE-UMBERS: No, no, it's very much the airport driving the investment and I think looking to convince some councillors that it will deliver fantastic benefits for the region, so there's some councillors who's ears have been bent, is how I'd characterise it - but it's not a push from the region.

Both of these examples are as a result of airports having and exercising market power and as we heard yesterday, you don't have to look far for similar examples in Australia - although I admit they're a little bit more colourful over here, in the form of a koala enclosure - we can't claim to have one of those in New Zealand. While the information disclosure WACC benchmarking and building blocks methodology provide a clear framework for airline/airport negotiations, it is still far from a level playing field; the power and balance between airports and airlines persists.

Under New Zealand law, airports can simply charge as they see fit and the Commerce Commission has no ability to intervene any airport pricing, only report on it within the constraints of information disclosure. If it chooses to go beyond that point, it needs to make a recommendation through two of the ministers. So airlines consequently, are reliant cap in hand, on monopoly airports behaving well.

So what is the way forward? As you know, a successful infrastructure regulatory regime strikes the balance between adequate incentives for

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timely investment at a reasonable rate of return, on the one hand with fair pricing and service quality outcomes on the other. This is exactly what airlines want on both sides of the Tasman. There is no objection to airport investors making fair and reasonable rate of return and in fact, as you know, airlines are completely dependent on that investment being made at the right time in order to be able to grow their businesses.

IATA has forecast that the international passenger numbers are going to double by 2036. In order for an already stretched aviation system to cope with this, airlines and airports are going to have to work closer together than ever - and that means that a trust-based relationship is going to be increasingly crucial and it's just not possible to build that trust when one of the parties holds the majority power.

So I believe regulatory settings should be working towards an environment that enables trust to be built, rather than leaving airports with significant market power and crossing fingers that they don't use it. The irrational economic players, in the end they will, as far as they can. The Productivity Commission is rightly focused on the cost benefit test for introducing new regulatory measures but I'd say you also need to consider the cost of not addressing the current power and balance and factor that into the equation.

I believe that if airports and airlines are going to be adequately placed to cope with this doubling of passengers, there needs to be a regulatory model that incentivises sound commercial negotiation and as backstop, by regulation. I found it a bit amusing yesterday watching airports argue on the one hand that there's simply no need for a negotiate/arbitrate model but on the other hand, saying that they're concerned about countervailing powers from airlines, so it leads me to say well why would they not want an arbitrary backstop - because arbitration cuts both ways. The only conclusion I can draw from that is that airports fear a level playing field and having to surrender some of their market power that they currently enjoy.

From a New Zealand context, we've got extraordinary capital build underway at Auckland in the next decade, including a new runway. That is going to require airports and airlines to work closer together than ever before, if it's going to be managed successfully. Similar points apply in many of the Australian airports.

Addressing the current power and balance is critical to allowing such closer relationships to happen. Trust-based commercial relationships can only be truly established if both parties have adequate commercial leverage. We agree with our airline colleagues in Australia, that negotiate/arbitrate is the way forward and we're also calling for this in the context of New Zealand's regime as well.

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What are the useful conclusions that the Productivity Commission could take away from the New Zealand experience? Well how a benchmarking regime can establish tight parameters for airports and airlines to agree appropriate returns and over time, reduce supranormal returns. Information disclosure or price monitoring is still a limited regime, monopoly airports are incentivised to maximise their returns up to the point of regulatory intervention and this something they've consistently done.

A successful regulatory regime needs to go further than just simply assessing whether market power is abused. In today's environment of record growth rates, it needs to be forward thinking. To incentivise the airports and airlines to work closely together to build costly airport infrastructure, which is of critical strategic importance to national economies, regulatory models need to address the current power and balance. Moving to a commercial negotiation model with a regulatory backstop, I believe is critical to airports and airlines both here and in New Zealand in being able to meet this doubling of passenger growth in our region into the 2030s.

They are just the initial points for the debate, thank you.

COMMISSIONER LINDWALL: Thank you, Justin. Could I ask about a couple of things on that. Of course, I remember that Professor Samuel, when he was over at Auckland Airport, said that it was - it had been run down in policy and - well on my own experience that perhaps with some investment it could be better, I suppose, in terms of terminal. Could that not be described because the WACC is too low and that therefore there's a disincentive to invest in that airport?

MR TIGHE-UMBERS: No, we haven't - we haven't seen evidence of that and in fact that's - a lot of this predates the WACC benchmarking regime. I think particularly if you look at the shed that is the domestic terminal there, it's a 1960s building which the airport freely admits just hasn’t managed to keep up an investment. So I think it is quite a historical situation. If anything, the airport now is - is really scrambling to catch up with the investment it needs to, and there's no disincentive around the WACC from their perspective. I think they're probably concerned that they've got too much to invest in and how are they going to actually smooth that from a pricing perspective for airlines, but also manage their own cash flow.

COMMISSIONER LINDWALL: In terms of the benchmark WACC, is that just for aeronautical services or also for non-aeronautical services?

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MR TIGHE-UMBERS: It's just for non - sorry, for aeronautical services. Yes. So it doesn't apply to all, so some of the conversations yesterday around, you know, Mercedes dealership wouldn't apply at all. Which is good, it simplifies those conversations.

COMMISSIONER LINDWALL: Do you think that there's another way of comparing New Zealand to Australia is that we have effectively individualised contracts between airlines and the airports; whereas I understand you just have the single contract between an airport and all the airlines. Is the Australian model better or worse than the New Zealand in that respect?

MR TIGHE-UMBERS: Look, I think they're just different and that's largely back to the size difference. So in New Zealand you get a situation where the vast majority of assets are common assets. We just simply don't have enough throughput to justify an individual terminal, for example, for an airline. I guess you could say it simplifies it for New Zealand.

While it is a common price book that we negotiate to, there are still individual contracts that airlines will undertake with the airport if they want; their own lease spaces or, you know, premium check-ins and those things. So I think we've got the flexibility there for both sides, but the common pricing model is a good, a good level playing field, if you like, to help the airport satisfy the needs of a broad range of customers, so you've got the full spectrum of airlines and those conversations tend to flush out through the common price book.

COMMISSIONER LINDWALL: In New Zealand, with the benchmark WACC, I can't see why you'd need negotiate-arbitrate as that would surely lead the airport and the airline to reach a WACC that they both agree with and by definition it's been set as the benchmark.

MR TIGHE-UMBERS: Yes, I think the reason we still want that is because ultimately it comes back to - there's two things, the inefficiency of the process, so you're having to do it ex-post as well, and you know we've gone through a protracted - really the whole pricing regime three years of fighting to get money back that you can argue was the airlines' in the first place, when you're looking at other recoveries that the airport has put. So that's a frustration, it's highly inefficient, but then also, you know, you look at an example like the Wellington Airport runway. You've got no ability to countervail that, so whereas if you have a good negotiation around what's required from the airlines and then you reach an impasse on that, then you have that backstop that you can fall back on. And I think, look, I don't think either parties want to rush to using that backstop. It's there. Because there's uncertainty at the end of the day with an expert arbitrator, and I just believe

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that the motivation there is to get as closely - equally disappointed as you can in the outcome, but as close as you can to where you're both satisfied without having to put it in the hands of an arbitrator.

COMMISSIONER LINDWALL: In New Zealand, just one more question. In New Zealand are there examples where negotiate-arbitrators are used in other industries?

MR TIGHE-UMBERS: No, look I don't believe it's been tested in other infrastructure. Certainly not in telecommunications. I could be wrong on energy but I don't think it has, so it would need to be developed, yes.

COMMISSIONER KING: As you note in some of the discussions yesterday, so around the negotiate-arbitrate, we're just thinking of how it would work. For example, in the case of Wellington Airport and the runway, which is obviously a common infrastructure, in that case you said that no airlines were supportive. But if it was the case that some of the internationals were supportive, perhaps Air New Zealand said, "No, we're not interested in a longer runway", and that has to be dealt with through a negotiate-arbitrate, would you then see it's really an arbitration with all the airlines in the airport, or would you see it being bilaterals, and if it was bilaterals who would it work?

MR TIGHE-UMBERS: Sure. Well by virtue of the fact that, you know, an asset the size of a runway is going to end up in the price book for all of the customers in one shape or form, either openly or clandestinely through maintenance charges or whatever else, it would need to be an negotiation with all of the airlines, albeit as I said the other two parties, Converse and Air New Zealand may do it bilaterally themselves. But ultimately it comes back to a position of the airport putting forward a case as to why it's justified and how it will be charged for. If they've got a strong case they shouldn't be afraid of arbitration, and then equally airlines will have a case. I think you're then forced to be on a fact base around costs and benefits for both parties. An arbitrator, if it had to go that far, would intervene.

COMMISSIONER KING: How is that actually different to the sort of capital evaluation or investment evaluation process, I assume occurred in New Zealand, certainly it occurs here where the telco company, for example, says, "Well we want to roll out the following infrastructure", and there's a regulator who they go to, to get some sort of approval for that so that it can be rolled into the asset base and they can allow a rate of return on that, and obviously the regulator talks to the customers to work out if it's - it seems like it's the same thing, just called negotiate-arbitrate rather than Telco regulation.

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MR TIGHE-UMBERS: Yes, sure. Well the difference is the leverage that you've got as a customer. So telcos are quite a different example because it's very rare that you get customers arguing that they don't need My World and new fibre connections rolled out, or mobile networks. The infrastructures, the customers want it; it's just a question of how much they want to pay for it. In an example like Wellington where none of the customers are wanting, you know, significant investment and asset extension, in the current regime under information disclosure there's (recording malfunction 10:27:01) anything about that, whereas you can move one more rung up the ladder to negotiate-arbitrate, you have that regulatory backstop which should hopefully force an agreed outcome between the two parties. But if it doesn't, as customers we've got an ability to go to arbitration and say, "Well here's why it's completely unreasonable, it's going to end up in the RAB or in the price book. We'll be paying for an asset we're not using" and put the facts on the table.

COMMISSIONER KING: Can I come back to the New Zealand - because my own ignorance, I didn't - I wasn't with Paul over in New Zealand, so when you were running through I thought, "Damn, it's been pretty effective". As you said, it seems to have got prices down. The rates of return have come down for the airports. Auckland now is investing after having a bit of a capital strike for a while. You know, I guess I was convinced by you that, you know, that is still light-handed with a negotiate-arbitrate seems to be working pretty well. I mean but that isn't the lesson that you seem to want us to take away, so I'm just wondering.

MR TIGHE-UMBERS: Sure. Look, it's part of the lesson I think to take away and it is working well because of that established benchmark, and that really does allow, as I said, contain conversation around a particular data point, but it still hasn't gone far enough. The drawbacks, as I said, are really around establishing trust-based relationships. The Wellington example is - well both examples, Auckland and Wellington, are where, you know, trust - it's very difficult to have a trust-based when you see asset investment being deferred or investing in an asset that none of the customers want. You just feel completely powerless as a customer to go ahead and build something that none of you want. So I strongly believe that, you know, there's growth that we're going to be faced with and we're already at a system that's creaking at the seams. There's just no two ways about it, that the airlines and airports, and that symbiotic relationship are going to have to work very closely together. But to do that you absolutely have to have trust, and it is very hard to be sitting there, depending on the benevolence of one of the parties who has all of the major power, to have a true trust-based partnership, is what we've called for to move forward. And I just think just to - it is light-handed regulation just to move into a backstop process where you have an arbitrator that comes along and applies it. It's just built on top

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of the information disclosure and data that we've got there around reporting and building blocks, model and WACC, all it is is agreeing how an arbitration process might work. From a Commerce Commission perspective it's still pretty light-handed in terms of their involvement because, of course, it's the two parties going and having the conversation, then working through with the arbitrator. So once it's established it's still very light touch, but I think it just allows you - it sets the scene for that trust base.

COMMISSIONER KING: Do you see, because you said building on top of the current approach, so do you see, in general, that to make negotiate-arbitrate work, you do need that, for example that benchmark WACC, to be built in there?

MR TIGHE-UMBERS: Yes, I think so. It think it - look, whether you need it is probably a question for further analysis, I think it's helpful because again it just gives you a data point that you're centring a lot of the conversations around from a pricing perspective. The other set of conversations of course are what go into that asset base and that's where, you know, you just have, which is what we do in our form with Auckland Airport, is just have a free range of conversation of, "Right, what is your vision for the future? What's the master plan? What is it airlines want and how to we make all of that work?" So you just continue with that as normal but when it comes to pricing of building blocks model, then WACC would help get that on a firmer ground of - well, a more constrained discussion, if you like, around what the appropriate pricing should be (indistinct).

COMMISSIONER KING: So just - sorry - - -

COMMISSIONER LINDWALL: No, keep going, keep going.

COMMISSIONER KING: There's two things I want to actually say. So one of the issues that's come up, and BARA mentioned it yesterday and in their submission, that others have mentioned that the focus on WACC or rate of return means that the focus becomes on prices and you lose focus on quality services and the sort of services that different airlines want. So low-cost carriers need different services and want different services to full service carriers; has that been the experience in New Zealand or in fact, and again - sorry this reflects my lack of knowledge of the New Zealand system, does the regime involve service benchmarks? If not, would that be a good part of the regime? Is that a problem with the current regime and how would it be addressed?

MR TIGHE-UMBERS: Sure. Look, from BARA I think that is a fair comment. You do find, you know, 80 per cent of negotiations is devoted

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to WACC rather than service quality which is - and we're looking to try and move that more into the service quality space, under information disclosure. There are some metrics, service level metrics if you like, that the airports have to provide but they're far from adequate. Coming from a telco industry where quality of service, (indistinct), are very tightly defined. I've been quite surprised to come across here and find the airline industry pays, you know, $.5 billion a year to airports but there aren't actually defined service levels between the two and/or penalties. I'm not necessarily a fan of penalties because they can drive distorted behaviour but certainly having an agreed set of what good service performance looks like is critical.

So we are working on that with the airport to try and develop those. It's a little bit more complex in New Zealand possibly than here in that you've got a lot of other parties involved, other than just directly the airport, because of the border agencies that control the customer experience all of the way through so we try and get them involved as well. I think there was the comment yesterday in some of the discussions that a multi-party development of those service levels is appropriate and that's certainly what we're trying to do in New Zealand. To your other question on, "Does it allow flexibility of service?". There are aspects where you can do that in New Zealand and I think the example I gave was at the premium end, you've got that.

At the other end, while we haven't got there with Auckland Airport, I think there would be an opportunity if parties wanted it to choose things like, all right, elect to take bus services all of the time instead of a context stand. Right, what would a price look like for that? And we've sort of had occasional conversations with the airport about that and I think if we wished to pursue it, their willingness to develop those services and a rate card for them if we pushed for them.

COMMISSIONER KING: The final one from me before I pass back to Paul.

MR TIGHE-UMBERS: Yes, yes.

COMMISSIONER KING: We have benchmark WACCs, and again perhaps I'll shift down the other end where you've actually had rate of return-type approaches or building block-type approaches, certainly the experience I think in Australia, and again apologise for not knowing the New Zealand experience, but in those industries where they've had quite heavy-handed regulation, the economics warns, "Well, that would lead to operational inefficiency and to overinvestment" because they're ways that you can reach the benchmark WACC without, you know, essentially taking the profits through everyone driving around in their corporate Mercedes and

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just overbuilding your facilities, "gold-plating" as it's sometimes called, because that's a way of pushing up your revenue and making your shareholders happy, and there's been some very - I'm not even sure they would be debated anymore, some of the areas in Australia where that has pretty clearly occurred.

MR TIGHE-UMBERS: Right.

COMMISSIONER KING: Just when you said, "Oh, Wellington wants to build a runway and none of the customers want it"; that just raised issues to me is all this New Zealand situation with that benchmark WACC starting to push that sort of overinvestment and perhaps taking the - you know, "corporate Mercedes" for want of a better word, is it starting to push the airports down that approach and how do we protect against that?

MR TIGHE-UMBERS: Look, I don't think that particular example is as a result of trying to somehow game WACC returns and get the largest returns that they can. And again when you look at the size of the operation at Wellington with a finite number of airline customers flying into there, it's probably difficult to push that too far before you start to get to breaking point with pricing.

In terms of the broader challenge overinvestments, it's difficult for me to comment on that and I think because coming from telecommunications, when I've been in the industry it's been heavily in growth mode so they're trying to roll out the infrastructure of the next 50 year asset in terms of fibre connectivity. Equally it's the same here in airports in terms of catch-up. It's in growth mode to try and meet this coming demand so it's difficult to spot if, you know, if there's gold-plating going on deliberately. I just don't think there's any need for the infrastructure providers to do that, if you like. They've already got more CapEx investment acquired on their books than they need.

COMMISSIONER KING: Okay, so given that - yes, it is a growth industry where the passenger numbers are going, it's probably not that bigger concern.

MR TIGHE-UMBERS: Yes, yes.

COMMISSIONER KING: Fair enough.

COMMISSIONER LINDWALL: I think my observation of New Zealand airports, I wouldn't say they're gold-plated. I mean, the only gold-plated airport I've ever seen my life is the one in Doha actually. That literally is gold-plated with gold everywhere.. I'd just ask about - in 2014

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Wellington Airport returned excess profits to customers, you said in your submission. How was that manifested and you meant customers as in airlines or to passengers?

MR TIGHE-UMBERS: Yes, well their return they went for a significantly higher WACC percentile, I think beyond the 75th. The Commerce Commission gave a very strong report about it and indeed I think some of the airports even tried them and convinced them to lessen that.

In terms of passing on, so that did reduce, I can't remember the precise numbers, I think it was about $20m from where they initially had it. In terms of the pass through to customers, you know, there was obviously a lot of conversation about this yesterday with the airlines, and that particular scenario that was before my time, but certainly it comes back to the competition of the routes and, in particular, Trans-Tasman served out of Wellington is one of the most competitive routes in the world so I think there's every incentive on airlines to pass that back through and the pricing wars that result, so.

COMMISSIONER LINDWALL: And going back to the runway at Wellington, and correct me if I'm wrong, I thought, for example, and I haven't asked Singapore Airlines this, but I think my knowledge of it is correct, that they were running the older 777s because they couldn't land the newer ones on the length of the runway at Wellington and therefore that reduced the competitiveness of, say Singapore Airlines wanted to fly from Wellington to Singapore to Europe or wherever, and I also thought I heard that Air New Zealand was the one that didn't want the runway extended in particular, so isn't that an example perhaps of an incumbent airline trying to restrict competition?

MR TIGHE-UMBERS: Right, sure. So two questions there: in terms of Singapore Airlines I'm not privy to specifics if that, you know, the 777 variant they're using. What I understand with wide bodies is they can comfortably operate in and out of Wellington at the existing runway links for dealing with Trans-Tasman because they've got a much lighter fuel load so that can do that and in fact I think during our fuel pipe outage a couple of years ago, Air New Zealand flew one in there to fill up fuel and back out, so.

COMMISSIONER LINDWALL: But they may not have taken a full load of fuel on board.

MR TIGHE-UMBERS: Yes, not sure exactly. It was empty so it might have been able to do that. In terms of - is it one airline looking to prevent

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competition in and out of Wellington? I don't think that's the case there at all because, as I've said, none of the other airlines that I'm aware of have indicated any interest in it - and you've only got to look at the economics of the region to see why to fill a wide-body aircraft consistently, you really need two million people in a catchment area ideally and it's very rare below that, that you have examples - and Wellington is 500,000 people, it's just - no airline is going to be able consistently fill a wide-body aircraft out of there.

COMMISSIONER LINDWALL: Fair enough. My final question - unless you've got any more Stephen - my final question is on negotiate/arbitrate. I think you told us before that it requires the Commerce Commission to recommend to the minister to change to negotiate/arbitrate - so the Commerce Commission hasn't done that?

MR TIGHE-UMBERS: No, that's right, they haven't and you know, that's up to us to press our case as to why it's needed. The recent change we have had in legislation previously, there was an anomaly with airport regulation in particular, where to be able to move up one of those rungs in the ladder, it actually took a rewriting of law, which is a much higher hurdle to get through - particularly when you've got a coalition government - but recently, we had a Commerce Act amendment bill which changed that, which means now it just needs to be a recommendation through the two of the ministers and then it will take place. So we are pleased that that's happened because it makes that - - -

COMMISSIONER LINDWALL: I think we were discussing that change to the law when I was over there - - -

MR TIGHE-UMBERS: Yes, that's right so that got passed and you know, that's a much more credible regulatory threat because you know, the airports can feel well we can get pushed up there fairly easily.

COMMISSIONER LINDWALL: Just one more. We very briefly touched on single-till dual-till or hybrid tills and other things. So in the Australian parlance - and I'm not sure if it's used everywhere - but in Australian parlance, the monitoring regime is a dual-till, it's focused on aeronautical services. I think you were present yesterday for some of the discussion about you know, the broader effects and whether the profitability of the airport as a whole should be taken into account in the spill over benefits that occur between different parts of the airport. From the New Zealand experience, is your view that the single-till is the way to go, would a better approach be the whole of airport approach, I am just interested in your views.

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MR TIGHE-UMBERS: Yes, I mean like some of the respondents yesterday, I think there's a recognition that there's pluses and minuses in both single-till and dual-till. I'd probably say we have a preference towards single-till but you need to be able to address some of the challenges with it. Regardless of the model, I think it's about you look at the outcomes that you want and the outcomes you want as an airport operator, to be focused on its core business - which is on the aeronautical side - and the rest that you have, particularly with larger landholding airports, is there can be a distraction and a diversion of investment into more profitable commercial activities, at the expense of the fundamental airport operational ones.

You know, at Auckland, there's concern that some of the commercial activities have added to the traffic problems there, for example, coming in and out of the campus. Sometimes we're looking for site and particular infrastructure and there might be other commercial uses at an airport that they're thinking of for that land and that makes conversations difficult, so you want - whatever the model is, it needs to strongly incentivise airports to invest in their core first and then I think it's a case of moving to a recognition that rather than adversarial, if you move to a - what they call an abundance mindset these days and I sound like we're talking about joining hands and singing Kumbaya here but when both parties succeed - when airlines are successful and bringing an increasing number of passengers, the airports just gain enormously from that, through the expenditure and their well-developed terminal. So it's win/win if you get this right for both parties and grow bigger than the current adversarial approach we have, I think.

COMMISSIONER LINDWALL: Thank you for coming over from New Zealand, a long way to come Justin, so we appreciate - - -

MR TIGHE-UMBERS: Not too far thankfully.

COMMISSIONER KING: Thank you.

COMMISSIONER LINDWALL: How about we take a five-minute break or so and Caltex is next.

SHORT ADJOURNMENT **[10.45 am]**

RESUMED **[10.53 am]**

COMMISSIONER LINDWALL: So I'm Paul Lindwall and we've got Stephen King. Say hello to Rohan.

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COMMISSIONER KING: Hello, Rohan.

COMMISSIONER LINDWALL: Rohan, if you mind introducing yourself and giving an opening statement to whatever you want to say, that'd be great.

MR DANGERFIELD: Okay. Good morning. My name's Rohan Dangerfield. I'm the General Manager Supply Operations at Caltex Australia.

COMMISSIONER LINDWALL: Good morning.

COMMISSIONER KING: Good morning, Rohan.

MR DANGERFIELD: I'd like to thank the Productivity Commission for allowing Caltex Australia another opportunity to discuss the Commission's work in their draft report into the Economic Regulation of Airports. Caltex is a strong and long-standing participant in the supply of jet fuel to Australian airports, and the design, construction, operation and maintenance of key supply infrastructure for jet and other fuel types.

Caltex is a joint venture, or JV, participants in joint user hydrant installations, the JUHIs, at five major airports. We are also either the sole owner, JV partner, in two key jet supply pipelines in Sydney and Brisbane. In addition, we are either the sole operator or the JV partner in 19 seaboard terminals around Australia, and the owner and operator of the Lytton Refinery in Brisbane.

At this time, we would reiterate our previous comments, that Caltex Australia firmly believes in jet fuel supply markets in Australia operates in an effective and competitive matter, through the presence of multiple supply participants, competing for volume, strong tender processes and through various established supply infrastructure routes, which provide efficient, cost effective, competitive and reliable methods of delivery.

We would also state again that we also do not believe that there are barriers to prevent new market entrants, as has been complained by some parties, including the Productivity Commission in their draft report, and to that point, we don't support draft finding 8.1 of the draft report.

With that in mind, Caltex is supportive of some of the draft recommendations made in the Productivity Commission's draft report, namely establishing a JUHI, or a fuel facility at Western Sydney Airport, with open access arrangements, and in the development of a Jet Fuel Supply

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Coordination forum, provided it is designed with suitable protections to commercially sensitive information, and has demonstrable benefits for communication between parties, which could improve future planning for developments or extensions.

I'm happy to take any questions you might have.

COMMISSIONER LINDWALL: Thank you very much for that, Rohan. On your basis that you support open access, I mean would that be to say that you're indifferent is airports move to open access, you would still want to supply fuel at those airports, provided that you get the right price, obviously.

MR DANGERFIELD: We would supply fuel through open access arrangements. Just because in any location there is an open access arrangement, doesn't mean we would necessarily supply fuel to that location.

COMMISSIONER LINDWALL: Of course.

MR DANGERFIELD: Depending on other parts of our supply chain, and the attractiveness of the, you know, that location.

COMMISSIONER LINDWALL: Yes, yes. Now, a common theme that we've had is from conversations with various participants, is that the joint venture JUHI and the fuel supply - supply itself, are completely separate. In your business, how do you maintain that separation so that there's no risk of information flowing from one part of it to the other?

MR DANGERFIELD: Yes, so the way it works would be, when it's a joint venture, the representatives report through our Distribution division, in the Aviation Operations team. Participants in joint ventures only have visibility of their own information, which is their volume flowing through the facility, and they would usually also get visibility of the total volume through the facility. They wouldn't see what other participants were putting through in a joint venture facility. So, you only get to see, say, location A, Caltex is putting through 500 million litres, maybe the total airport's putting through a billion litres a year, and we'd know that our throughput is 50 per cent of what was going through the facility. We would have no visibility on what volume each of the other participants are putting through.

COMMISSIONER LINDWALL: Who the other were, and what their volume is?

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MR DANGERFIELD: Well, we would know who the other equity participants were, but we wouldn't have any visibility on if there were multiple participants, yes, who put through what quantities. The Operator of a joint venture would have visibility of some of those, for the purposes only of efficiently operating the facility, such as stock reconciliation and the like. They need to keep a record of who's delivered what, and who's withdrawn what product, and that information is only visible to a small number of people within the operations team for that purpose.

There's protocols within the industry in addition to local Australian competition law, for the aviation fuel facilities, usually have in place, although it's termed the Core Principles, which is from the Joint Inspection Group, which provides some additional restrictions. One of those is people who work in operations of a joint venture, can't work within a marketing and sales business, I think, for a period of 12 months after working in a joint venture on an airport.

Our Sales and Marketing team, who manages jet fuel sales, reports through quite a separate line in the business and they have no visibility of the sensitive information that the Operators see and I think that is pretty strictly followed around the industry and joint ventures that I've seen in Australia.

COMMISSIONER KING: I mean, I understand all the protocols and the various - - -

MR DANGERFIELD: Sorry, the other comment I would make is the JUHIs themselves are not fuel marketers and so they have no visibility of market pricing. So even in an airport a joint venture, the site manager might be coordinating deliveries for three different fuel companies and delivering them onto the planes for those companies, the joint venture operator has no visibility of pricing for that product. That would be handled through the marketing company's head office and their sales team, and the people on airport have no visibility on pricing to airline. All they see is the cost - the joint venture operator only sees the cost of operating the facility on airport; things such as the lease cost, the electricity cost, the staff and labour cost on airport. They only have visibility of costs of operating onsite, they have no visibility of pricing.

COMMISSIONER KING: Yes. So understand the protocols and the Chinese walls and so on, can I come to what I think is the practical basis. Let's say that Caltex has lost a contract with an airline at a particular airport, so you know what you bid; it's a small group of players, you've all got interests into the into-plane services, I would have thought it would have taken, you know, maybe two or three days at the most before your into-plane guys notice who's filling up the planes of the customer you've

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lost. That would immediately be known to your sales staff so it strikes me that, you know, you can have all the Chinese walls you want but the practicalities of a small number of suppliers operating in what is a very confined space to a relatively small number of customers, it wouldn't take an Einstein to work out who's got what where, who you've lost customers to, who's gained customers, what sort of volumes each party's doing; I mean, practically isn't that the case?

MR DANGERFIELD: Well, there's a few things to your comments. I think, you know, if you go to an airport like Brisbane Airport, for example, a member of the public can go and stand in the public access area and observe which fuel company's truck is servicing which aircraft. So you can stand at a window and you can look out there with - airline A's plane is there and fuel company B's truck pulls up to put fuel in it. So I think it's quite, in that sense, observable to the public what's going on. And then I think probably through the, you know, if a sales team bids on a contract they may get an indication back from the airline as to, you know, they know whether they've won or lost the business. They may also get an indication of how far off - you know, if they lose the business they might get some indication on, "You were out of the market by so much…", you know, or "You lost out by a certain percentage or tolerance" to give them some idea on how far they're out of the market and why they didn't win. I think that's probably the case of, you know, how this works.

COMMISSIONER KING: And again in a practical sense, you've got the meeting of the JUHI participants. Yes, of course there's no discussion of sales and so on in the meeting but you're sitting around at the coffee break - are we really to believe that the conversation doesn't come where, "Look, we know you guys nicked customer A from us at this airport. What are you trying to do, screw the market?", you know, "Pull your heads in, guys", you know, "Why should we be doing this to each other?"; surely those conversations occur?

MR DANGERFIELD: No, I categorically deny that characterisation of joint venture discussions. In joint venture discussions they're only as highly sensitive to competition law obligations, and discussions like that do not happen. To the point people wouldn't eat lunch together, or wouldn't go out for dinner after a meeting.

COMMISSIONER KING: Okay.

MR DANGERFIELD: They wouldn't. People don't interact outside that forum.

COMMISSIONER LINDWALL: Okay, Rohan - - -

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MR DANGERFIELD: We might, you know, have a coffee and a 20 minute lunch, like, in the morning tea break but those things that you characterised would not be discussed.

COMMISSIONER LINDWALL: Okay, Rohan - - -

MR DANGERFIELD: And - - -

COMMISSIONER LINDWALL: Sorry, did you want to say more?

MR DANGERFIELD: No, I think (indistinct).

COMMISSIONER LINDWALL: All right. Rohan, I was going to ask how the bidding process works with your airline customers. Well, I think, in practice they're sealed bids, is that correct, and so the airline won't say, you know, "There's a volume of fuel over this period at this airport" and they put a bid out for one or two or three years; is that pretty much the way it works?

MR DANGERFIELD: Yes, it works probably slightly different between airlines depending on the scale of their operations, how many locations they're in, but yes they would indicate they may have a fuel requirement that one or more airports, they're looking for offers for whatever time period, you know, one or two or three years might be common, and they would ask for submissions from the aviation fuels marketing team as to get their offers on that business, like, any sort of tender would work and - - -

COMMISSIONER LINDWALL: Do they set a price that they're trying to seek or they leave it to the parties to bid on the price?

MR DANGERFIELD: Sometimes there would be multiple rounds of offers in a tender where, you know, they might ask for buyers and then they might narrow it down and fuel might be given feedback as to where their bid was compared to what they thought the market was.

COMMISSIONER LINDWALL: Okay, yes.

MR DANGERFIELD: So you might put in a bid at - MOPS plus 20 cents a gallon and they might give you an indication that they think you're two cents off the market and then if you have second round you can choose your bid at 20 again, or go in at 19, 18, 17, or do you think that market's at 21 and that should be a number, right, like (indistinct) work and then the airlines, I guess, presumably take either the best offer on price or they may weigh off against other services that may be offered or, you know,

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reliability of different fuel suppliers or things like that may factor into the decision as well. Some airlines will choose to split their supply contracts for supply reliability. For example, they may not choose to place all their volume with just the cheapest supplier.

COMMISSIONER LINDWALL: Okay. When participants have spoken to us about Melbourne and the problem with supply they had a few years ago, the issue was announced that it was to do with the duration of the term of the lease for the JUHI. How long do you think is normally required for them to provide certainty for your investment profile? Is it a ten year period, 15/20 or something period?

MR DANGERFIELD: I guess sort of twentyish years (indistinct) number that used, dependent on some of the (indistinct) about what happened at the end of the term. Obviously once you get into a term, as you approach the end of whatever that was even if, you know, it's 20 years to start with; when you're five years out from the end of the term, to make any investment in an asset would, you know, tens of millions of dollars, some uncertainty as to what's going to happen at the tenure is important. That's possibly been an area that is (indistinct) that some facilities have been lacking.

So what happens to the assets at the end of the term? My experience would be usually the JUHI Operator would engage with the airport, you know, three to five years before the end of term to talk about, you know, an extension for the next periods and that certainly happened in the case of Melbourne, however it took - yes, that wasn't resolved for quite a number of years.

COMMISSIONER LINDWALL: Sorry, just to clarify one thing that you said there. So in some of the JUHI contracts, is it actually not particularly clear what happens in terms of say the airport buying back the infrastructure, how much the airport will pay - are those sort of terms not clear in some of the JUHI contracts?

MR DANGERFIELD: So in the leases, there's a whole variety of arrangements and depending on what that is, would influence investment decisions, if you make an investment today and you know that the lease expires in three years, if there's uncertainty in what happens in three years or even if there's certainty, well then the business case would need to pay out to make a rational economic investment.

COMMISSIONER LINDWALL: Yes, okay so - that's right.

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MR DANGERFIELD: So even if it was clear as to what happened, that those numbers would be factored into an investment decision and it may or may not make an investment attractive.

COMMISSIONER LINDWALL: Yes, so for example, if it were a fixed payment at the end of lease, if the airport wanted to take back the facilities, obviously the JUHI is not going to be pouring money into the facility in the last five years, when there's a potential that they'll simply get a fixed payment, regardless of whether they've made new investments or not?

MR DANGERFIELD: That's correct, yes, so a fixed payment or if - even if there's some - you know, it's not uncommon, some leases might leave it a bit open as to what happens to the assets ah, maybe there's elements to (indistinct words) handback (indistinct) um, that would you know, that - if you got no residual value on your asset, well that significantly impacts an investment decision.

COMMISSIONER KING: Yes, okay.

MR DANGERFIELD: I think the other one that's been an uncertainty in the industry is if there's provisions in a lease or what could happen at the end of a lease, where a JUHI facility might be asked to relocate - perhaps the airport wishes to expand a terminal or cargo facility or something, where the current JUHI premises is, if you're going to be asked to demolish the assets and build new assets in another location, that would significantly impact investment decisions.

COMMISSIONER KING: You disagreed with Draft Finding 8.1, fair enough. Now what you're saying by disagreeing, to my knowledge, would be that you don't think that an open access JUHI owned by a company that's not a fuel company, is any more competitive than a JUHI that's owned by fuel companies. Would that be fair?

MR DANGERFIELD: There's probably a few things. I'm not - you're talking about it being characterised by conflicts of interests where whoever the party is has a variety of interests - whether that's the airport or the airlines or the fuel suppliers or an infrastructure company, you still have a variety of interests and interests of those different parties all obviously intersect. I think that's just by the nature, such arrangements, lack of open infrastructure arrangements, I think we said we're open to open access arrangements, we see that it's then coming. You have the through putters, as we see that becoming more common in the industry and we're okay with that, as long as where infrastructure is owned they can get an adequate return. I'm unclear on - even if there's transparency on access, our feedback

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from airline customers is they're not quite sure they even want to pay or be exposed to the transparent fee.

COMMISSIONER KING: Yes, so that varies by airport, that's true.

MR DANGERFIELD: That varies by airport, so I guess Melbourne and Darwin I think are probably a couple of leading airports in that space, moving towards an open access model. Our feedback from the market is airlines still prefer to contract for a fixed period or fixed margin over the MOPS jet price and they wish the fuel suppliers to take on the risk of changes in fees. So I think there's a number of aspects there that we find a little bit challenging, as to whether they would actually help deliver - the changes will deliver to lower prices. I think our observation is, by formalising and/or regulating the returns and fees, our experience or perspective of the prices will not improve. If anything, if you carve out returns at each point of the supply chain, the aggregate of those might actually increase the returns.

COMMISSIONER KING: Okay. Now could I move away from that to look at the overall fuel supply in Australia? Of course, the OECD has a particular rule or objective, in terms of supply. Are you confident that Australia's network of fuel supply, including its refineries and its importing capacity, is sufficient to cope with the posited growth rate in aviation fuel demand, over the next ten to 20 years?

MR DANGERFIELD: I think the industry has got a good track record of making investment where required, to support you know, reliable, safe and efficient supply to airlines, airports and all parts of the fuel supply chain for fuel supply works well.

COMMISSIONER KING: And the consultative forum that we spoke of in our draft report, would that assist if it's as you mentioned, some caveats about confidentiality and so forth, in trying to give some formulation about the types of infrastructure that needs to be constructed to meet that posited demand?

MR DANGERFIELD: So I guess there's a - there's (indistinct) on airport and off airport investments or I think on airports. It makes sense obviously, where I usually say is, if the airports are supportive in investment and the airlines are supportive of investment and realise it'll come through in higher charges, well then the fuel infrastructure providers should - you have to make an investment and so you're getting good alignment on those, it's important, amongst some of the other submissions other parties have made, talking about a non-fuel infrastructure sometimes what the airport is seeking to do versus what airlines think is a reasonable place of investment. It

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doesn't always align but it makes it hard for a fuel infrastructure provider, where feedback from airlines and the airports sometimes are at cross purposes as how much infrastructure should be built if they were building infrastructure and are unclear how they're going to get that return. Do they want to build things that people aren't prepared to pay?

COMMISSIONER KING: Of course, yes.

MR DANGERFIELD: I think that's a challenge. On airport infrastructure is usually one set of assets are built, to provide efficiency and practicality and so if that makes sense. Off airport, I think some of the consultative forums can be helpful, although when there's multiple supply routes to the airport, it's always a little bit unclear as to how you know, one party's trucking, there might be multiple pipelines, there's multiple import terminals. While it might be obvious that more import tankage say is required in a location, I think that's pretty obvious to (indistinct). The caveat is then how do you - who makes that investment and on what terms and if it's multiple people owning facilities, who puts up the money and whose, or what throughput goes through each facility. In that context, the different infrastructure owners are perhaps competitors and can't really, those things can't be co-ordinated, in that sense.

COMMISSIONER KING: Okay. Could I - - -

MR DANGERFIELD: Having some level of co-ordination with industry though can be useful I think, in Melbourne and Sydney, examples over time at specific points in time, it made sense.

COMMISSIONER KING: Okay.

MR DANGERFIELD: Arguably, similar outcomes could have or should have been achieved without them.

COMMISSIONER KING: All right. Could I ask - - -

MR DANGERFIELD: I think the other observation I would make is, I think Brisbane is an interesting example of where - there's multiple import terminals, multiple pipelines and significant investment has been made on and off airport over the last number of years and the significant reason for that is servicing of tenure on airport and good engagement by the joint venture of the fuel infrastructure, provided it's with the airport and has provided the certainty for off airport infrastructure, parties have invested in tankages with their joint venture partner build a new pipeline to the airport. So we actually see in that case now - where there's certainty each of the different parties make their own decisions on investments and actually

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(indistinct) it's a good infrastructure good reliability of supply and, we believe, quite efficient fuel pricing as well.

COMMISSIONER KING: I wanted to ask you a bit about the bio jet fuel trial in Brisbane. Now, firstly I understand that bio jet has a much denser molecular structure than traditional Jet A1. I don't know if you can comment on that but a) could you talk us through the trial? How it worked, what the lessons from it were and what do you posit the future of bio jet fuel over time?

MR DANGERFIELD: Yes, so we worked with one of our customers to trial putting a bio jet product through our Brisbane supply chain and we were approached by that customer Virgin and we worked with them to put that product through our tankage at our Lytton refinery, through our pipeline and off airport terminal arrangements and then by pipeline into the airport. I think we worked collaboratively with the other joint venture participants to ensure that was achieved.

The particular bio jet that was trialled at the time wasn't compatible with both industry standards, however the other infrastructure provider owners at the Brisbane JUHI worked cooperatively to enable us to trial that and subsequently, there's been some changes to standard since then but it's been done a number of times quite easily and efficiently. But I think we've demonstrated proof of concept, it can be safely and effectively done and it's open for people to do for fuel suppliers to do that in the future. I think it's quite likely we might just see more of that both in Brisbane and elsewhere around the country and the world.

COMMISSIONER KING: And, of course, at the moment it will just be mixed product. Is that correct? Because obviously the planes are not just filling up on bio jet I assume, it's just mixed?

MR DANGERFIELD: So what we put in there, we mix it with regular jet fuel and it's transferred through the supply chain, I think it comingled at the airport and, indeed, passes through the fuel supply going to all planes filling up during that period.

COMMISSIONER KING: In our draft report we recommended a number of options for reform. We've spoken of a couple of them, like the open access. One of them - and I just wanted to see what you thought about this and I assume you wouldn't like it, but I want your thoughts on it about the implications of it – would be recommending the Minister for Infrastructure apply to NCC for a recommendation to declare jet fuel infrastructure services or introducing an industry-specific access regime.

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So clearly that has costs and benefits and implications. Could you give us your thoughts about that?

MR DANGERFIELD: I'm just looking through the copy of the report. Which recommendation was that one?

COMMISSIONER KING: I think it was near 8.1, so let me try and find it for you.

COMMISSIONER LINDWALL: It may actually have been in the text I think.

COMMISSIONER KING: Yes, it was in the text rather than a formal finding or a recommendation.

MR DANGERFIELD: Yes.

COMMISSIONER LINDWALL: It's on page 265, 266 or thereabouts. If you've got nothing to say about it that's fine. It's just if you had any thoughts about that declaration process. I mean Stephen can talk more coherently about that type of thing than I can.

MR DANGERFIELD: So, I think there's a whole range of access regimes that could, you know, could be put in place. I think we're comfortable with the current ones, and are supportive of the NCC findings from, I think it was 2011.

COMMISSIONER LINDWALL: So that was presumably where Sydney airport JUHI wasn't declared.

MR DANGERFIELD: Correct.

COMMISSIONER KING: Yes.

COMMISSIONER LINDWALL: Okay. Just on - - -

MR DANGERFIELD: I think that was ours at the time. I think what we put forward was, we thought it was quite an efficient model that is delivered, and we're still of that view, probably added, per my opening remark and my comments earlier, that we see there is a trend towards the more open access models, but we think industry together with airports is progressing down that path. And that's, I think, some would say that's a welcome addition to the industry.

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COMMISSIONER LINDWALL: So, a couple of bits where we sort of feel like we've got holes in our information, first, the equity buy-in approach to access. So, for example, I understand that's what operates at Sydney Airport, or has operated at Sydney Airport, and again, we get different views put across from access seekers, saying it's overpriced, from participants in the JUHI saying, "No, no, it's a - it's completely reasonable." Either here or in further submissions to us, are you able to provide us more information in exactly how the equity buy in works? And in particular, what I'm interested in is how the value of the equity is measured.

So, is it done on some sort of historic cost of the equity, is it done on some sort of re-evaluation? If it is done on a re-evaluation, is it - does the re-evaluation include the risk of - of the lease, there being a buy back, for example, when the lease expires? Because again, this feeds back to everyone saying, "Well, this uncertainty about the end of the lease," but on an equity buy in, that shouldn't matter, because it should - that uncertainty should be built into the value of the equity. So, are you able to help me there? You know, and as I said, either here or in further submissions, just to understand that?

MR DANGERFIELD: I probably can't go into any specifics here. I think the - the challenge people have is, depending on, you know, the arrangement might be different across different - specific arrangements, equity buy in might be different across locations, but even following a - you know, a replacement cost less fair wear and tear or a DORC model or something like that that might be - you know, some models that might be talked about. That might be the value of the equity, and a fair value of a point in time. I guess, how that plays in over - over tenure, and the - you know, five, 10, 20 years on is quite important.

COMMISSIONER LINDWALL: Yes. Yes. So, if you're able to provide further information to us, and I realise this is a sensitive area, so - but if you can provide further information, if some parts of that need to be redacted - I mean, as much public as possible is what we prefer. But, because it is an area where we just don't understand. We just haven't got the information to be able to understand exactly what's happening there. So, for example, if it's a depreciated optimised replacement cost, so a DORC as you mentioned, would need to understand how that fits in with the termination of the lease, or potential termination. So, more details on that would be fantastic.

MR DANGERFIELD: Obviously, if you make an investment with five years to go, and you make a $10 million investment in an asset that's going to last for 30 years, I guess the challenge is, how do you - yes.

COMMISSIONER LINDWALL: Yes. I understand.

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MR DANGERFIELD: Get a business case to put in - put in the investment at that point, and then if someone wants to enter between there and when the lease terminates, what's the right buy in price, and what happens - what's going to happen at the end of the lease. I think they're things that people struggle with, both in the initial investment, people who may wish to buy in as equity participants, when there's only a short period to go before the end of the lease, and where there's significant uncertainty on how airports with leases to go for the next period, are all - or what the residual value of the assets might be, or liabilities that might crystallise at the end of the lease, they're all quite important considerations.

COMMISSIONER LINDWALL: Yes. I agree completely. It's more helping us - it's helping us reconcile the fact that (indistinct) seem to view it as overpriced, and (indistinct) participants say no, it's not. It's purely to answer that question.

MR DANGERFIELD: Well, the participants have made significant capital investment over prior years. Obviously, they don't wish to sell their share of their assets and be diluted at less than for a fair number. But of course, trying to – it seems like part of the tension is trying to find what is a reasonable price.

COMMISSIONER KING: Different parties may have different views of what is fair.

MR DANGERFIELD: That's true, it's a good observation. At least in one location, an airline bought in and found that that was acceptable. So it can and does happen. I think there was a comment earlier from (indistinct) Paul. You asked around how people – what happens when people would buy in. It possible both for an equity participant to sell their share, so sometimes that would happen - or, if companies merge, there might be – equity shares might be combined. Alternatively, when a new entrant comes into a joint venture, commonly the existing equity holders would be diluted. And so if you're being diluted of your equity share, getting a fair turn on that is important.

COMMISSIONER KING: Yes. Can I just turn to another bit of information, and apologies if we've already got this from Caltex – I can't remember what we've got exactly from whom, and I discussed this briefly with Viva before as well – information on churn of customers. So how often you find you gain and lose customers, where you gain customers, where you lose customers; understand the commercial sensitivity of that.

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And we don't need to know the names of customers; we don't even need to know the names of airports, but just understanding – the claims are made, this is a competitive, dynamic industry, and churn of customers is what we would expect to see in such an industry, and making sure we've got that information from all of the major participants I think is important. So if you've already provided that, apologies for bringing it up again. But if you haven't got it, we'd be very keen to get that information in an appropriate form.

MR DANGERFIELD: I'm not sure whether we've provided anything previously, but I can say there's significant churn of customers, and customers are regularly both renewed – new customers won and customers lost as they move to other – to our competitors. That happens on a very regular basis, that customers churn between suppliers. The fact that for the airlines, there's practically not much to do. People will still have established assets and into-plane services. It can happen – usually airlines churn at very short notice. It's not uncommon for airlines to change a fuel supplier, and that fuel supplier changes at the end of the month.

COMMISSIONER KING: Yes, so just making sure we've got the full data on that. It's going to be very helpful from our perspective. Statements about churn are helpful, but the data, of course – in an appropriate form, because it is commercially sensitive – but getting that in an appropriate form I think would be valuable. Last part from me. We had different views on fuel throughput levies. It has been put to us that these are simply opportunistic prices, they're opportunistic fees put in place by airports. They're simply using the refuellers as a backdoor way of getting an illegitimate price increase from the airlines, and that these are opportunistic.

For example, they're introduced and potentially changed at the whim of the airport. The alternative view that has been put to us is that fuel throughput levies are explicitly part of the contract with JUHIs, that it's simply another way of charging the JUHIs, that it could be a per-litre charge that was just directly in the JUHI contract, and calling it a fuel throughput levy, everyone is getting excited about the name, not about the content. From Caltex's perspective, which, if either, of those views that's been put to us is more correct?

MR DANGERFIELD: So, across airports that I'm aware of, there's – some airports have the cent per litre fuel throughput levy, or sometimes it goes by another name, like a license fee or something. Some airports have a fixed annual charge that's quite significant. It does a similar thing. It's not for leases of the land; it's just an arbitrary fixed fee. So there's a couple of models. Some of the other airports I think in their submissions have confirmed they did not have such a fee.

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I think I've said in my – at the prior hearing, I think we would generally subscribe to the IATA principle that these should be for services provided, and that would still be our view. I think in one of the submissions, there was some commentary around whether it reflected other risks and things that were taken on by an airport, in which case, I guess, if that was a fair and acceptable argument, the question would be on, what's the right quantum?

COMMISSIONER KING: So would you view a - - -

MR DANGERFIELD: So if there is risk being taken by a party, having a fair return is reasonable, and the question becomes, what is that fair and reasonable level?

COMMISSIONER KING: As you noted, it has been put to us by the airports that they're taking on some passenger risk, or I guess some fuel risk, by having a throughput charge. Do you think that is a reasonable argument? Is that actually risk sharing? And from Caltex's perspective, do they want to share that risk, if it exists, with the airport?

MR DANGERFIELD: So there's I guess lots of views of what the different risks might be. Interestingly, there's a range of different views from different airports. Generally, our view is, it would be appropriate to pay a lease for the premises where the tankage is located, and any other fees should be for a service provided, or genuinely a risk taken on. But it's not always clear as to how that risk is determined, and is it properly quantified. That's probably all I can comment on.

COMMISSIONER KING: Are you aware of any fuel throughput levies or equivalent cent-per-litre charges that have been either increased, put on, established, decreased, removed, that haven't been connected with JUHI lease negotiations?

MR DANGERFIELD: The ones I'm aware of would usually be incorporated in a lease or a license. If they weren't in such a lease or a license, I don't know how they would be contractually imposed. So unless it's part of some contractual obligation, I'm not quite sure how it would be imposed and charged.

COMMISSIONER KING: I'm just thinking back to - - -

MR DANGERFIELD: So that's usually where they would be specified.

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COMMISSIONER KING: I'm just thinking back to – I think the original throughput levy was by Brisbane Airport, about the day after it got privatised. The fuel throughput levy wasn't part of the price cap. I don't know contractually how they put it in place, but it would be an interesting coincidence if that just happened to also be with the JUHI renegotiation. But it may be; I'm not saying it wasn't. I don't know.

MR DANGERFIELD: Some leases may have a provision for the airport to charge a throughput levy, and even if, at the date of commencement of a lease, there's no fee, there may be – some leases would have in them the ability for an airport to do that, at which point, if they exercise that right, well, then, that would happen.

COMMISIONER KING: Thank you, we'll - - -

MR DANGERFIELD: Other arrangements – they would be specified what that schedule of increases would be. What dates.

COMMISSIONER LINDWALL: Okay, thank you very much for speaking with us today, Rohan. I think that's been very helpful and I hope that you have a great weekend.

MR DANGERFIELD: Excellent, thank you. Have a great day.

COMMISSIONER LINDWALL: Thanks Rohan.

COMMISSIONER LINDWALL: Would you mind just introducing yourself and give an opening statement?

MS ARBLASTER: Yes, I would like to do that, thank you. First of all, my name is Margaret Arblaster and until 2010 I was a senior manager at the ACCC. In terms of my experience, it dates back to the early 90s when immediately after the deregulation of airlines, when I was working at the PSA and I think one of the first responsibilities I had there was monitoring airfares, and my experience followed through the FAC period leading the inquiry into the FAC, the introduction of price caps and monitoring to about 2008.

I am here today because I am concerned that the PC draft report has not addressed some important issues I have raised in relation to economic regulation of airport services in my advice attached to the A4ANZ submission.

I would just like to note that I've raised some similar issues in other contexts, which have similarly been ignored by the PC in the past and also

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were ignored by the Harper review competition policy. The arguments I have put in my submissions and in published research papers, have been factually based and I am not aware of any responses that have either disputed or countered arguments that I have made in the past.

I made a submission to the PC draft inquiry in 2011 and that was particularly focused on the credibility of a threat of further regulation, and I made two submissions to the Harper review and they were focused on the prices surveillance provisions, Part VIIA of the Competition and Consumer Act.

My submission on the draft report has addressed an important aspect, particularly the approach to economic regulation of aeronautical services, and it is generally described as periodic review and threat of regulation including by comments by Dr Harry Bush.

As a general comment I feel the PC generally takes a fairly abstract and conceptual sort of approach, and I don't think there's sufficient attention given to institutional arrangements for economic regulation and the context in which they operate. Further, the actual experience with the current policy framework, doesn't seem to be given enough attention in my view.

In assessing economic regulation, it is important to bear in mind that economic regulation – as Stephen, of course well knows –appropriately operates in legal and institutional frameworks, and the foundation of the current framework is based primarily on Part VIIA of the Competition and Consumer Act, but it is also supported by regulations in the Airports Act, of course.

Now, as I have sort of said in my submissions, the Part VIIA framework was designed in a completely different era with different objects to the one used by economic regulation today, and it has been relatively unchanged since that time. The application of prices surveillance provisions to complex monopoly pricing issues in the 2000s, essentially involved the development of work around arrangements including through the development of operational procedures in the early 2000s to expand the time for consideration of proposed prices beyond the statutory period. It is not best practice regulation.

Price monitoring was incorporated into competition policy legislation in 1995 which formalised a function being applied to oligopolistic industries like domestic airfares and industries where there were concerns about inflation and price levels. This provision was applied to monopoly infrastructure for the first time in 2002. It was not designed for the purpose of economic regulation of long-lived privatised infrastructure assets, such

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as airports. Specifically the provisions give the ACCC the power to monitor costs, prices and profits when directed to do so by the Minister. It is not yet established that publically reporting these three indicators of firm performance on an annual basis, is a suitable regulatory approach for long-lived monopoly infrastructure, especially without a credible threat for stronger regulatory action.

The current framework does not have a credible threat for strong regulation if a review finds that market power has been used. I did not think the proposals in the draft report have provided a credible threat either to support the light-handed monitoring framework and this is common with the PC's recommendations related to credible threat for stronger regulation of airports in 2007 and 2011.

In the 2019 draft report, the PC opposes increased information provisions, in addition to the existing regulatory measures currently available. Increased information provision could potentially increase the probability that the use of market power can be identified, however PC still primarily relies on Part VIIA of the prices surveillance provisions in the Competition and Consumer Act as the stronger regulatory intervention if regulation is considered to be warranted.

I have argued in my submission on the draft report and in my advice incorporated in the A4ANZ submission, that price controls through the prices surveillance provision under the Act, are not suitable to apply to privatised airports. They would be an unsuitable and ineffective response to the use of market power.

There are key issues associated with introducing prices surveillance and I have gone through them in a number of context including that – you know, they are voluntary and only relate to price increases, and the industry doesn't want them, so why would government apply something that either party wouldn't want, and another thing is, the wording of the prices surveillance provisions is difficult from a legal point of view and the directions that impose price caps were redrafted a number of times.

Outside the prices surveillance provisions, there's the suggestion that – sorry, price inquiry as Stephen would know, is it can be an extremely resource intensive exercise, and this was particularly the case for the petrol inquiry in 2007. And further, it is difficult to see what a prices inquiry would achieve in their current environment with the PC having reviewed every five years.

Outside the prices surveillance provisions, there is the suggestion that a stronger regulatory approach could be through the Minister invoking a

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declarations process under Part IIIA. However, this is another uncertain action, presumably the NCC would first have to make an assessment under the declaration criteria before the minister made a decision and as experience has shown, these declaration procedures are protracted, costly and uncertain.

In relation to negotiate-arbitrate regulations in the PC's draft report, I think there are points that have not been given sufficient attention or overlooked. To date there's no evidence that the Part IIIA legislative provisions which have been operating for over 20 years, have been used lightly by the parties involved. Arbitrations are rare and I understand that this is in common generally with dispute resolution processes. People don't, sort of, generally leap into them, they are fairly cautious before they – my understanding is – before they use them, and the approach adopted by the NCC and the ACCC in the cases that have been dealt with to date, under access in context of airports has generally been to narrow rather than broaden the scope of the assessments under Part IIIA.

Negotiate-arbitrate is a flexible approach and is scalable to suit the circumstances of particular cases. I don't think it's necessarily a disproportionate response to a situation. The approach adopted for the arbitration of the Sydney Water dispute involved minimal use of legal and economic consulting resources, for example, the access seeker in this case was quite a small party, and the process involved – which hopefully Stephen agrees – was a fairly efficient process in terms of the resources consumed in the time period which it was carried out.

COMMISSIONER LINDWALL: I think you have the two Commissioners involved in the only ever - - -

MS ARBLASTER: Yes, I wouldn't disagree - - -

COMMISSIONER LINDWALL: - - - arbitration in the room so.

MS ARBLASTER: That's right. And other parties can join in – in terms of an arbitration, other parties can join an arbitration so to give wider context to an issue being considered under arbitration, and if you look at the Sydney Water case the arbitration did consider the legislative framework that was applicable in New South Wales so it wasn't narrowly confined, and there are appeals provisions in relation to an arbitration so if a party felt that the ACCC, if it was doing the arbitration, got it wrong, there is scope for review. Some protection.

And I think another thing that is important is that arbitrations are designed to deal with quite a wide variety of circumstances, not just price, and some

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of the instances where people have sought to use an arbitration provision in an airport context, haven't just been related to price.

In conclusion, I would just like to say that based on my experience and research, I think there are three elements that are important related to the effect of a light-handed approach to regulation in the case where an airport might have significant market power.

One is the degree of transparency under the regulatory approach. The other is that there's a credible threat for strong regulatory measure if poor performance is identified, and the third is that regulatory compliance administrative costs associated with the approach used are fairly minimal or not onerous.

If you look at the PC's proposals in the draft report in relation to light-handed regulation, they potentially increase the degree of transparency of airport performance. They do not provide a credible threat of a stronger regulatory action in my view, and it could – some have argued that the PC draft report could have actually weakened the threat of stronger regulation, and they also increase the compliance, the administrative costs of the light-handed regime.

So there are costs and benefits associated with what the PC is proposing, and I think that the PC should re-examine its proposals in relation to light-handed regulation that are in the draft report, and I am hoping that you will take a closer look at the institution and legal framework of which the current framework for economic regulation of airports operates in, and also experience.

COMMISSIONER LINDWALL: Thank you, Margaret. I might start and then handover to Stephen. This issue about the lack of a credible threat, obviously we've tried to outline the types of analysis that would lead us to recommend to the government for a higher level of regulation which could be negotiate-arbitrate, it could be a price cap, it could be a number of other things. We did mention Part VIIA, but I don't think we hung our hats on that and I take your view about the weaknesses of Part VIIA. I mean, if you took our report if we'd removed entirely Part VIIA from it, would not the credible threats be there for you, because I'm saying that effectively the PC, if it found, and it might find in the final report, that there was an exercise in market power would recommend - - -

MS ARBLASTER: Would it recommend – sorry.

COMMISSIONER LINDWALL: Would recommend increased regulation, we haven't articulated which form yet.

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MS ARBLASTER: Well, I think that's the problem. I mean, there is no articulation that – of a direct declaration – sorry, deemed declaration for certain airport services. That was strongly - - -

COMMISSIONER LINDWALL: So you think it should be more articulated is the - - -

MS ARBLASTER: Well, it should be and I think that the recommendation that the minister could then ask the NCC to go through a declaration process is very distant and uncertain.

COMMISSIONER LINDWALL: Could I ask one other question before I hand over to Stephen?

MS ARBLASTER: Yes.

COMMISSIONER LINDWALL: You have criticised Part VIIA as being out of date and this is more a general point rather than for this report. Should it be repealed or can it be saved? Is there a way of reforming it to make it more useful?

MS ARBLASTER: Years ago, I was aware that there was some constitutional difficulties the Commonwealth has in relation to pricing, but I'm not a lawyer and I am not sure whether that is still the case. At the moment Part VIIA – well, apart from airports – the price surveillance provisions just apply to Airservices Australia which is a government owned corporation, and I think through the Minister's involvement has incentive to sort of comply with Part VIIA.

And similarly, Australia Post letters – well, letters are almost a dying industry, I think you could say, and also Australia Post is a government corporation, they are not a privatised company. But I mean the PC was strongly opposed to the airport specific access regime in 2002, and I didn't see anything in this current draft report that suggested that you would support that again.

COMMISSIONER LINDWALL: I've got one more question before – some people will say that because this is the fourth PC inquiry, if we recommend the same things as we did in our draft, that the credible threat is reduced because of that. You agree with that, do you?

MS ARBLASTER: I think so.

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COMMISSIONER LINDWALL: On the other hand is it not, could it not be said that it is an efficient outcome and it is working because the analysis that we had in our draft was that the market power was not being exercised. Couldn't that not be said that the credible threat has been working because they haven't been exercised in market power if we take out - - -

MS ARBLASTER: Well, I really don't want to get into the assessment of your market power, but just from what I understand – I mean, a lot of it is generally reliant on sort of price benchmarking prices.

COMMISSIONER LINDWALL: Yes, yes.

MS ARBLASTER: And I am aware – I mean, there are a lot of people who are a lot more expert in benchmarking than I am. I've been to quite a few of the ATRS's conferences, and I have heard, Tae Oum, who is present of the ATRS actually say, you know, it is designed to assess operational efficiency. Whenever the results are presented each year at the conferences they are presented on the basis of regions. They are not – and the awards are given by regions. They are not presented across the board and I've never heard it claimed that they're an appropriate tool for assessing airport market power. So, you know, I just have some doubts about that but because it's not my area of expertise, - - -

COMMISSIONER LINDWALL: No, that's fine.

MS ARBLASTER: I just wouldn't want to get into that, yes.

COMMISSIONER KING: Sort of a follow-on from that, there is obviously disagreement in this area about whether there has or has not been an exercise of market power by the airports. I think the representative of IATA yesterday says, "The process is, you know, find out if there's a problem then if there's a problem, look at the solutions". So I'm wondering your perspective on that. So, let's say that, you know, clearly if the PC determines that there has been exercise of market power against the consumer interests or against community interests in our final report, we would be addressing what needs to be done to, you know, what baseball bat needs to be brought out, for want of a better word.

MS ARBLASTER: Yes, I mean that's what you should do, yes.

COMMISSIONER KING: But if in our final report we have the conclusion there has not been or is there no evidence that there is an exercise of market power to the detriment of the community, why would we need to go any further on that? So you're talking about credible threats. If there isn't a problem, why would we want to then go down and explore and say, 'Ah

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but if there is a problem which we haven't seen, then this should be the solution'. Can you expand on that?

MS ARBLASTER: One is, I think - well, it depends on the adequacy of the assessment and, you know, what your - - -

COMMISSIONER KING: Well, let's assume we're competent and it's an adequate assessment.

MS ARBLASTER: I mean, I don't disagree you are not competent people but, you know, it's just that the assessments that have been made in the past have been very light. And, you know, I think it was the 2011 reports that you have said, "Oh, you know, based on a comparison with other airports, they don't seem to be all that out of alignment" but when some - I mean, I'm aware of other people like the Grattan Institute study and that, you know, and other work that, you know, (indistinct).

COMMISSIONER KING: They were looking across the entire airport (indistinct).

MS ARBLASTER: Yes, who have got sort of different impressions.

COMMISSIONER KING: Yes, but if we find in our report - - -

MS ARBLASTER: Okay, assuming you do find but I mean I think there still has - I mean, the idea of light-handed regulation is that to have the incentive effect you need to be, I would have thought it was reasonable to expect that, you know, if you don't do what - the performance isn't consistent with, you know, reasonable competitive efficient outcome, that there would be some penalty and - - -

COMMISSIONER KING: Yes, but wouldn't we not want to be too precise about - well, it is about the company working if we find that there is - if our evaluation, and you can criticise our evaluation, but "if" our evaluation in the final report is there hasn't been an exercise of market power to the detriment of the community, doesn't that say, "Well, for whatever reason and despite differences of views and whether we need a bigger or a different baseball bat, that doesn't need to be addressed because we haven't found the problem."

I mean, it seems to me that there's a lot of debate here about solutions in search of a problem. The people that are saying, "Ah, well we've decided there's an exercise of market power so here's our solution", our draft report says, "We don't see that" and so we see all these solutions out there saying, "Oh, if there was a problem please choose us, please choose us" and with

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all due respect you're another person who says, "If there's a problem, please choose my solution".

MS ARBLASTER: Well, if you'd like to compare with price cap regulation, price cap regulation is said to work because there's an incentive, you know, and the incentive with a price cap is that if you can decrease your costs more than was the forecast with the underly of price cap, you could increase your probability so there's an incentive for (indistinct) in theory, you know, to be efficient.

COMMISSIONER KING: Yes.

MS ARBLASTER: Now, if you assume that you found that the airports were misusing their market power and you assume that the assessment, you know, is valid and - where is the incentive going forward for continued - you know, like you have an incentive with a price cap going forward because you can increase your profitability but there's no - - -

COMMISSIONER KING: Margaret, with all due respect aren't you falling into the economist's trap of, "It seems to work in practice but it doesn't work in theory, therefore we have a problem"? I mean, if we say in the 17 years since 2002 and the numerous and you can - and I am working on the basis that we - wherever we end up, and I'm not saying we "will" end up here but it is a possibility that the PC will be competent and they will reach this conclusion and after 17 years I do worry about falling into this trap of saying, "Damn, we've got something that seems to be working but in theory there's a problem so we need a solution".

MS ARBLASTER: I mean, there's also the ACCC reports which have, based on their assessment, identifying problems going back into (indistinct) which are not resolved. I mean, you've got issues that are not resolved.

COMMISSIONER KING: So are you saying that simply, "If the PC - - -

MS ARBLASTER: And the other thing is that price is just one aspect of performance. I mean, it's an important aspect.

COMMISSIONER LINDWALL: But isn't it only contractual between airlines and airports, that's the way it's working at the moment, they negotiate and they come with an outcome and they come up with service level agreements, they come up with a price, they come with a plan of infrastructure investment and so on, yes again Stephen is exactly right. We don't know where at this stage where we'll end up in the final report. I mean, we have to logically take the evidence before us but if we do end up saying, as we did in the draft, that there has not been an exercise of market power,

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I don't see where there's a problem with the actual airport and airline negotiations then because that would be our finding.

MS ARBLASTER: Well, it depends on, you know - well, I suppose your assessment of the negotiations and whether or not they are, you know, how they compare with other peoples' assessments. I mean, the airports themselves are in one.

COMMISSIONER KING: We can't second-guess negotiations. I mean, they're commercial negotiations between two parties who know a hell of a lot more about their business than we do. We're just seeing whether there's any evidence that would point to them using their market power to some detriment and there's a lot of reasons, well there are some reasons, why they might not and there's debate about countervailing power, there's debates about different business lines and so on.

MS ARBLASTER: And the airlines aren't the only users - - -

COMMISSIONER KING: Correct, correct.

MS ARBLASTER: - - - which is, you know, another point. But, I mean, it just would seem odd to me that, you know, if you've got sort of all this other information out there, like the ACCC who have been monitoring year in and year out, and raising problems and concerns.

COMMISSIONER KING: Yes, but we've addressed that. We've looked at the monitoring reports and likely there's a strong principal here that a regulator should not be trying to dictate policy, that's the PC is a separate body to the ACCC. If the ACCC was to determine whether there should be more regulation of airports, they would say yes because as far as they can see the ACCC - - -

COMMISSIONER LINDWALL: (Indistinct) put it in their submissions saying that, so.

COMMISSIONER KING: They regulate just the courses of monopoly. Our view, the PC's view has been always that monopoly per se is not sufficient to regulate. You need to have the proof that there's an exercise of market power.

MS ARBLASTER: But if you've - I mean, if you come to that view and, I mean, it has to be - there are a lot of dimensions to performance and you've come to that view with a sound, well, basis on every aspect?

COMMISSIONER KING: Well, sorry - - -

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MS ARBLASTER: I mean, if you do come to that view, I mean - well, it's a question of - well, hopefully - well, maybe people would accept that but it will still be the issue of what it would be going forward and, "Have you evaluated right back to 2002", you know, has it always been the case?

COMMISSIONER KING: The ACCC hasn't looked at every aspect when it said there are problems.

MS ARBLASTER: No.

COMMISSIONER KING: I mean, are you saying that the onus of proof here should be that, "We assume there's a problem unless it is proven otherwise"?

MS ARBLASTER: What I'm' saying is that with light-handed regulatory frameworks, from my research, the general properties of them is that there is a threat - there is an incentive embedded in them. When they're applied to sort of strong monopolies, there is an incentive for good performance. Like with a price cap there is - the way the price cap is designed, there is an incentive for good performance if there's not a credible threat of a stronger regulatory framework, then the framework does not have any incentive for - or there's no incentive effect for good performance. And, you know, the proposals about regulation is just vague and we've been through the Part VIIA approach which, you know, is pretty weak and - - -

COMMISSIONER LINDWALL: Don't you trust the PC that if it says, as I've said in speeches, I'm sure Stephen has, and we've said it in our report, that if we found an exercise of market power, we would not hesitate in recommending more regulation.

MS ARBLASTER: But the PC has had a very consistent approach not only in relation to airports but also in relation to other regulatory measures. They've been totally opposed to any increased regulation so it's hard to sort of believe that the PC would recommend something like sort of a direct access arrangement, quite frankly.

COMMISSIONER KING: Are you familiar with the New Zealand approach to regulation by the way?

MS ARBLASTER: Yes, I am. Well, I mean, not the last couple of years I haven't been following it so much, but.

COMMISSIONER KING: But you'd be aware, it's not - it's light-handed, it's got some features that are different to Australia.

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MS ARBLASTER: Yes.

COMMISSIONER KING: For example, there is a - - -

MS ARBLASTER: Yes, has a lot of features different to Australia.

COMMISSIONER KING: - - - set rate of return but again, the Commerce Commission there analyses the performance of the airports, it puts forward a report but that report, very much like price monitoring, is not binding.

MS ARBLASTER: No.

COMMISSIONER KING: The airports can say, "Up yours, well do something else".

MS ARBLASTER: Well, except that the - sorry, go on. I shouldn't interrupt, go on.

COMMISSIONER KING: No, no. But I'm keen, and today we heard from the airline representatives for New Zealand airlines that operate out of New Zealand. They said they felt that there should be more, and I don't want to pretend that they said they were happy with regime, but the testimony before us was that that regime has seen a drop in the returns to the airports and has been effective so what's your view on the New Zealand regime?

MS ARBLASTER: Well, my view is that the framework is quite different to what is here because there are credible alternatives that could be easily instigated if, you know, poor performance was identified and they are credible. I mean, for example - I mean, the legislation was passed in 1998 and there are a variety of different forms of price controls and they're far more modern than the prices surveillance provisions. There's also negotiate access regime in the range of regulatory tools that are available and the New Zealand Commerce Commission gets very detailed information, even more detailed and more based on economic principles that proposed in the PC draft report.

So the New Zealand Commerce Commission is in a position to identify whether airports are sort of creating excess profits. It also evaluates performance. It gets quite a number of different measures, not just profits, you know, innovation and things like that so I think it - - -

COMMISSIONER LINDWALL: But it still hasn't recommended negotiate-arbitrate.

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MS ARBLASTER: No, but Auckland Airport has - you know, it has identified that it's been able to do that because of the information it gets.Auckland Airport has actually sort of reduced its charges and I think there's Wellington Airport that is or has been identified as having some higher charges. But Wellington Airport, I understand, has also made some changes as well as a result of the assessments made by the New Zealand Commerce Commission.

COMMISSIONER KING: So just to understand how to then improve what you see our system as being forward - so we've said in our draft recommendations that we think there should be more information gathered and brought to the PC. Is it your view then - well, is it a step in the right direction? Does it not go far enough? Should we be saying, "No we need more information like New Zealand" or another jurisdiction. I just sort of wanted to understand, so is it an information problem that we've got here?

MS ARBLASTER: Well, I mean, information is one aspect and potentially, you know, your proposals can improve the transparency of airport performance over the current situation but look, as I understand, that they are still based sort of basically accounting sort of data and I know, for example, in New Zealand there was a lot of debate on some of that with elements of the information before it was actually implemented in the information disclosure regulation. And in relation to, for example, the 2001 Sydney Airport price determination, there were a lot of elements of price there that were really quite contentious and had significant bearing on how you would assess the profitability of prices. I mean, airport land is one in particular. You know, it is fairly difficulty to value, or put an economic value on it and it was quite contentious.

So I think that, in terms of information, it is probably an improvement. What you would get as a result of the - I mean, you're still not proposing common methodologies? I'm not suggesting that that necessarily should be the approach but I'm saying that it's not clear that the information that ACCC would get, as a result of your proposals, is going to be sufficient to actually identify economic profits.

COMMISSIONER KING: All right. So we notice both the costs and benefits of our proposed extra information in our draft report. I assume it's your view that any information, you know, if we wanted more information and uniform across that, that would need to go through a cost benefit analysis.

MS ARBLASTER: Yes it would, yes.

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COMMISSIONER KING: Okay.

MS ARBLASTER: So that's one element and the other element is what you do when you've got the information? You know, I mean, so you get the information and so - - -

COMMISSIONER KING: And also puts out a report - sorry, New Zealand Commerce Commission puts out a report.

MS ARBLASTER: They put out a report but they are backed - and they put out a report and they're in a position to do a (indistinct) because of the information they get, they can assess pretty accurately, you know, the performance of the airports more accurately than you'd be able to assess with the extra information proposed.

COMMISSIONER KING: So, I mean - - -

MS ARBLASTER: And then there is all the other credible alternatives that could be put in place if the New Zealand Commerce Commission identifies that - - -

COMMISSIONER KING: Such as - - -

MS ARBLASTER: Such as negotiate-arbitrate regulation.

COMMISSIONER KING: Or such as deemed declarations.

MS ARBLASTER: Such as that, yes.

COMMISSIONER KING: So that's an option that we would have if we found a problem in Australia? We could recommend that the airports be declared under, or effectively deemed declared, under Part IIIA; would that be appropriate for Australia?

MS ARBLASTER: It was applied, as you'd know, when the airports were first privatised and I think it worked effectively then.

COMMISSIONER KING: But they were under a price cap regulation rather than a - - -

MS ARBLASTER: Well, they were but there was also - well, Virgin, for example, applied to have coverage of that provision but the ACCC said, "Well, you've got a price cap so, you know, we won't do it".

COMMISSIONER KING: Okay.

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MS ARBLASTER: I mean, that did restrict its application I agree but it was interesting that there were a number of other parties that actually used that provision at the time.

COMMISSIONER KING: Yes, but again coming down to credible threats; we have that credible threat.

MS ARBLASTER: Well, the question is: how credible is it when the PC has this very long history of being totally opposed to any - - -

COMMISSIONER LINDWALL: Different commissioners each time, it's not like it's the same person.

COMMISSIONER KING: And let's imagine that the reason is that the PC has had inadequate information: if we had the adequate information along the lines that you've suggested and we have, as we do now, the threat that if we find there's a problem we could recommend, for example - and I'm using deemed declaration as an example because I think you mentioned deemed declaration in your introduction.

MS ARBLASTER: Yes.

COMMISSIONER KING: So we could recommend deemed declaration at the airports. So that strikes me that you're suggesting we improve the current system, not that - - -

MS ARBLASTER: Well, if you had the deemed declaration, that would improve the current - - -

COMMISSIONER KING: The threat of deemed declaration.

MS ARBLASTER: Yes. Well, I don't know - - -

COMMISSIONER KING: Do you believe that even in the absence of evidence of an abuse of market power, the airports should be deemed declared?

MS ARBLASTER: Well, I think what I've been saying is that it gets to the credibility of the assessment of the absence of the exercise of market power.

COMMISSIONER KING: No, no, as of today given your knowledge of expertise and your background in this area, is it your opinion that the airports should be deemed declared today?

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MS ARBLASTER: Well, I can't see that it would be harmful for that to occur because of all the protections that are available under the Part IIIA provisions.

COMMISSIONER KING: Well, remember we're going passed a whole bunch of protections because we're not going through declaration. But you believe basically that - - -

MS ARBLASTER: Well, yes we've discussed the problem with - I mean, if declaration wasn't such a long costly and uncertain process, then maybe that's - - -

COMMISSIONER KING: Hang on, let's go back to that. Because of course the most recent example that I'm aware of with an airline, Tiger applied to have Melbourne Airport declared and the process was all so fast. The NCC didn't reach a decision before Melbourne and Tiger had done a deal so that doesn't seem to me to be an example of a failure of Part IIIA.

MS ARBLASTER: Well, that's one example but there are a lot of other examples that are.

COMMISSIONER LINDWALL: I think we'll have to finish.

COMMISSIONER KING: Okay. All right, we'll finish up.

COMMISSIONER LINDWALL: I think that Margaret would (indistinct). So thank you very much for speaking to us today.

MS ARBLASTER: Thank you very much.

COMMISSIONER KING: Thank you very much.

MS ARBLASTER: Thank you.

COMMISSIONER LINDWALL: Could I invite Peter Forsyth, Professor Peter Forsyth. How are you today, Peter?

MR FORSYTH: Fine, thank you.

COMMISSIONER LINDWALL: Good to see you. Peter, if you wouldn't mind introducing yourself and give any opening statements. By the way, the notes of your points of discussion. Do you want us to treat that as a public submission?

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MR FORSYTH: I'd say whatever you - they are informal notes but if you think that they're useful - - -

COMMISSIONER LINDWALL: I think if you're happy for them to be treated like that, they'll be a public submission. It doesn't amplify, it just records.

MR FORSYTH: Okay, then.

COMMISSIONER KING: Yes, if you could just say your name for the transcript.

MR FORSYTH: Yes, I'm Peter Forsyth. I'm an Adjunct Professor at Monash University. Thank you very much for having me here. I have provided a few notes. They are fairly simple notes and they are rather going in a rather sort of different directions, in a sense, so it's not as though it's a sort of very specific approach to looking at whatever. So essentially there are six points which I highlight. There are a couple of other things that I could mention but depending on time and so forth. Okay, the first point was the rationale of light-handed regulation and this was made by way of a comment about the way things are going. The original idea of light-handed regulation, as I understood it, perhaps in the 2002 airport regulation report, was that light-handed regulation would improve efficiency and also investment.

Now, in the current report avoidance of excessive returns seems to be the main objective and so there seems to be something of a move from one to the other. Originally that light-handed regulation was all about keeping, you know, basically looking at productivity: if it's good, great. If it's not, there's a problem. Whereas now the emphasis to be, "Is there market power being used?" Now, it could be a possibility. It might be that market power is being used. Let's say that prices are 10 per cent higher than they should be, okay. It still might be the case that productivity under this arrangement has been extremely good. Now, as it turns out the evidence on productivity, particularly over time, is fairly good. Now, there are some questions about the last few years, I've addressed that in my submission, but nonetheless (indistinct).

So I'm not saying that you should, you know, forget about how much basically whether prices are too high or low or everything else, but I'm just saying that that was something that was a real emphasis in the earlier approach and therefore is a question to what extent do you sort of really want to emphasise mainly (indistinct) about prices relative to costs.

COMMISSIONER LINDWALL: I hear you, yes.

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MR FORSYTH: The second thing, the report seems to argue that there is little passthrough of charges to passengers because there is strong oligopoly in the airline industry. Now, let's take it that there is strong oligopoly in the airline industry, it's still perfectly possible that under that arrangement or situation there could be substantial passthrough. In other words, I'd like to see a bit of a model which justifies those sorts of statements. I think that the passthrough, whether you think whether it's very important or not, I'm not so sure that - you've tended to be very, shall I say, blasé about the scope for passthrough. Now, whether you think that's an important issue or not, I'm not commenting upon that. I'm just saying that you really need to justify that more perhaps with a simple model or whatever.

Now, that comes up to the next one; countervailing power. And again this is the same sort of issue that I think that the PC in its report has more or less said, "Well, okay. Here's the situation. We don't think there's much of a problem. Let's go on to the next issue." Now, in the case of countervailing power, it's still quite possible that airline passengers could be badly affected, let's say, if an airport is using its market power substantially.

Again, this is a matter that you do need to have a bit of a model to see what's actually going on. Now, this I think is a bit more important because it may well be that there are other benefits from aviation. It had been argued in certain cases there are wider economic benefits from aviation. Now, if that's the case, the use of market power could be more costly in terms of (indistinct) terms than people such as myself have argued and, I think, the PC has argued.

The next point is about monopoly and relocation rents at parking places. I really don't think the discussion of parking rents is very convincing. Now, if there is a low opportunity cost of land, low prices are efficient as long as there's no particular constraint no matter how convenient the actual car parks are. As long as you've got low opportunity costs of land, then low prices are in order.

Now, that means that there really needs to be some empirical assessment (indistinct) the opportunity costs of land in different airports. Now, I don't think that - well, in the case of say Sydney Airport, I see it's very built-up and the land value of Sydney Airport is around about, according to my calculations and other people's calculations, about $10b around that area and so on.

So in other words Sydney, I think, could have a perfectly legitimate claim to say, "Look, the prices that we're charging reflect opportunity costs of our land". On the other hand Melbourne, is that really the case? I mean, when

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you look at Melbourne it's a lot further out and there's quite a lot of land around and so on. Of course there are location rents in the inner areas of Melbourne parking but what about the outer areas. Now, I really don't think that the comparisons between Rod Laver Arena and all sorts of other places really are justified.

This is the sort of thing that airports claim, that they say, "Well, our airport is out in the sticks but in the city you'll pay an awful lot more for parking". That really doesn't cut it. You really have to get some sort of indicator of how - well, basically of the opportunity cost of that land and you have to do that with some sort of empirical work and I don't think that that's been done in the report. It basically says, "Well, we believe it is the case that they are high opportunity costs for the land". Well, that could well be the case in say Sydney but may not be the case in Melbourne.

Okay. (Indistinct) was talking about, and I have some notes on, the rationing price at Sydney Airport. Now, I think the issue of rationing prices will be a major one from now on and think it would be useful if the report could give some more guidance about the role prices may play. Now, there's some statements, they are somewhat vague such as on page 171.

The issues I think need to be analysed more thoroughly. Higher prices in a case of excess demand could be a very good walkway of rationing demand but there are other ways as well, there are slots. Then becomes the question, "How efficient are the slots?" and so that becomes (indistinct). Furthermore, and this is a more subtle point, airport prices as we start with embody a (indistinct) price structure. In other words, raising revenue to cover costs. But when you've got excess demand, that issue doesn't really come in anymore and you can have lower prices and so on.

And so all in all, particularly with (indistinct) pricing and so on and so forth, one shouldn't necessarily assume that if the airport is in high demand, then higher prices are the only way of achieving efficient ration (indistinct). There are other ways, and one really needs to go through them and discuss them and evaluate them, it's not to say that they could be a good way but slots have been used in lots of very busy places such as London and that seems to work quite well.

On that, I support the idea of a review of the Sydney slot management system but I think it's important to really have tradable slots then on the agenda because otherwise I wouldn't be surprised if there is a review, let's say, that the people who are involved in such a review are more, shall we say, administratively minded and basically tradable slots might be docked off the agenda and I think that that would be a real pity.

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It's quite possible that the revised IATA system may also be bringing more regulations and also which might lower (indistinct). So I think you really need to spell out what you mean by, "You think it's a good idea to have that sort of review of slot management system and what issues it might look at and how it might address them (indistinct).

Finally, airport lease conditions: the discussion at page 287 is very brief. How much of a constraint on behaviour does the Commission really think these pose? Now, I must admit that I haven't even looked very much at these conditions but in the talk that Stephen gave last week, you did seem to put a lot of emphasis on that and that could well be the case that that could be a real constraint on behaviour.

If so, I think it really needs to be expanded a lot more because if it's going to be so critical, and it's only about less than half a page and it was almost actually tending to downplay that role so I think that that is - that was something that I hadn't really thought much about. I thought it was just some technical legal-type stuff and it wasn't very important but it could well be and so I - - -

COMMISSIONER LINDWALL: Well, thank you very much, Peter. I don't really have any questions apart from maybe on countervailing power because I think you've been very clear here about where we could improve our report in the final and areas that we should look at so I think the way I think about is that we'll go away and talk about some of these. We might come and talk to you some more if we need to clarify anything. I mean, in terms of countervailing power I guess my question would be, "Do you think that if an airline has countervailing power, does it act as a constraint on monopoly power?".

MR FORSYTH: It would be - yes, but that's not the end of the story.

COMMISSIONER LINDWALL: Yes, that's what I'm saying.

MR FORSYTH: You have to go further down - deep down (indistinct) and see what happens (indistinct).

COMMISSIONER LINDWALL: I understand where you're going there. All right, thank you.

COMMISSIONER KING: Okay, actually to, because that was one of the questions I had, so is the concern on countervailing power - so, you know, there's two starting models - the first year undergraduate models that you can think of with a chain of monopoly airport - let's for the sake of arguments say less than competitive downstream monopoly airlines and

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then the passengers. So, you know, model 1 that you first give for undergraduates is airport sets a price, then that price gets marked up at the next stage and the customer ends up in complete strife and, you know, that's a terrible outcome for the customers. Their countervailing power would be that middle section pushing back on the airport and leading to a benefit for end users, so that's model 1.

Model 2 would be airport and airlines get together in a room, negotiate together, come up with a scheme to maximise joint profits, they fight about who's going to get what share, and the customer's, end users, end up facing essentially an integrated monopoly profit. Countervailing power there has no benefit to the customers because all it is is about rent sharing. When I read your point here, I thought that might be what you were getting at but I have to make sure.

MR FORSYTH: Yes, indeed you've put the words more effectively than I have so, I mean, that's one of the sort of things I was thinking about, yes. And I think in your discussion of it, I think that it would be nice to have some sort of simple modelling saying, "Okay, this effect could be possible, that effect could be possible".

COMMISSIONER KING: And thank you very much by the way for these points because there's a number of points here where I was reading through and my reaction "Oh if you've got that impression, we need to improve our exposition" because I thought, for example, on investment I thought we'd done quite a bit but it may be - you know, one of the issues when you're writing one of these things is you think, "Ah yes, we've got on top of that and here's the half page and we move on". For someone coming with fresh eyes and sort of saying, "Oh we've dismissed this quickly" so thank you very much for that.

MR FORSYTH: Yes.

COMMISSIONER KING: The other one I had was on the opportunity costs because that's really interesting because of course it's the opportunity costs to whom and let's focus on those inner car parks. We haven't really seen complaints about say the long term car parks and so on. It really tends to be those at terminal where people get quite upset and the opportunity cost I would have thought there is the opportunity cost to the airport. So if, for example, there was less terminal car parking at Melbourne Airport, we probably know what the next best use of that land is because they're already doing it. They have a great big hotel sitting there and so probably the opportunity cost is the potential for having a hotel on that site rather than having the car parking. Whereas you tend to say, "Well, the opportunity

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cost would be farmland if it wasn't used for car parking" which isn't - it may have been an opportunity cost when the airport was built but is not today.

MR FORSYTH: Well, I think there's still farmland around. I think there's some - - -

COMMISSIONER LINDWALL: Well, because of the rules.

MR FORSYTH: Okay, I'm thinking about sort of the median area around the terminal, yes I think that that's very much what you said. On the other hand when you start going a little bit further, what is (indistinct) and so you would then look at the sorts of prices that they are charging, sort of middle to further distance, and they seem to be higher than other places very close by but it is just they're outside the airport area. Now, I think you'd have - well, you've have to check the actual data on that (indistinct) impression was. And so yet somewhat inconvenient car parking but some of it could be a lot more convenient. For example, I car park usually in a place that's very close to the terminal actually but, you know, there's a barrier there.

Now, that actually comes back to the Commission's point that's saying, "One thing that you need to - if you think that there is a bit of a problem in terms of market power being used, try to lessen it."

COMMISSIONER LINDWALL: Yes, (indistinct) of landside access, yes.

MR FORSYTH: And so looking at landside access, particularly at Melbourne Airport and so on, is that designed as it were to bolster the use of market power or can be used to lessen any degree of market power?

COMMISSIONER KING: Yes, and I think that's the approach that we've taken is that if there's a problem there, let's make sure that the competitive alternatives, such as off airport car parking, have the best possible chance to compete.

MR FORSYTH: Yes. May I give just a couple more sort of observations.

COMMISSIONER LINDWALL: Yes please, yes.

MR FORSYTH: One thing is that when you're measuring, when anyone's measuring, the use of market power and you look at rates of return in airports, I think it's important to recognise that a lot of airports are publicly owned and others are, if not publicly owned, they're not-for-profit organisations (indistinct) and - - -

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COMMISSIONER LINDWALL: Yes, councils (Indistinct).

MR FORSYTH: And you can't necessarily assume that they are maximising profits.

COMMISSIONER LINDWALL: No, that's right.

MR FORSYTH: So looking at different rates of return and saying, "Well, the Australian airports rates of return are higher than anywhere else", I think you really need to take that very much into consideration. Of course what you'd then do, you say, "Well, we need better data on costs, prices and rates of return" (indistinct) be a good idea and I think that that's where the ACCC is going as well. I think they would like to see more better data on trying to measure the actual rate of the economic profit on airports. And so that's, I think, something that - - -

COMMISSIONER LINDWALL: I understand where you're going, yes.

MR FORSYTH: So don't read too much into what's going on. International comparisons, I think in this particular case have some real problems but I'm not saying they shouldn't ever do them, but yes.

COMMISSIONER KING: So just on that though, a lot of international comparison airports are also regulated so in a sense, do they provide - you know, if you're saying, "Well, how do our airports go compared to a regulated alternative?"

MR FORSYTH: Okay, you'd really need to have privatised, and genuinely privatised, airports to make a good comparison. But quite a lot of airports are in a sort of partly privatised situation, others are government owned, and also I don't consider that all airports that are "privatised" always maximise their profits.

COMMISSIONER LINDWALL: Correct, yes.

MR FORSYTH: Now, in my view I think Sydney is a good example of a profit maximising firm. I'm not so sure about others. I am very doubtful about Adelaide and I think also, in the case of Brisbane, which until recently was publicly owned until 2010, was owned by other firms that were publicly owned, that they necessarily have been right at the forefront of maximising profits and as a result maybe they've been very keen to invest, for example, in the new terminal and runway - well, in the case of the runway there doesn't seem to be a lot of congestion and yet the runway is due to open next year. It's quite a contrast with Sydney where they're quite

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slow in responding but I think are arguably optimal. Yes, so I think those were the points that I was going to make.

COMMISSIONER LINDWALL: Well, thank you very much for speaking to us, Peter.

MR FORSYTH: Just a comment on your discussion with Margaret.

COMMISSIONER LINDWALL: Yes.

MR FORSYTH: You say that if the system's working well, why change it, okay, but I think that there is another thing in terms of, "What about the future?" The next time that you guys will have a look at it will be in seven years' time. What about if over the next, you know, few years the airports really start pushing up their prices well above, let's say, costs, okay. What can we do there? So in other words I'm looking not just at the past, so far okay, in the future, next seven years, what is there?

If the various constraints are not as strong as you're suggesting, what happens, is there some role for some sort of negotiate-arbitrate sort of system which is put in place and I have been rather sceptical of that. I think now I'm beginning to think, "Well, maybe there could be some sort of backstops that doesn't necessarily get triggered very easily". It actually could be quite difficult to trigger but is there as something if the airports do start excessively pricing. So, in the future.

COMMISSIONER LINDWALL: (Indistinct) about that.

MR FORSYTH: And I don't want to have - well, I wouldn't suggest a very detailed and substantial - but something that actually has, you know, at least some sort of thing that needs to be - it's fairly difficult to trigger but if need be it can be triggered.

COMMISSIONER LINDWALL: Okay, well - - -

MR FORSYTH: One thing that I think you need to think about is that there's not just one form and level of negotiate-arbitrate, I think that it can be tighter or less tight, as you like, and that can be worth thinking about.

COMMISSIONER LINDWALL: All right, well thank you, Peter. I think we probably should move onto our next guest. We appreciate you coming along and we'll be in touch again, thank you.

MR FORSYTH: Good, okay, then. Yes, bye bye then.

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COMMISSIONER LINDWALL: Could I invite Edmund Carew to come forward.

MR CAREW: Commissioners, I'll just organise myself if I could. Firstly just some housekeeping. Congratulations on your forthcoming 21st birthday in April as the PC so I've got you a carrot cake and some sticks to beat people like me with.

COMMISSIONER LINDWALL: Thank you. You know that we can't accept gifts though but that's all right.

MR CAREW: Well, indeed. You'll have to declare it on the register, Commissioners. Commissioners, the draft report that you've submitted for us is correct in some areas such as that there's high modal substitutability between Canberra and Sydney is one; I don't agree with the airlines on that and that's partly due to Qantas and Virgin's inability to run on time and their many cancellations.

However, overall the report is deficient and I was interested to see that on Monday in the Carlton Oration, a deceased gentleman, who I had the pleasure of knowing when he was a Federal member of Parliament because that's my background having worked for Federal and State MPs for 26 years until 2017, Jim Carlton was a great friend of the Industies Assistance Commission. He was pivotal in getting tariffs and quotas abolished, a great step that the PC can, you know, or its predecessors can take a lot of credit for. But Mr Moran at this Oration said:

> *Community sentiment has swung away from the primacy of light touch regulation of markets. Instead, there is increasing acceptance of a larger role for government,*

Not a philosophical position I might historically come from having worked for the Liberal Party although I've never been a member of it:

> *Including involvement in service delivery, more effective regulation and bolder policy initiatives. Australians want government to be active and collaborative players*

And then he said:

> *There should be acknowledgement that the untested and supposed superiority of the private sector is actually an illusion cultivated by rent seekers monetising service delivery opportunities*

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Commissioners, I want to give you one example of how over many years Melbourne Airport has neglected mass transit at the airport. This morning I went out to Melbourne Airport on the 7.54 Craigieburn line train from Southern Cross and with five minutes at Broadmeadows Station, I was actually at the airport in 53 minutes.

Now, admittedly that's a 15 minute frequency on the Route 901 SmartBus which I must say your researchers didn't even seem to be aware of, probably because Melbourne Airport hides it away in bay 17 of terminal 4's lower ground floor but my point simply is that people are being royally ripped off, the community's being royally ripped off by Melbourne Airport and it's not just on price.

It's on indicators such as when I went to Melbourne Airport this morning I saw terminal 4 and I noted about the lack of travelators in my submission of course and I think one or two others did as well and that's been the subject of media comment, but there's no canopies that extend, unlike say at Hawksburn or Camberwell railway stations done in 1910 by the Edwardians, you know, wonderful architectural heritage on our rail network.

But at Melbourne Airport if you walk from, as I had to this morning taking eight minutes up to the Qantas terminal, much longer with luggage, you'll find no canopies there, no weather protection when it's raining, if in fact it ever rains again in Melbourne I'm not sure. So, look it's very disappointing, Commissioners, that your report has been put together without participation from Public Transport Victoria, the RACV, Professor Graham Currie from Monash Uni, and the Public Transport Users Association and nor have Sydney's airport train, Brisbane's Airtrain, Melbourne SkyBus, Transport of New South Wales, Queensland Transport, Trans Perth, Metro Adelaide, or Adelaide Metro as they're called, and so I'm (indistinct) to make a submission.

Yet many Victorians are concerned about high car parking charges and that's not an area of expertise for me but the route 901 SmartBus is and the history of this is that in September 2010 the initial airport bus stop was in, what I term "Antarctica", opposite the freight handling area south of terminal 3, a kilometre to some terminals so I struggled with a suitcase and backpack uphill. Few passengers used it.

Today actually there were ten passengers on my bus from Broady station and that's the interchange with Metro Trains Melbourne. Coming back, Commissioners, the level of public knowledge at this particular service is so low that I had two Americans ask me, "Do we interchange for the city at Frankston?" and I very quickly told them that they didn't.

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In June 2013 after negotiations occupying PTV officials for countless hours, Melbourne Airport granted a couple of bus links for its new stop at the Qantas terminal's north end. It was a long walk to or from the Virgin check in counters or baggage carousels, that could be called the "Arctic bus stop".

Finally, when the T4 car park was built, airport management placed these buses at the extreme southerly end. This morning I think I got off in Bay 4 which is down near the south end and I got on the bus to go back to Broadmeadows Station at bay 17. The staff buses are closer to T4. Now you might say that's reasonable because there's more staff than there are Transdev Melbourne buses contracted to PTV. But infrequently timetabled shuttle buses are allowed to be closer to the airport such as those that run to, I think it's Bendigo or Ballarat, and there was one called "Stream Shuttle" there this morning which I'd never seen.

So, Commissioners, I put it to you that this an example of even the Victorian Government's bureaucrats lacking negotiating power because thank goodness, as the Minister's advisor at the time, I didn't get myself involved in the argy-bargy of negotiation and quite frankly wouldn't want to, to benefit public transport users.

So if they had any or much power it wasn't apparent to me when I worked for Terry Mulder, you know, the one Coalition transport minister that we've had in 19 years. The government owned, and if I recall still does, a small minority stake in SkyBus so SkyBus of course has got poll position at the airport, got three stops at the airport. The official mass transit, which is far cheaper at $4.40 as compared to, I think, $19.85 one way for SkyBus, doesn't.

Commissioners, so that's an example of Melbourne Airport egregiously using its huge market power to even bash down the government. So I've got absolutely no confidence under the current government that can't even provide an interchange of two new underground platforms at Osborne Street, South Yarra, our busiest station outside the five city loop ones, I've got no confidence that the Melbourne Airport mass transit arrangements will be any better.

And I say to the gentleman from Melbourne Airport, Lyell Strambi and Ms Lorie Argus, "If you've admitted as you did yesterday that there was a problem with the T4 walkway being too long and not having travelators, it's great that you've admitted that you got it wrong but why after several years haven't you fixed that particular problem?"

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And, Commissioners, I just wanted to give you another example of egregious behaviour but in this one I don't quite know whether to blame the airlines or the airports. Melbourne Airport's submission states on pages 25 and 26, "Scheduled demand exceeds runway capacity by a typical 20 per cent in the morning peak".

So when I went out to Melbourne Airport this morning, QF413 was late, QF471 was late. The delays varied on a pretty benign sort of weather wise morning between 10 and 30 minutes but it's like if you schedule more movements than you can actually have, something that the other only mode with tracks, as in a railway, would never do because, you know, the signals can only handle so many trains, the headways have to be maintained et cetera et cetera.

But Melbourne Airport doing this, because I assume it's Melbourne Airport, it's never made public prior to travel by Qantas, Virgin Australia, Jetstar, Tigerair or REX or the airport, the scheduling lacking slots implies to passengers, "You're in Sydney. You've got a CBD meeting in Melbourne at 10 o'clock. You've decided to book on the 7.30 in the morning from Sydney Qantas or Virgin or whatever, due in at 09:05 but most times the aircraft will hold at the waypoint above Mount Buller and its arrival time would be 9.15, 9.20 or later so you should really have your first meeting at 10.30 but we won't ever tell you that". False advertising, Commissioners.

Look, Commissioners, I also just wanted to raise publicly, and I know this is a matter that you may not be particularly interested in in the report, but you talk, Commissioners, about investment and one way or another I guess it's probably fair comment that passengers pay in the end. For instance, Singapore Airport because of its redevelopment it's got a per passenger charge I think it's Singapore $6.50, Hong Kong has got a similar one et cetera, that may or may not turn out to be the case in Melbourne.

Even if it isn't, we pay indirectly through higher fares which is another reason why I'm amazed that some people in the business community haven't made submissions to this sort of inquiry because I would have thought high airfares, higher than necessary airfares, affect adversely small business, big business, you name it, we all pay. Even the public service pays more for its travel.

But I'd like to know because as a community member interested in transport, and I've never actually heard from Qantas or Virgin Australia whether they agree with Melbourne Airport selecting an east-west orientation to complement the existing east-west runway 09/27 and as you probably know, Commissioners, you refer in the report briefly and rather favourably to Airservices Australia. Well, given that Airservices Australia

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says that the 48 month and 24 month delay trends for Australia's major airports are on a downhill trajectory and, you know, and you quote some figures from 2017 which is great but, you know, I can give you, as I will shortly, in the last bit, the 2018 figures and they're pretty bad but my point simply is: with very little public discussion, Melbourne Airport has said, "Well, because we don't want cross movements across the existing north runway" which I think from memory is oriented 16/34 not 09/27 like the other runway is.

We don't want cross movements so even though eventually in 2043 or whenever we're going to have the fourth runway, we'll plonk our third runway so that people in Gladstone Park, Westmeadows, Broadmeadows et cetera, actually get however many decibels, whether it's 67 or 70 or whatever, they're in the ANEF noise contours for perhaps the first time and there's been very little public discussion.

In fact I've never seen anything as to whether Qantas, Virgin Australia, BARA et cetera, favour this east-west orientation. As you probably know from May this year, I think Airservices Australia is instituting a change such that there will be many more arrivals coming in in the east-west runway.

Correct me if I'm wrong but, you know, obviously it varies enormously due to seasonal weather patterns but the north-south runway, to my way of thinking and looking at the statistics, appears to be used more at present than the east-west and, you know, whilst I don't take a lot of notice of chatter on the Internet because people generally don't want to identify themselves, there is some "minor" chatter that possibly Melbourne Airport is going to make this major investment and it will be suboptimal and I guess the test is whether or not passengers like your good selves, Commissioners, when you're going up to Sydney or more importantly you want to get back to your family and friends punctually and given that, you know, safety is a given.

I mean, we know that safety is paramount in the airlines experience and that it's a very safe mode of transport, whether it's as safe as rail is a debate for another day, but it's a very safe - far safer than me crossing Punt Road or something like that in the morning as I often do, but my point is the test is, will it improve punctuality, reduce holding, which of course environmentally wastes millions and millions of kilograms of fuel each year and so forth. And given Airservices' record, I'm not really confident that it will but they're the experts at that so if they fall down, well obviously there'll be political consequences.

But this orientation, Commissioners, runs the risk that within 15 years I believe Melbourne Airport may be facing a curfew. That was never

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envisaged by Victoria's forward thinking Liberal Premier, Sir Henry Bolte, back when Tullamarine Airport opened in 1970, yet it's a real possibility. So I merely ask, is it appropriate for the airport to forge ahead with this huge investment for which the business community will pay, leisure passengers like me will pay, you'll pay in one way or another? I don't know the answer to that but there you go.

And the last thing, Commissioners, I note that high speed rail between Melbourne, Sydney, Canberra and Newcastle is very much favoured by Anthony Albanese who I humbly submit to you is highly likely to be the next Transport Minister in Australia because quite frankly I can't, having worked for the Coalition for 26 years, I can't see that the Coalition is going to win the next Federal election. I mean, I just could not see that happening because no one will listen to Mr Abbott and he's the only person who could win the election for the Coalition in my humble view, but Anthony Albanese, who I must say was quite dismissive and some might say very rude about your particular report.

I think he dismissed it in about seven words and made some comment that I perhaps won't repeat but all I'm trying to say is: high speed rail between these locations may significantly reduce demand for air travel as it has between Barcelona and Madrid or many other city pairs, yet there's little or no analysis by anyone and there seems to be this assumption that Western Sydney Airport is going to be some saviour and in Melbourne we're going to struggle along with two runways and then get a third and, as I've said, I've got some reservations about that.

But look, the last thing I would like to say, Commissioners, your report gives a tick to airline punctuality. I find that sort difficult to sustain in arguments for - - -

COMMISSIONER LINDWALL: I'm not sure that I actually said that, but anyway.

MR CAREW: Well, I think you actually said that it's declining but - - -

COMMISSIONER KING: Yes, on-time performance is declining and most airports I think (indistinct).

COMMISSIONER LINDWALL: Is what we said, yes.

MR CAREW: No, you said here, "On-time performance has declined but remains average to high". Well, Commissioners, I don't call 27 per cent plus of Melbourne-Sydney flights in at least one direction in 2018 as found by schedule analyser OAG to be a satisfactory performance. As you know,

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you know, airports and airlines have got many constraints. We can't blame one of them for everyday but the punctuality standard, as you know, is within 15 minutes of - and I'm talking arrivals because a departure time, Commissioners, to me doesn't really matter, it's the arrival time and we can argue as to whether or not the airlines pad their schedules. The pilots say no, other people say yes et cetera, et cetera and of course the allowance between Sydney and Melbourne used to be 75 minutes northbound and now it's 85 minutes and typically 95 minutes southbound now and it used to be 85 minutes but the airlines say that's because of problems in Sydney Airport.

But the delay trend is continuing to worsen and yet this is the second busiest domestic air route in the world so I would say to you that humbly that - and this might be outside your parameters, that the community needs high-speed rail as has occurred in so many other jurisdictions.

COMMISSIONER LINDWALL: Thank you. Probably you need you to wrap up shortly.

MR CAREW: Thank you.

COMMISSIONER KING: We're running out of time.

COMMISSIONER LINDWALL: Yes, running out of time.

MR CAREW: Commissioners, my last quick point if I may: at Melbourne Airport, for instance, between Sydney and Melbourne in January 2019, holiday season, 29.7 per cent of Jetstar flights arrived at least 15 minutes late; Qantas had 18.2 per cent; Virgin had 19.2 per cent; and Tigerair was at the back of the field with 31.5 per cent of flights 15 minutes or more later.

Not satisfactory from my perspective, not satisfactory from a traveller's perspective, so I don't see how the PC can conclude that it's average to high and last thing, Commissioners, I would implore you, as many others have, to look again at your draft report and, with respect, I think read the tea leaves, read the attitude of Anthony Albanese, although you may say, you know, he's a fair bit forward and all that sort of thing, but we need a single till approach at Melbourne Airport.

I need, as a mass transit user, to see the airport not just saying it believes in mass transit, but not shoving me down to the back of the airport because I don't want to pay their favoured Skybus bus fares which aren't even available on a weekly basis unless you're an airport staff member and so the proof of the pudding, Commissioners, is in the eating but I would just hope that, as Margaret said far more eloquently than I can, that you would revise

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your report, recognise that times have changed, and that it would be egregious to continue on with the PC's historic approach, which I must say I support in many other sectors but this is a sector specific thing and maybe the airlines need to have the EU261-type compensation scheme imposed on them. I don't know, we have very little consumer protection in Australia, the domestic airlines don't even guarantee to convey us on the day of travel.

COMMISSIONER LINDWALL: You'll have to finish up there.

MR CAREW: And that's it. Thank you, Commissioners.

COMMISSIONER LINDWALL: I mean, this is an airport inquiry not an airlines inquiry nor is it a train inquiry but we'll go and check out route 901, Edmund, and I think that we will - I mean, you make a point there that it's worth looking at and some other things.

MR CAREW: Thank you.

COMMISSIONER LINDWALL: And you're right about on-time performance. I mean, if we say that it's good and you don't think it's so good, it's something we should look at as but as for this very fast train, well that's outside our (indistinct).

MR CAREW: Indeed, I understand.

COMMISSIONER LINDWALL: Thank you very much for appearing.

MR CAREW: Thank you so much, okay.

COMMISSIONER LINDWALL: And thanks for the cake.

MR CAREW: Okay, very good. Just throw it in the bin now. Thank you so much.

COMMISSIONER LINDWALL: Thank you. Does anyone - because that was our last official participant. Does anyone else want to say something, this is your opportunity? All right, well thank you all for coming, for those that have lasted.

COMMISSIONER KING: Hang on, I do think - is there anyone other than Emma has been to all of these?

COMMISSIONER LINDWALL: No, I think Emma - - -

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COMMISSIONER KING: I think, Emma, you have been here from the start.

COMMISSIONER LINDWALL: Well, and you and me.

COMMISSIONER KING: Well, yes we've got to but I think you have been her from the start to the finish.

COMMISSIONER LINDWALL: Congratulations.

COMMISSIONER KING: Which I think you deserve a cake.

COMMISSIONER LINDWALL: So, thank you. I'd like to also thank the Productivity Commission staff led by the very able boss over there, Anna, for making sure we keep on time and we asked reasonably good questions hopefully.

COMMISSIONER KING: Although she hasn't thrown anything at us which is a change from usual.

COMMISSIONER LINDWALL: And that's it for the hearings. That's the end of them and we'll continue talking to participants and look forward to our final report being tabled eventually.

COMMISSIONER KING: Thank you. And thank you to our transcriptors.

COMMISSIONER LINDWALL: And thanks to our transcriptors.

ADJOURNED **[1.15 pm]**

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