IATA Submission to the Productivity Commission's inquiry into the Economic Regulation of major Australian Airports

4 April 2011

Executive Summary

This submission presents the response of the International Air Transport Association (IATA). IATA's mission is to represent, lead and serve the airline industry and brings together 230 member airlines whose flights account for 93% of all international scheduled air traffic.

IATA welcomes this opportunity to submit its comments in response to the Productivity Commission's Issues Paper on Economic Regulation of Airport Services. IATA's comments are from an international perspective and are based on the requirements of, and practice in, international civil aviation.

This is a summary of the IATA position:

Part 1: Issues with the current regulatory model

- Australian airports generally have high profitability and a tendency to increase charges wherever possible.
- There are no adequate incentives for the airports to reach fruitful commercial agreements with airport users.
  - Price monitoring is not effective.
  - Proper commercial negotiations are lacking.
- There are no clear rules on asset allocation between aeronautical and non-aeronautical activities.
- There is an abuse of the investment process (NNI process) allowing the airports to increase charges on an ad-hoc basis.
- There is a lack of transparency on financial information and detailed accounts.
- Regulation omits the key aspect of aviation fuel supply which if allowed to deteriorate in its reliability and efficiency, will load significant costs on the industry.

Part 2: Opportunities for improvement

- Need for more transparent and effective consultation
  - ACCC to conduct a detailed investigation on Sydney airport pricing policies
  - Provide better visibility on financial information and detailed accounts
  - Improve the investment process (NNI)
  - Agree financing of assets vs pre-financing
  - Provide access to arbitration
  - Extend the regulation to airports where risk of market power exists (e.g. regional airports)
- Set productivity targets
- Ask for an independent review of the monitored airports' WACC
- Need for more rational asset allocation
- Ensure the regulation is flexible and allow traffic risk sharing
- Use Key Performance Indicators to track the quality of service

Part 3: Airport planning

- Terminal buildings should be of modular design and IT systems assessed to increase capacity.
- Airport Master Plan should identify and safeguard land required for future development.
- Adequate "inter-modal" transport system required to support present and future airport throughput.
- Airports need to assess support services and determine whether their operational status necessitates a need to be within the immediate vicinity of the airport, or, can be delivered within an acceptable distance off the airport.

Part 4: Reliability and efficiency of aviation fuel supply

- Fuel supply infrastructure development lags behind growing aviation fuel demand particularly with increasing reliance on imports.
- Fuel infrastructure ownership by vested parties in fuel supply impacts effective competition.
- Government intervention is urgently needed for key fuel infrastructure to create true open access, mandate stakeholder consultation on planning and development, and incentivize timely investment.

For clarity purposes, all the questions contained in the Productivity Commission's Issues paper will be listed in a summary table. The IATA position will be covered under the relevant question including references to specific parts of this document.

For additional information or clarification, please contact:

Vinoop Goel
Assistant Director
Industry Charges, Fuel & Taxation
Tel. +65 6499 2261
Fax. +65 6415 1259
goelv@iata.org

International Air Transport Association
111 Somerset Road, #14-05 Somerset Wing
Singapore Power Building
www.iata.org

Magali Collot
Manager
Airport & ATC Charges
Tel. +41 22 770 2759
Fax. +41 22 770 2689
collotm@iata.org

International Air Transport Association
Route de l'Aéroport 33, P.O. Box 416
1215 Geneva 15 Airport, Switzerland
www.iata.org

Questions and Answers table

Questions	IATA Position
The Economic Regulatory Regime	
Price monitoring	

Questions on topic 1:
Is there evidence that the price monitored airports have increased charges by more than could be justified on the basis of costs, new investment requirements, and/or other enhancements to service quality? What is the ability of airports to vary prices year on year given many have long term contracts with airlines? Is price monitoring providing a constraint on aeronautical charges at the major airports?
 	
Questions on topic 2:
Has the need to adjust the previous FAC's pricing legacy been fully accommodated? Has the price monitoring regime promoted efficient investment and facilitated commercially negotiated outcomes? How would it compare relative to counterfactuals of explicit price regulation, or no regulation? Does the information emerging from the price monitoring process assist commercial negotiations between airports and their customers?
 	
Questions on topic 3:
Has the 'line in the sand' for asset valuations been effective or have airports, airlines or other users encountered problems with this approach? Should the line in the sand be extended to other airports? Is there a better alternative approach?
 	
Questions on topic 4:
How adequate are the data in the ACCC's price (and quality) monitoring reports for judging the effectiveness of the monitoring regime? Are the regulatory accounts provided by the airport operators sufficient to reveal monopoly pricing and rates of return? Are there material gaps or limitations in that data and can they be practically remedied? What other data sources should the Commission use in its assessment of the price (and quality) monitoring regime?
 	
Questions on topic 5:
Are the ACCC's monitoring methodologies appropriate? Is there adequate consultation with the monitored airports?
 	
Questions on topic 6:
How do recent charges for aeronautical services at the price monitored airports compare with those at comparable international airports? What conclusions can be drawn from international comparisons of airport performance?
	- Price monitoring is not effective or efficient in preventing airports from realizing windfall gains (see section 1.2.1).
	- The current price monitoring regime has lead to the following main issues:
	  - Australian airports generally have high profitability and a tendency to increase charges wherever possible (see section 1.1 and annexes 1&2).
	  - No adequate incentives for the airports to reach fruitful commercial agreements with airport users (see section 1.2).
	  - No clear rules on asset allocation between aeronautical and non-aeronautical activities (see section 1.3).
	  - Abuse of the investment process (NNI) allowing the airports to increase charges on an ad-hoc basis (see section 1.4).
	  - Lack of transparency on financial information and detailed accounts (see Section 1.5).
	- "Line in the sand" for asset valuations should apply to all monitored airports but past revaluations continue to impact future charges as they are contained in the existing asset base.
	- The data in the ACCC's airport monitoring report is not adequate to judge the effectiveness of the monitoring regime.
	- Need more detailed information through transparent and meaningful consultation (see section 2.1):
	  - Need to put in place Service Level Agreements (SLAs) (see section 2.6).
	  - Monitor airport service delivery through Key Performance Indicators (KPIs) (see section 2.6).
	- Comparison of recent charges for aeronautical services at International airports is provided in annex 2.

Compliance costs	
Question 7: What are the compliance and administration costs associated with fulfilling the regulatory obligations imposed by the price and service quality monitoring system?	- There is a need for the current economic regulatory regime to be strengthened. - The regulatory instrument should not, however, be cost or resource intensive.
Car park price monitoring	
Questions on topic 8: What percentage of passengers use the airport's car park facilities? What is the level of competition from other sources of transport? Are off-site car parks a real source of competition to the airport car parks? Is there evidence that airports are influencing the level of competition from alternative transport modes? Questions on topic 9: Has the pricing behaviour of airports indicated the use of market power in car parking? Do the price increases reflect monopoly rent, locational rent (e.g. accounting for the opportunity cost of alternative uses of land dedicated to car parking), or both? Are monopoly profits evident for short-term, long-term, or all forms, of parking?	- Car park facilities should be part of the aeronautical revenues. - Car park costs lead to increased cost of travel. - Natural monopoly activities such as car park facilities need to be regulated.
Service quality monitoring	
Questions on topic 10: How responsive have the monitored airports been to users' service needs and preferences? Are there any significant quality problems for services under the control of the airports that are not being addressed? Have necessary new investments been made in a timely fashion? How does the quality of service at the monitored airports compare with comparable international airports? Questions on topic 11: How robust are the survey techniques in indicating quality of service? How useful is quality of service monitoring given the differentiation between DTLs and common user facilities, and how would this affect international comparisons?	- The monitored airports have not been very responsive to users' services needs and preferences (see section 1.2.2 & 1.4). - Need to enforce SLAs and KPIs linked to pricing with penalty clauses (see section 2.6).
Access arrangements	
Question 12: Has the Federal Court's interpretation led to Part IIIA becoming the operative regulatory instrument for the major airports or has the threat of potentially easier recourse to Part IIIA 'conditioned' negotiations between airports and airport users, or has it had little impact? Question 13: Have recent legislative changes (in 2006 and 2010) addressed concerns that Part IIIA could supplant price monitoring as the operative regulatory instrument?	- No impact on negotiations between airports and airport users. - Need to have easy and effective access to arbitration (see section 2.1.5). - The regulatory instrument should not be cost or resource intensive.

Future arrangements	
Is a further period of price monitoring needed?	
Questions on topic 14: At a broad level, is there value in continuing the monitoring of aeronautical services and/or parking prices? Is there evidence that the current light-handed approach has not been successful in addressing market power concerns, and if so, what alternatives are available? Is both price and service quality monitoring needed? Questions on topic 15: Should there be a fixed duration for any future period of price monitoring? Are further prescheduled reviews necessary? Questions on topic 16: If there is a further period of monitoring, are there opportunities to streamline arrangements to improve reporting, without compromising effectiveness? Could the number of indicators be reduced? In some areas, would more information be desirable? Do reports need to be produced annually?	- Price monitoring has not encouraged greater efficiency and has not been a sufficient constraint on airport market power (see section 1.2.1). - Need to have better visibility on financial information (see section 2.1.2). - The NNI process should be improved (see Section 2.1.3).
Market power	
Questions on topic 17: Have there been changes in the overall market power enjoyed by any of the price monitored airports and if so why? For example, do Avalon and Gold Coast airports materially reduce the market power of Melbourne and Brisbane Airports? Questions on topic 18: What are the constraints on the airports' market power? Do the airlines have countervailing power in dealing with the airports, especially smaller airports? Questions on topic 19: If monitoring was to continue, should some airports be removed from, or added to, the list of monitored airports? If airports are removed, would the second tier self administered scheme, or some other web-based self-reporting regime for the major airports, suffice? Questions on topic 20: Are the definitions of aeronautical services appropriate in reflecting market power in particular services? Should some services be excluded or others included? What is the market power of the major airports in relation to car parking prices?	- Each of the price monitored airports serves different regions and markets. These airports, therefore, do not compete with each other. - Even if 2 airports served the same market, high costs would be incurred if an airline decides to move to another airport. Additionally, existing capacity constraints would make it even more difficult. - The price monitored airports remain, therefore, natural monopoly providers. - The regulation should be revised to include more airports such as regional airports (see section 2.1.6). - Need to set productivity targets (see section 2.2). - Ask for an independent review of the monitored airports' WACC (see section 2.3). - Need to have more rational asset allocation between aeronautical and non-aeronautical activities (see section 2.4). - The regulation should be flexible and allow traffic risk sharing (see section 2.5). - Although aviation fuel supply is a non-aeronautical service, there is a need to ensure that aviation fuel can be delivered in a safe, reliable and efficient manner (see section 4).

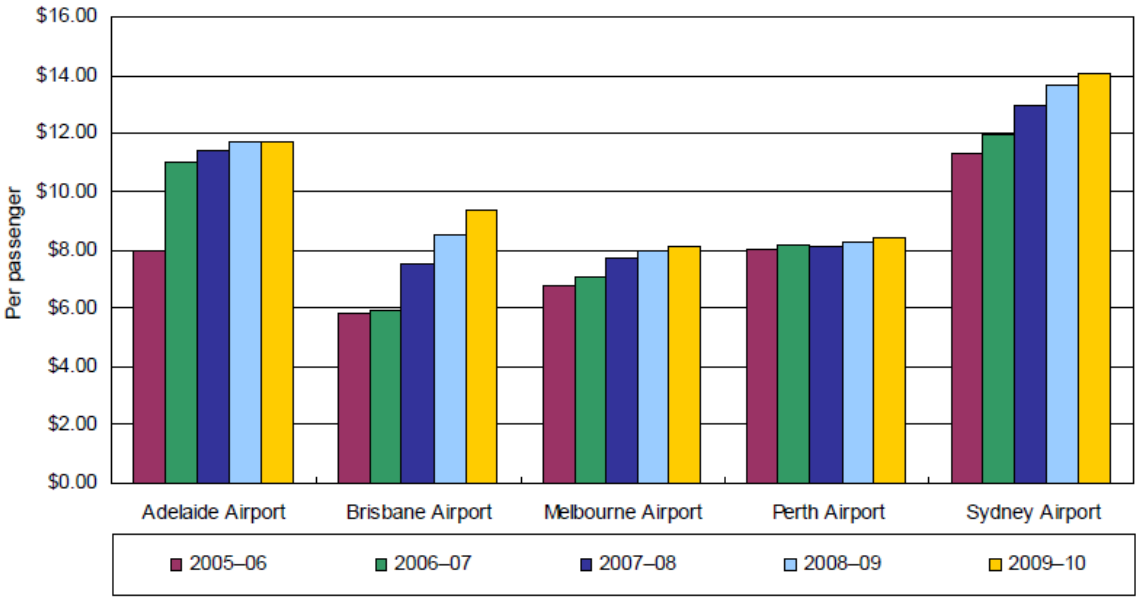
Deterrent and remedies	
Questions on topic 21: Is the existing range of remedies effective in deterring misuse of market power? Are these remedies effective 'punishment' for misuse of market power? Questions on topic 22: What impact does the lack of a 'show cause' process have on ensuring appropriate pricing and investment outcomes for aeronautical services? Is there a better approach to developing a 'show cause' process or an alternative trigger process? Would there be benefits in a requirement for independent commercial arbitration and if so, how could this be effected? Are there any public interest reasons for such arbitration to be conducted by the ACCC? Question 23: Do concerns about the potentially adverse effects of more heavy handed price regulation on investment militate against its reintroduction?	- The existing remedies are not effective in deterring misuse of market power or "punishment" for misuse of market power. - Little impact of "show cause". - Independent commercial arbitration is needed but should not be as resource intensive as the current ACCC process (see section 2.1.5). - The regulation should ensure transparency, meaningful consultation and access to 3rd party arbitration (see section 2.1).
Airport planning regulation and transport	
Transport linkages to airports	
Questions on topic 24: The terms of reference request the Commission to focus on the provision of passenger transport services at and surrounding main passenger airports operating in Australia's major cities. Which major cities should the Commission focus on — those housing the five price and service monitored airports, all capital cities or some other combination? Should potential links between airports (such as Canberra and Sydney or Melbourne and Avalon) be examined? Questions on topic 25: Are planning and development regulations working effectively? Can 'excessive' or 'inappropriate' economic development at airports impinge on effective transport linkages to and from airports, or might such development facilitate better transport linkages? Questions on topic 26: What mechanisms exist at airports to coordinate with local and state governments on planning issues? Can more be done by airports and governments to better coordinate planning of transport options? Will recent changes to legislation to impose additional requirements on airport Master Plans (such as ground transport plans) help to alleviate past problems? Questions on topic 27: What transport options exist at the major airports in Australia? Are these reliable, frequent and cost effective services? Are they integrated into the suburban transport network? To what extent are they used relative to private cars? Is there evidence that land transport service providers (such as taxis, shuttles, off-airport car parking providers) are impeded unduly in gaining access to airports? Are charges and conditions of access to airports (e.g convenient pick-up and drop-off points) appropriate? Is there a need to monitor such terms and conditions?	- Terminal buildings should be of modular design and IT systems assessed to increase capacity (see section 3.1). - Airport Master Plan should identify & safeguard land required for future development (see section 3.2). - Adequate "inter-modal" transport system required to support present and future airport throughput (see section 3.3). - Airports need to assess support services and determine whether their operational status necessitates a need to be within the immediate vicinity of the airport, or, can be delivered within an acceptable distance off the airport (see section 3.4).

1 Issues with the current regulatory model

1.1 Australian airports generally have high profitability and a tendency to increase charges wherever possible

- Average prices have increased over the 5-year period 2005-06 to 2009-10 at the 5 price monitored airports. The increase in traffic over the same period (see chart 2.2.1 – Volume of passengers in annex 1) should have lead to a reduction in charges if the current regulatory model was efficient.

Chart 2.2.5: Average prices (aeronautical revenue per passenger)

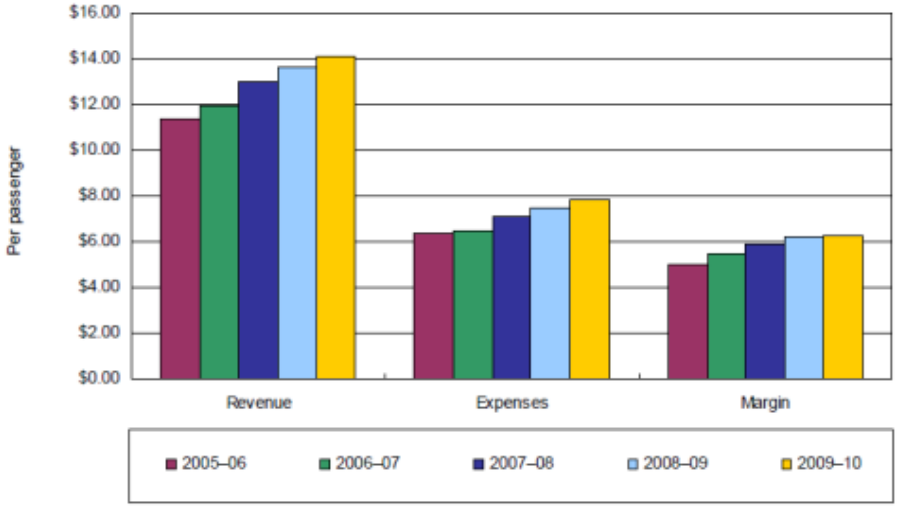


Source: ACCC's Airport monitoring report 2009-10 (page 25)

- From the ACCC's airport monitoring report 2009-10, passenger traffic at Sydney airport decreased in 2008-09 whilst aeronautical revenues increased during the same year (see chart 8.1.1 – Sydney airport – volume of passengers, tonnes landed and aircraft movement in annex 1).
- Additionally, Sydney airport's operating margin per passenger increased by 25.6 per cent over the 5-year period, which was driven by a higher growth in revenue compared to expenses.

Aeronautical revenue, expenses and margin per passenger

Chart 8.1.2: Sydney Airport—aeronautical revenue, operating expenses and operating margin per passenger



Source: ACCC's Airport monitoring report 2009-10 (page 260)

- Sydney airport has indeed increased profits by permitting service quality levels to fall below that which could be expected in a competitive environment over a sustained period.
- This fact appears under the key points of the ACCC's airport monitoring report 2009-10 which lead the government to bring forward a planned review of the current regulatory model.

Section "COMMERCIAL IN CONFIDENCE" – see in Annex 2

1.2 There are no adequate incentives for the airports to reach fruitful commercial agreements with airport users

1.2.1 Price monitoring is not effective

- With price monitoring the only constraints on airport pricing are the threat of re-regulation and the shareholdings of local government, who may be concerned to attract tourists.
    - The reason this is the only constraint is that there is clearly no competition and considerable market power for the main Australian airports. Population density and geography means that passengers or airlines would have to travel hundreds of kilometers to the closest alternative to any main airport.
    - Even large airlines with a large share of traffic at an airport have little countervailing power in negotiations with airports. Unless they have a feasible alternative to switch to they have no power in negotiations.
- Critiques by the ACCC report and Prof Peter Forsyth [1], University of Monash (2006), conclude that "*if the objective was to keep prices close to costs and minimize the use of market power the system may be seen as less successful.*" Price monitoring has not been a sufficient constraint on airport market power. Airport charges at Sydney airport have increased well above costs as evidenced by the high EBIT and EBITDA margins (see annex 2) while delivering sub-standard quality.
- A second critique is that price monitoring has not encouraged greater efficiency. Assets are used very inefficiently at Sydney airport (see annex 2). Much less revenue is generated per $ of asset than in other countries which could partly be a reflection of spare capacity.

1.2.2 Proper commercial negotiations are lacking

- The current regime does not allow for proper commercial negotiations between airlines and airports due to the bargaining power imbalance that comes from airports' natural monopolies. As such, it has been reported that the quality of negotiations has deteriorated over time with the monitored airports.
- Key aspects of the commercial agreements are largely determined once every 5 years when new agreements are negotiated.

1.3 There are no clear rules on asset allocation between aeronautical and non aeronautical activities

- The lack of clear rules about cost allocation does not provide the level of transparency necessary. This could lead to different interpretations resulting in further deterioration of the commercial negotiations between the monitored airports and the airlines.
- Furthermore, the rational for changes between aeronautical and non aeronautical activities are not clearly communicated to the airlines. As an example and as mentioned in the ACCC report after chart 8.1.4, *"Sydney Airport advised that the decrease in non-aeronautical revenue from $681.2 million in 2008-09 to $411.6 million in 2009-10 was due to the airport preparing the accounts on a group consolidated basis in 2009-10. This resulted in the removal of intercompany dividends received from the accounts in that period, which Sydney Airport included in other non-aeronautical income in previous periods."*

[1] Key Policy Issue – Light-handed regulation of airports: the Australian experience – April 2007 http://www.iata.org/whatwedo/economics/Pages/outside_views.aspx

1.4 There is an abuse of the investment process (Necessary New Investment – NNI process) allowing the airports to increase charges on an ad-hoc basis

- Airport investments have a significant impact on airport users and costs to passengers. Without effective open communication between all parties there is a real danger that individual strategies will result in unnecessary and expensive investments, resulting in over-capacity issues and unnecessary cost increases for airlines and their passengers.
- In Australia, there is a lack of proper consultation regarding especially the price monitored airports for long-term investments. Sydney airport, for example, has refused to develop a committed 5-year CAPEX program for the purposes of establishing an aeronautical price path over the 5-year period. Sydney airport also tends to under invest in its asset infrastructure as there are still some uncertainties linked to the new airport or 2nd airport.
- The existing NNI process is not subject to regulation and the price monitored airports are using a building block model for their infrastructure plans which is not necessarily aligned to the airline users needs.
- Moreover, there is an abuse of the NNI process as certain investments related to maintenance or replacement are sometimes included in this process which should only focus on new investments.
- It must also be noted that there are some cost allocation issues as certain investments such as public roads are currently largely funded by the aeronautical revenues.
- All the above elements lead to higher airport charges.

1.5 There is a lack of transparency on financial information and detailed accounts

- The data in the ACCC's airport monitoring report 2009-10 is not adequate to judge the effectiveness of the monitoring regime.
- This issue is highlighted in the report itself under section 2.7.4 as follows: *"…the historical accounting data contained in the airports' regulatory accounts may not represent a reliable measure of the efficient long-run costs of providing aeronautical services. It follows that a comparison of aeronautical revenue and profit data with the available cost information is only a partial indicator of the 'reasonableness' of the airports' returns. As such, a comprehensive evaluation, which is beyond the scope of monitoring, would be required to measure the airports' economic returns on aeronautical services and determine conclusively in each instance whether or not the airports are earning monopoly profits."*

2 Opportunities for improvement

The current regulatory regime would be improved with the following recommendations.

2.1 Need for more transparent and effective consultation

2.1.1 ACCC to conduct a detailed investigation on Sydney airport pricing policies

- The Australian government has brought forward the review of the Productivity Commission given the concerns it has on the commercial conduct of Sydney airport.
- In order to remedy this specific situation and as a first step, the regulator should direct the ACCC to undertake a detailed review of Sydney airport's commercial conduct.
- Based on the detailed review, the regulator could then decide how to improve the economic regulatory regime in Australia.

2.1.2 Provide better visibility on financial information and detailed accounts

- Airlines need adequate information to evaluate the operational and financial performance of an airport in order to identify mutually beneficial improvement opportunities.
- The ACCC reports mentions under 2.7.4 that:
    - *"in order to determine conclusively whether or not the airports are earning monopoly profits from aeronautical services, the airports' aeronautical revenue and profit data needs to be considered against the efficient long-run costs of providing those services."*
- The price monitored airports should, therefore, provide additional financial information and especially more detailed accounts. This would improve transparency and lead to more meaningful consultation with the airlines.
- As a minimum, the following financial data should be transparent to airlines:
    - Cost base calculations for the setting of charges
    - Traffic and revenue detailed breakdown
    - Historic financial statements
    - Aeronautical operating costs breakdown
    - Aeronautical asset base, capital expenditure and depreciation
    - Revenue segments – aeronautical/commercial
    - Corporate financial structure and shareholder commitments
    - Unit costs and productivity metrics and targets

2.1.3 Improve the investment process (NNI)

- Investments falling into the Necessary New Investment category should be clearly defined and classified.
- All the Necessary New Investments should be listed for each airport and clearly discussed with the users.
- Additionally, there should be proper consultation with the airlines on the 5 to 10 years capital investment plans of each price monitored airport.
- IATA believes that airport capacity development should form an intrinsic part of a stakeholder agreed Airport Master Plan. Capacity improvement must be demand led, i.e. facilities should be functional, modular, expandable and appropriately sized to suit airline needs and built only when there is a proven need.
- Discussions between the price monitored airports and the airlines should take place and show the relevance of the 5-year plan with regard to longer term plans.

- Each airport should provide enough information to determine:
    - o The necessity for each of the investment projects
    - o That it has been developed in the most cost-effective manner
    - o How the investment will be financed
    - o The impact on airport charges

- The price monitored airports could put in place an operational committee by terminal when applicable. The role of each committee in terms of investment should be to review the investment projects at terminal level over a 12-month period. This process, which was introduced recently at Aéroports de Paris, should provide more transparency, ensure investments are cost effective and meet future requirements in addition to improving on-going communication with airlines.

2.1.4 Agree financing of assets vs pre-financing

- Financing of assets should be agreed in advance with users through a formal and open consultation process.
- Pre-financing of investment directly through charges increases the cost of air transportation. It is inefficient, unnecessary and unfair since those airlines paying are not necessarily those who will benefit. Airlines should only pay for agreed investments on an as and when used basis. This will require airports to develop other means of financing their capital expenditure programmes.

2.1.5 Provide access to arbitration

- An independent appeal body should be available in the event of a dispute between the airports and airline users.
- The Australian government should ensure that consultation is a process and not an event where a decision already made is merely announced and subsequently implemented. The goal of consultation should be to reach consensus between the airports and airline users.
- Any unresolved issues between airports and airlines should be addressed as part of the consultation process prior to airport charges being finalized.
- European member states are now required to have an appeal process in place through an independent supervisory authority for unresolved disputes related to the modification of airport charges as per the EC Airport Charges Directive 2009/12/EC.

2.1.6 Extend the regulation to airports where risk of market power exists (e.g. regional airports)

- The regulation in Australia should be extended to airports wherever the risk of market power exits.

2.2 Set productivity targets

- Efficiency is a primary requirement and fundamental to the delivery of effective regulation. It should be ensured that services and facilities operate efficiently and are not provided at a higher cost than necessary.
- As price monitoring has not encouraged greater efficiency, IATA suggests a cost efficiency target of X percent on average per year.
- This target could be appropriately set once the detailed review of Sydney airport's commercial conduct has been completed (see section 2.1.1).

2.3 Ask for an independent review of the monitored airports' WACC

- The cost of capital must be set at an appropriate and realistic level that ensures the most cost effective method of financing the airport.
- The Australian government should review the principles laid down by the ACCC dating back to 1998 and ensure that a proper independent review of the monitored airports' WACC is conducted.
- The values of some of the parameters should take into consideration the following elements:

  Risk free rate:
  - Government index linked bonds should be looked at. A 10-year average shows 2.9% and a 5-year average shows 2.5%.
  - Another way would be to use Australian government bonds of similar maturity to infrastructure provider's debt (e.g. average of 5 and 10-year nominal bond yield).

  Cost of debt:
  - The credit rating should be appropriate. The spread should be forward looking and not based on the 2008-2009 period when spreads were blown out of proportion by the exceptional financial crisis.

  Gearing:
  - The calculation should use an actual leverage instead of a notional leverage as was used previously at Sydney airport.

  Equity market risk premium (ERP):
  - Australian infrastructure providers are accessing global equity markets and not just local Australian savers funds. It is, therefore, appropriate to use the world average ERP which gives an average of 5.1%.

  Asset beta:
  - The asset beta should be representative of history, the next 5 years or what investors will be looking for. As an example, the London airports have an average asset beta of 0.53. Bloomberg estimates that Sydney airport's asset beta is close to zero based on the past decade and gives a forward looking asset beta of 0.3.

2.4 Need for more rational asset allocation

- There is a need to have more rational asset allocation between aeronautical and non-aeronautical activities.
- On the one hand, car parking, retail in terminal building and other revenue streams from passengers should be included in the aeronautical revenues. It is reasonable to assume that in the absence of aeronautical services there would be no market for non-aeronautical services such as retail and car parking. Thus aeronautical services are primary drivers for non-aeronautical services.
- Given that the non aeronautical revenues are dependent on passengers travelling on airlines and coming to the airport, they need to contribute to the aeronautical revenues. A percentage of non aeronautical profit should, therefore, be used to defray the costs of aeronautical services.
- On the other hand, land transport infrastructure to the airport should be partitioned to recognize non-aeronautical contribution of commercial users.
- When clear allocation rules exist, these should be audited by an independent entity and communicated to the airlines.

2.5 Ensure the regulation is flexible and allow traffic risk sharing

- The monitored airports should encourage airlines to increase traffic.
- If traffic increases above the initial forecast, the airport should share the benefit from this increased growth in the form of reduced charges.
- As an example, an agreement in traffic risk sharing exits at Frankfurt airport for 2012-2015 that takes into account the possibility for traffic at the airport to develop faster than expected whereby airlines will be reimbursed one third of the additional revenue.
- In order to conduct this exercise successfully, it will be important for the price monitored airports and airline users to reach an agreement on the 5-year traffic forecast.

2.6 Use Key Performance Indicators to track the quality of service

- The key aspects of the service provided by an airport should meet agreed quality and operational performance standards. These standards should be contained in a service level agreement between an airport and its airport users, which should also encourage continuous improvement and detail penalties for non-compliance.
- There is a need to put in place Service Level Agreements (SLAs) at the price monitored airports in order to encourage improvements. SLAs are a useful tool for defining the terms of engagement or rules that will govern the relationship between the airport and its airline partners. The airport and airlines should agree which services and what level of performance should be provided in exchange for the charges paid for their use. The parties also need to agree how success or failure will be measured. Through the SLA, airlines are contracting to an agreed level of service.
- Manchester airport has put in place SLAs in consultation with airlines for a long time now. These SLAs are still working well as they are simple to understand, measure and administer. BAA has also used a similar approach after experiencing some service level issues. The standards of service condition for both Heathrow and Gatwick airports are reviewed with the airlines as part of the consultation process. New indicators have been added whilst several existing indicators were given more stringent targets.
- Airport service delivery should also be monitored through Key Performance Indicators. The monitored airports should agree with the airlines the most relevant global indicators to monitor. Some indicators could also be monitored at terminal level.
- As mentioned under section 2.1.3, Aéroports de Paris has put in place an operational committee by terminal. The role of these committees in terms of quality of service is to monitor on a regular basis the quality of service indicators agreed at both global and terminal level. This process enables to involve airlines, track progress and agree on concrete action plans to improve the quality of service at each terminal.

3 Airport planning

3.1 Terminal buildings should be of modular design and IT systems assessed to increase capacity

Passenger traffic at airports is set to continue to grow worldwide in the region of circa 5 to 6% per annum. To address this growth, airports will need to constantly review their Airport Master Plan (AMP) to ensure that airport infrastructure capacity demands is made available on a Just in Time basis. Land identified for future development should be safeguarded to meet the demands of airport development.

Airports should where feasibly possible, design facilities around a modular design. In doing so will considerably reduce the inconvenience to the travelling public.

Airports nearing capacity should seek to introduce IT solutions where practicable as a way of delaying the inevitable need for expansion. The use of automated check-in facilities, pre screening regulatory processing lanes and e-ticketing will address growth within the same foot print of a terminal facility, providing for an additional 5% to 10% of passengers capacity.

Major city airports that are land constrained need to ensure that all on site businesses fall into essential. The airport should determine the type of airport *it is to be* for the future, and look to divest those elements that do not fall into core. The likes of flying training, general aviation, military and point to point traffic could be accommodated at a smaller airport.

Cargo warehousing with appropriate security controls in site could be developed off site, along with catering, airline offices etc. Aircraft maintenance and point to point cargo operators should also be reviewed.

3.2 Airport Master Plan should identify and safeguard land required for future development

The land surrounding airports should be safeguarded for future expansion. No matter how far an airport is cited from a large populous, history has shown that those who work at the airport prefer to live within a reasonable distance to the airport.

A reasonable sized airport will create circa 1000 jobs per million passengers as a rule of thumb. As a consequence, as the airport develops 10,000 jobs per 10 million passengers and thereafter in multiples provides a good indication that a small town will be required to support.

Planning applications must take into account the closeness of new build to an airport and in particular the height of buildings. The conditions pertaining to the Control of Obstacles is available in ICAO Doc 9137-AN/898 Part 6.

On the direct approach to airports, the avoidance of buildings that contain large number of persons should be avoided, e.g. schools, hospitals etc as a precaution in the event of a major incident occurring.

3.3 Adequate "inter-modal" transport system required to support present and future airport throughput

Airport Master Plans (AMP) need to be developed to cover a time span of a maximum of 15 to 20 years. Beyond this time frame is unrealistic given the speed of changes within aviation in the development of new types of aircraft and the introduction of new IT systems.

Airports need to be provided with an inter-modal travel system that will support the growth and development of the airport in relation to the size of development outlined within the AMP. Of particular interest, should be in matching the passenger throughput numbers and in ensuring that the road and rail infrastructure is able to adequately support.

Inadequate inter-modal infrastructure will witness severe delays being created and a severe loss of revenue being inflicted on the airlines and airport.

3.4 Airports need to assess support services and determine whether their operational status necessitates a need to be within the immediate vicinity of the airport, or, can be delivered within an acceptable distance off the airport

Where land is at a premium, the airport should determine what service is considered ''core'' and needs to be located on the immediate airport site. Services deemed as non core should be relocated off airport in doing so releasing land for core activities.

Off site employee car parking, cargo warehousing and airline stores are just some of the services that should be considered. The introduction of a rapid passenger transit system will reduce the need for private vehicles to enter the core area. Road infrastructure will be required for the delivery of goods and where possible should be on a dedicated basis.

4 Reliability and efficiency of aviation fuel supply

Aviation fuel supply at an airport is traditionally treated as a non-aeronautical service and normally not subjected to the same rigors of economic regulation as airport aeronautical services. This, however, should not diminish the need to ensure that aviation fuel can be delivered in a safe, reliable and efficient manner into the wing of the aircraft especially given the fact that aviation fuel is an indispensable part of flight operations and its cost forms a major component of an airline's operating cost. An unreliable and economically inefficient aviation fuel supply system will invariably load significant costs on consumers and the industry.

In Australia, aviation fuel supply has been plagued by concerns over supply reliability and price efficiency.

- In the past eight years, fuel differential (the component of the fuel price paid by airlines over and above the international market price) had risen steadily. Fuel differentials that airlines pay at Australian airports are significantly higher than those paid at the main airports in the Asia Pacific region such as Singapore, Kuala Lumpur, Jakarta, Bangkok and Hong Kong.
- There has been a number of high profile occurrences of fuel shortages at Sydney airport (in 2003, 2005 and 2009) and Melbourne airport (in 2008 and 2010) as well as constant threat of fuel supply disruptions. Besides the additional operational costs incurred when a fuel disruption happens, there is also the erosion in confidence of airlines to plan for future growth to the airport.

The concerns over supply reliability and effective competition culminate from the current Australian aviation fuel supply landscape which is characterized by the following:

- Aging refineries with relatively poor yields have not been upgraded or supplemented with modern refineries. As such, there has been a growing reliance on imported jet fuel. Supporting infrastructure for product import such as ship berthing facilities and tankage storage at import terminals have not been sufficiently boosted to keep pace with growing imports.
- The most efficient way for transporting jet fuel is by pipelines but it is common for key pipeline infrastructure to the airport to be owned by individual oil companies. There is little incentive for pipeline owners to invest in pipeline capacity substantially beyond their own needs. Consequently, as the pipeline owners' own needs grow amid growing market demand, the pipeline capacity available to competing fuel suppliers would have to shrink. This has an effect of stifling competition.

The current status of the aviation fuel supply landscape has not yielded the necessary supply reliability or price efficiency one would expect from an open market economy like Australia. The absence of new supplier entry into the Australian aviation fuel market at least for the last twenty years (other than the entry of Qantas as a self-supplier in Sydney) is symptomatic of a less than dynamic market that could bring about complacency and inefficiency.

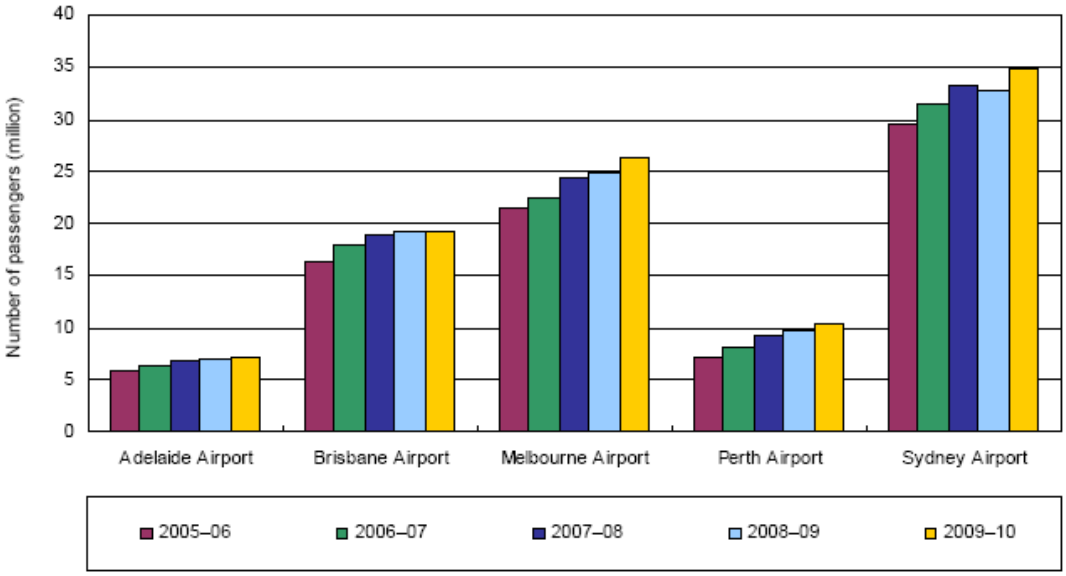
A more dynamic fuel supply market is the solution to the industry's woes of nagging supply reliability concerns and cost and price ineffiencies. Freeing up the supply bottleneck brought about by a conflict of interest in fuel infrastructure ownership will go a long way towards achieving this end.

The government needs to step in to:

- Regulate on-airport and off-airport fuel infrastructure ownership to ensure true open market access and a level playing field for fuel suppliers.
- Mandate stakeholder (airport, fuel suppliers and airlines) consultation for fuel infrastructure planning and development and in the determination of cost-based fuel charges in accordance with ICAO principles.
- Incentivize timely investment in fuel infrastructure (such as pipelines, on and off airport storage, and import facilities) to ensure that future demand growth can be adequately catered for.

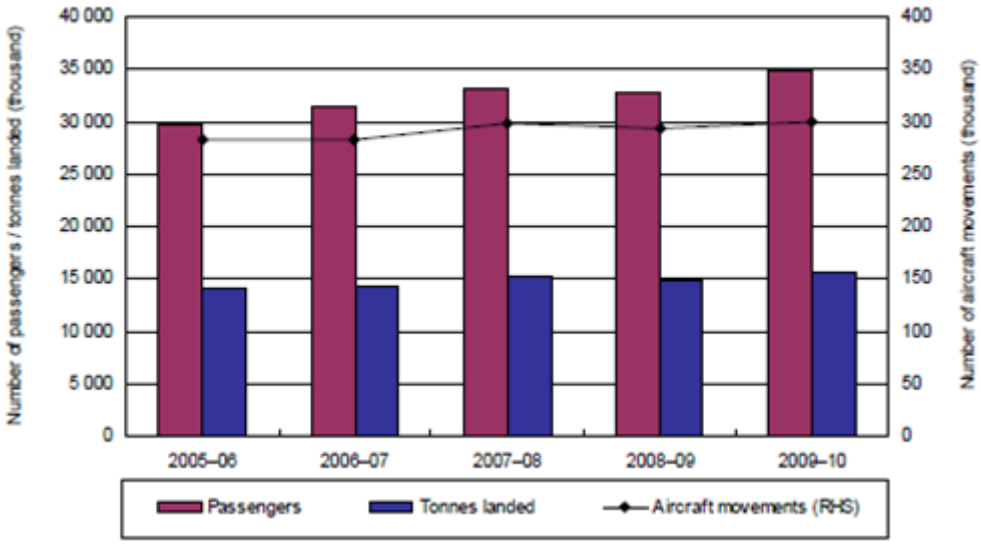
Annex 1

Chart 2.2.1: Volume of passengers



Source: ACCC's Airport monitoring report 2009-10 (page 22)

Chart 8.1.1: Sydney Airport—volume of passengers, tonnes landed and aircraft movements



Source: ACCC's Airport monitoring report 2009-10 (page 254)