Economic Regulation of Airport Services
Submission to the Productivity Commission Inquiry

Sydney Airport Corporation Limited ('Sydney Airport')

08 April 2011

Sydney Airport - Gateway to Australia

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STRUCTURE OF THIS SUBMISSION – PUBLIC VERSION

This submission is structured along the major themes of the Terms of Reference.

Chapters 1 to 3 discuss the aviation industry.
Chapter 1 describes the importance of the aviation industry and the benefits Australia is already receiving from the progressive deregulation of the industry over the past two decades.
Chapter 2 describes the changes to the aviation industry over recent years – including a significant increase in both the need for flexibility and airport competition – and the importance that the regulatory framework does not inhibit collaboration, competition and flexibility.
Chapter 3 outlines the regulatory framework within which the airport operates and the implications for economic regulation and efficient use of the airport.

Chapters 4 to 6 discuss the performance of Sydney Airport since the introduction of light-handed regulation.
Chapter 4 demonstrates the benefits of light-handed regulation in the aeronautical business, including significant investment, multi-faceted commercial agreements, service level initiatives, and stable and reasonable airport charges.
Chapter 5 demonstrates the need for, and current lack of, adequate land access to the airport boundary.
Chapter 6 looks in more detail at airport access within the terminal boundaries – including car parking – and demonstrates the significant improvements made to all airport access options by Sydney Airport.

Chapter 7 discusses effective airport monitoring and recent ACCC Airport Monitoring Reports
This chapter considers the principles and potential benefits of effective airport monitoring, and recent ACCC Airport Monitoring Reports. An alternative scheme of monitoring based on a robust and independently verified methodology is proposed which would provide more useful and timely information, avoid the publication of misleading information, and have lower administrative costs.

Chapter 8 presents Sydney Airport's recommendations.

Appendices and Attachments
Appendix A provides a cross-reference between the Terms of Reference and this submission.
Appendices B to F provide supporting information for the main chapters.

Five independent expert reports have also been attached which provide additional reasoning, evidence and expert opinion. These expert reports relate to land transport, car parking, the ACCC service quality monitoring and the competitiveness of Sydney Airport's intra-NSW charges.

In addition, Sydney Airport supports the Australian Airport Association (AAA) submission and the expert reports prepared for it.

LIST OF ABBREVIATIONS

AAA	Australian Airport Association
ACCC	Australian Competition and Consumer Commission
ACICG	Aeronautical Capital Investment Consultative Group
ACI ASQ	Airports Council International – Airport Service Quality
AGTP	Airport Ground Travel Plan
AOC	Airline Operators' Committee
AQIS	Australian Quarantine and Inspection Service
ASQ	Airport Service Quality
BARA	Bureau of Airline Representatives in Australia
CBD	Central Business District
COAG	Council of Australian Governments
COU	Conditions of Use agreement
CUTE	Common User Terminal Equipment
FAC	Federal Airports Corporation
FIDS	Flight information display screens
GFC	Global Financial Crisis
GPPCA	Ground Power and Pre-Conditioned Air
GSP	Gross State Product
IPART	Independent Pricing and Regulatory Tribunal
IFRS	International Financial Reporting Standards
LAGS	Liquid, Aerosols and Gels
LCC	low cost carrier
LTOP	Long Term Operating Plan
RESA	Runway End Safety Area
SACL	Sydney Airport Corporation Limited
SARS	Severe Acute Respiratory Syndrome
SLA	Service level agreement
SQIP	Service Quality Improvement Program
T1	Terminal 1 (International terminal)
T2	Terminal 2 (Common user domestic terminal)
T3	Terminal 3 (Qantas domestic terminal)
UK	United Kingdom
WACC	Weighted Average Cost of Capital

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Competitive and regulatory environment

The National Aviation Policy recognises the benefits to Australia of an open, competitive and innovative aviation market that benefits tourism, trade and consumers which connects all Australians to the world, our major cities and our regional communities.

Since 1990, the thrust of aviation policy has been to enhance productivity and services through the progressive deregulation of the entire industry. The process of deregulation has been a catalyst for – and taken place parallel with – enhanced commercial relationships between airports and airlines. The current healthy state of Australia's aviation industry – with more people flying than ever before – is due to the success of this policy framework.

Sydney Airport's key interests are strongly aligned with the National Aviation Policy:

- Traffic growth is the fundamental driver of airport value
- Efficiency, innovation and investment contribute to long term traffic growth and sustainable returns
- Strong, sustainable returns can only be achieved in collaboration with our stakeholders, – particularly the airlines – and meeting customer needs.

The aviation industry has changed dramatically over the past decade, including:

- Technology improvements in aircraft, air traffic control and airports
- The transformation of the aviation industry due to the development of low-cost airlines within Australia and the rapid growth of airlines from the Middle East and Asia
- Airline failures, consolidation, and proliferation of global alliances
- Air traffic disruptions that are occurring more frequently and having a greater impact with higher risk
- Structurally higher aviation fuel prices
- Introduction of new operational regulations and additional security requirements
- Concerns over climate change which are impacting on the behaviours of passengers, airlines, governments and airports
- Increased support of tourism and aviation by some state and local Governments, but with planning shortfalls more evident.

Many of these changes have increased the complexity of the business environment, including the choices available to airlines when making route decisions. Increasingly the airlines no longer serve primarily national catchments, but instead serve economic regions (for example, Europe or Asia) or global catchments. All airports globally are competing for the new aircraft which are being delivered to airlines – deliveries which are predominantly to Asian, Middle Eastern and LCC airlines. These developments have therefore dramatically increased the level of competition among airports for traffic in Australia as elsewhere.

The changes to the aviation industry also require much greater flexibility from airports. Whilst sudden changes in traffic volumes, new security requirements or operational regulations, and competition happen in the short term, airports are planning and investing for the very long term

(up to 100 years) in the knowledge that the aviation industry will continue to evolve and will be profoundly different from the industry today. It can be expected that the airports of the future will, through the use of technology, be very different to the airports of today, both in the experience offered and their operation and expansion. Ensuring that the long term vision is delivered through innovation and substantial incremental investment in the short term is a challenge best met through the collaboration of airports and airlines, and supported by strong commercial relationships.

Given that increased commercial uncertainties associated with large and long term investments have been more apparent over the last decade, it is therefore even more important that investment in airports is not also subject to regulatory uncertainty.

Sydney Airport operates under a range of economic and operational regulations that are numerous, complex and intrinsically connected. These regulations are more onerous than those applying to other Australian airports or to any of the other top 50 airports in the world. These regulations inhibit the economically efficient and timely operation and use of Sydney Airport. This materially fetters the airport's contribution to the economy. The 650 businesses associated with Sydney Airport already contribute some 6 percent to the New South Wales (NSW) economy and 2 percent to the nation's economy. Improvements to facilitate further growth promise further benefits to the economic welfare of Australians, through enhanced services, employment and government revenues.

Whilst the *Master Plan 2009* demonstrates that Sydney Airport is able to meet projected demand until at least 2029, it is in the national interest that the most efficient use is made of the Australia's most important infrastructure asset and international gateway. Sydney Airport recommends that the constraints in place at Sydney Airport be reviewed and updated to ensure that the Government's overall objectives are being met, balancing the interests of all stakeholders. This will attract new airlines and services for the benefit of the community. It will also ensure that Sydney Airport is able to meet demand well beyond 2029 – postponing the need for governments to spend substantial sums to construct additional capacity elsewhere.

Achievements under the light-handed regulatory regime

The light-handed regime at Sydney Airport has delivered benefits to the community consistent with the policy goals underlying the progressive deregulation of the aviation industry over the past two decades. Most importantly, the original policy expectation that benefits to consumers would flow from the efficient growth of airport services, while the interdependence of businesses would keep in check the exercise of potential market power, has been borne out over time, and indeed has been given commercial form through negotiated agreements supported by service standard targets. Thus there has been:

- Negotiation of multifaceted commercial agreements with all domestic and international passenger airlines
- Adaptation and renegotiation of commercial user agreements to reflect changes to the economic and aviation environment, including reprioritisation of capital investments
- Reductions in overall airline costs through airport investment in centralised services
- Over $1.8 billion (of which 70% is aeronautical) of investment since July 2002 to meet passenger and airlines needs, following extensive consultation with airlines on the timing and design

- Increased customer focus and the introduction of collaborative service level commitments, resulting in increased passenger perceptions of service quality, with international passenger service quality measures as high or higher than comparable international airports
- Underlying price stability, and returns on capital that are clearly not excessive.

These are the types of outcomes expected from the introduction of private sector innovation and discipline through the airport privatisation program.

Airport monitoring

Price and quality monitoring has been a key feature of the light-handed regime. Sydney Airport supports its continuation. However, it is important that this regime is updated and serves its policy purpose as well as possible. Monitoring needs to respond to changing competitive and commercial circumstances, as the costs and benefits of monitoring are not static. With the increasingly complex business environment, the costs of regulation and monitoring (especially poor monitoring) continue to rise, while any benefits are diluted.

The key principles of good monitoring should include:

- **Consumer-focussed:** the airlines and airports have commercial relationships to provide a joint product to passengers. Monitoring should be designed to support consumers, particularly the passengers, who have varying relationships with businesses and government agencies which are all part of performance assessment
- **Non-distortive**: it should not distort collaboration to improve performance
- **Focused:** monitoring should concentrate on areas in which the airport has potential market power, should provide useful information concisely, and exclude extraneous information
- **Robust:** methodologies for obtaining, analysing and reporting data should be objective, unbiased, transparent and statistically robust
- **Comparable**: benchmarking should be against comparable airports in comparable circumstances
- **Timely and cost-efficient**: the monitoring should be cost-efficient and the results published quickly.

The recent monitoring reports fail the contemporary policy purpose through the absence of useful, comparable and up to date information, and contain poorly founded data and unsupported and out of date commentary.

To have integrity and be useful the monitoring process must be consistent with the principles above and compliant with appropriate ISO standards. The current ACCC Monitoring Reports fail the basic test of 'natural justice'.

Landside access and car parking

Land transport access to Sydney Airport is inadequate:

- The train fare costs are prohibitively expensive for many users – (for example, it is cheaper to get to Bathurst than the airport from Sydney Central). In addition, the trains have inadequate luggage storage for passengers travelling to or from the airport
- There is only one public bus route to Sydney Airport (for 140,000 passengers, meeters and greeters, and staff each day)

— There is congestion on the surrounding roads, particularly during the peak hours when the roads are being used heavily by commuters, Port Botany and to access the airport.

This inadequacy is the result of a lack of investment in roads, buses and rail over the past decades by the NSW government, which is responsible for providing for consumers land transport infrastructure to Sydney Airport and Port Botany.

It is therefore critical that the NSW Government prepares the long overdue Sydney Airport/Port Access Plan in consultation with the community and other key stakeholders (including the airport and port operator).

It should also be recognised that Sydney Airport faces strong competition in the market for access to the airport and therefore does not have market power. For example:

— Sydney Airport faces strong competition from off-airport car parks and several other alternatives to car parking (drop-off, taxi, rail, bus and car rental), with consumer choice enhanced by transparent pricing and prices less than Sydney Central Business District equivalents.

— Sydney Airport has invested heavily in expanding its car parking and landside facilities. Service quality has strengthened materially over time and Sydney Airport has repeatedly advocated for better public transport (which would increase competition but better serve broader consumer and airport interests). None of these factors are consistent with the exercise of market power.

Recommendations

Sydney Airport believes that the Productivity Commission inquiry should support the broad benefits of improved and updated light-handed regulation of the aviation industry. This would continue to foster commercial relationships designed to service consumer needs and, through the resulting partnerships, the aviation services and connectivity required by a growing modern economy.

Specifically, Sydney Airport recommends improving and updating the current regulation and monitoring regime with:

— Focused reporting of key financial and service quality information

— A scheduled Productivity Commission review in 10 years to reduce regulatory uncertainty (corresponding with best regulation review practice)

— Publication of the international ACI (Airport Council International) ASQ (Airport Service Quality) survey results

— Publication of the scope of the service level agreements and whether the airports and airlines are meeting the commercially agreed targets

— Publication of the audited average return on capital earned by the airport since July 2002

— Self-publication of car park prices on the website

— A framework for governments to address road, rail and bus transport needs and planning links with the airport to improve competition and consumer welfare

— An estimate of the benefits to economic welfare (including equity) of efficient growth in airport services under the improved regime.

In addition, Sydney Airport recommends that the 'artificial constraints' in place at Sydney Airport be reviewed to ensure that the Government's overall growth and distribution objectives are being met to the full extent possible, balancing the interests of all stakeholders. This will both attract new airlines and services, for the benefit of the community, and will also ensure that Sydney Airport is able to meet demand well beyond 2029.

1. The importance of aviation and Sydney Airport

Key points

- Since 1990, the thrust of Australia's aviation policy has been to enhance productivity through the progressive de-regulation of the entire industry.
- The process of de-regulation has been a catalyst for – and taken place in parallel with – enhanced commercial relationships between airports and airlines.
- The current healthy state of Australia's aviation industry, with more people flying than ever before, is a clear indication of the success of this policy framework.
- Sydney Airport's interests are aligned with the National Aviation Policy. In particular, promoting traffic growth is the fundamental driver of airport value.
- Sydney Airport believes that this Productivity Commission inquiry should support the continued evolution of the industry with steadily less government intervention and regulation. Such an outcome will promote commercial relationships and the aviation services and connectivity that a growing modern economy requires.

The National Aviation Policy recognises the benefits to Australia of an open, competitive and innovative aviation market that benefits tourism, trade and consumers and which connects all Australians to the world, our major cities and our regional communities.

Aviation is an industry of national strategic importance to Australia. Perhaps more than any other country, Australia depends on air transport to link our people with each other and the rest of the world. More than this, aviation is a critical enabling industry for the broader economy. A safe, secure and efficient aviation industry underpins a range of business, trade and tourism activities that contribute significantly to our economic prosperity.[1]

Sydney Airport is arguably Australia's single most important piece of infrastructure – the gateway to the nation and to the global city of Sydney. It handles almost half of all flights to or between Australian airports, is the destination for more than half of all first time visitors to Australia, and is the largest transport hub in New South Wales. It is also a major contributor to employment and the national and state economies – directly and indirectly, Sydney Airport generates more than 200,000 jobs and is estimated to contribute in excess of $16.5 billion per annum to GDP[2] with the associated substantial revenue streams for all levels of government.

Sydney Airport's key interests are aligned with the National Aviation Policy:

— Traffic growth is the fundamental driver of airport value

— Efficiency, innovation and investment contribute to long term traffic growth and sustainable returns

— Strong, sustainable returns are best achieved in collaboration with our interdependent stakeholders, particularly the airlines – and Sydney Airport believes the level of collaboration within the industry is higher than it has ever been as a result of the increased focus on commercial agreements under the current light-handed monitoring regime.

[1] National Aviation Policy White Paper, page 2

[2] The Economic Impact of Growth at Sydney Airport – Report prepared by URS Australia Pty Ltd – 9 January 2008. Available http://www.sydneyairport.com.au/SYDNEY AIRPORT/Economic-Impacts-Report.html

- Australia already benefits from an aviation market that has promoted enhanced connectivity for the economy and society generally, supported by airports that have promoted competition and innovation. For example, in the last decade, the entry of Virgin Blue, Jetstar and Tiger Airways to Sydney Airport demonstrates both the openness of the market and the foresight of Sydney Airport to invest in the conversion of Terminal 2 (T2) to a common use terminal in 2002. The evolution of these airline business models, supported by the airport, has resulted in an array of new products, new technology, service innovation and competitive air fares.

The National Aviation Policy identifies a number of goals which will continue to promote more open, competitive and innovative aviation markets in the future. High amongst these goals is the need for continued investment in airport infrastructure and land transport links, whilst recognising that incentives to invest need to be balanced with fair pricing and transparency.

Balanced with the goal of promoting aviation supported by appropriate airport infrastructure, are broader community goals to continue to better manage noise, reduce aviation's contribution to global warming and ensure safe and secure air travel.

The continuation and further development of a commercial, competitive, innovative and collaborative aviation industry is a long term project. Over the last two decades the Australian aviation industry has been transformed. In 1990 the Australian Government owned all the airports, major airlines (Qantas and TAA), the air traffic control agencies, and regulators. As well as extensive government ownership, there was extensive and intrusive government regulation of routes, fares and other operational matters.

Since 1990, the thrust of policy has been to enhance productivity through the progressive de-regulation of the entire industry. Key steps in this process have been:

1990 Cessation of the two airlines policy
1993 Privatisation of Qantas and other government-owned airlines
1997-8 Privatisation of Australian airports (except in the Sydney region)
2002 Introduction of 'light-handed' regulatory regime (under probation)
2002 Privatisation of Sydney Airport
2003 Privatisation of other Sydney airports
2006 Continuation of 'light-handed' regulatory regime, with refinements.

The process of de-regulation has been a catalyst for – and taken place in parallel with – enhanced commercial relationships between airports and airlines. The current healthy state of Australia's aviation industry, with more people flying than ever before, is due to the success of this policy framework. Most importantly, the original policy expectation that benefits to consumers would flow from the efficient growth of airport services, while the interdependence of businesses would keep in check the exercise of potential market power, has been borne out over time and, indeed, has been given commercial form through negotiated agreements supported by service standard targets. Sydney Airport believes that this Productivity Commission inquiry should support the continued evolution of the industry with an improved and updated light handed regulatory regime. The continued evolution of light-handed regulation will continue to foster commercial relationships and, through the resulting partnerships, the aviation services and connectivity that a growing modern economy requires.

Sydney Airport vision is 'to be a world-class airport management company'. Consistent with the vision set-out in the approved *Sydney Airport Master Plan 2009* (Master Plan 2009), it is 'to create long-term value for Sydney Airport and its stakeholders' by presenting the best of Sydney and the state of NSW to the world, and to continue to be a major contributor as a sustainable business to growing employment and the national economy. Sydney Airport's core values include:

- **Safety and security** - maintain a safe, secure and reliable airport operating environment as the number one priority
- **Environmental sustainability** - operate the airport in an environmentally sustainable and responsible manner that addresses climate change and aircraft noise impacts
- **Community leadership** - be a sustainable business, which is a valued member of the community and a key economic driver for Sydney, NSW and Australia, regularly engaging with all key stakeholders to strike the right balance between the economic and employment benefits of the airport and the environmental impacts of the airport
- **Service quality** - provide quality experiences for the travelling public and airport visitors
- **Business and operational excellence** – plan and develop new and enhanced capacity to cater for forecast growth, including:
  - facilitating introduction of new aviation technologies and new larger, quieter, cleaner and more fuel efficient aircraft
  - operating the airport to maximise the efficient use of existing infrastructure
  - ensuring flexibility to meet changing user needs
  - exploring new business opportunities to enhance the Airport's value.

Over the past decade, Sydney Airport has undertaken extensive investment – particularly in capacity, differentiated services, and environmental improvements– and has introduced new services, increased choice, improved management and promoted traffic development. It is recognised that continuing to achieve and improve these outcomes will require a committed and sustained effort.

2. Evolution of the aviation and airport industry

Key points

- In both Australia and globally, the aviation industry has changed dramatically over the past decade
- Most noticeable has been significantly increased competition between airports and an increased need for flexibility because:
  - All airports globally are competing for the new generation aircraft which are being delivered to airlines – deliveries which are predominantly to Asian and Middle Eastern airlines and low cost carrier (LCC)
  - Airports are planning and investing for the very long term in the knowledge that the aviation industry will continue to evolve and will be profoundly different from the industry today
- Airports are responding to competition and change through commercial agreements. Sydney Airport has negotiated commercial agreements with all scheduled international and domestic airlines, including many individualised commercial agreements with various airlines. This has supported growth, new entry and flexibility.

As discussed in this chapter, the aviation industry has changed dramatically over the past decade. These changes were far more profound than in preceding decades and change is expected to continue into the future. Whilst many of the changes arise from trends experienced throughout the economy, others relate specifically to the aviation industry. The changes to the economy, the airlines and the airports have interacted with each other and made a significant difference to the economic and commercial environment of airports.

Most noticeable has been significantly increased destination competition between airports and an increased need for flexibility. Airports are responding to these demands with the development of stronger commercial relationships with their customers. These relationships are continuing to develop as both airports and airlines improve their understanding of each others' businesses, and of the opportunities for collaboration.

Without these commercial relationships, it would be more difficult to invest in the uncertain and competitive environment.

2.1 Economy-wide trends

Technology: the passenger and community experience of aviation has generally been improved by new technology in all areas of the industry and the effects of technology improvements will be even stronger in the future. Aircraft technology is improving route economics and making possible direct routes that were previously not viable – for an airport such as Sydney this provides opportunities for new routes but also threats of lost transfer traffic as other Australian airports attract direct services. The new generation aircraft also offer enhanced passenger experience in the air such as higher ceilings, quieter cabins and individual entertainment systems. Improved air traffic control, new fuels, larger aircraft with better engines and quieter airframes benefit the community with fewer emissions per passenger and lower noise. In addition, the development of the internet and airport self-service technology has simplified, streamlined and personalised the passenger experience.

Airports around the world are today focused on improving the future passenger experience through the innovative use of emerging technology. The goal is to substantially reduce queues – and eliminate them where possible. The technologies required are still embryonic, but the potential is demonstrated by the self-service check-in and bag-drop being employed by Qantas on domestic flights for its frequent flyers. It is with this goal in mind, and in the context of still developing/evolving future technologies, that airports today are planning for the long term future in collaboration with the airlines.

Aviation fuel prices: while the long term price of oil is unclear, it is certain that it will be significantly higher than the prices which prevailed over most of the last quarter century. While the impact on traffic of the 2008 oil price shock has passed, the structurally higher oil price is reflected in increases in air fares and decreases in air traffic volumes. As a result of the structurally higher oil price (combined with airlines' efficiencies in other areas), fuel now accounts for a much higher proportion of total airline costs – 24% of Qantas Airways' costs are now fuel related[3]. This situation means that air traffic volumes more vulnerable to increases in the oil price, increasing risk throughout the aviation supply chain.

Climate change: concerns about climate change are influencing the behaviours of passengers, airlines, governments and airports – and these structural changes are just beginning. Airlines and airports are taking measures to reduce carbon emissions, both through reduced energy consumption and the development and use of alternative energy sources.

2.2 Economy-wide events

Traffic disruptions: traffic disruptions have been a regular event over the past decade, with a frequency and impact greater than in previous decades. In fact, in the second half of the 20th century, the only material disruptions to traffic volumes on a global scale were the oil crises in the 1970s – with the domestic pilots' strike disrupting Australian domestic traffic in 1989. In the first decade of the 21st century, traffic has been disrupted to varying degrees by terrorism (the September 11 attacks in the USA, Bali and London bombings), significant airline failures (Ansett), war (Iraq), fear of pandemics (Severe acute respiratory syndrome (SARS), Avian flu or Swine flu), the ash plume caused over Europe by the eruption of the Eyjafjallajokull volcano in Iceland, severe and prolonged weather events (snow, hurricanes and floods), an oil price shock, and the global financial crisis (GFC).

There are two striking features of this list - human-caused disruptions are occurring more frequently and all events, both man-made and natural, are having a greater impact. Whilst the causes of the increased frequency of events are most likely complex, the increased impact is, to a large extent, a result of the increased global interconnectivity of air travel and the increased speed of information flow. More complex and interdependent systems, while offering enhanced services and efficiencies, mean that disruptions are more difficult to manage.

Increased regulation: Both Commonwealth and State Governments have tried to reduce regulations across the economy, with the exception of the aviation industry for which regulatory burdens have increased particularly in additional security and operational regulations (see Section 3.3).

[3] Qantas Airways Limited, Final Report, Financial Year ended 30 June 2010, page 3

2.3 Airline-specific changes

Low-cost airlines: the development and transformation of LCCs over the past decade has changed the whole industry. A decade ago it would have been reasonable to describe almost all LCCs as niche airlines, offering cheap fares to leisure passengers on leisure routes and a basic level of service – no transfer of baggage between flights, no airline lounges, no medium or long-haul flights, no premium class, no interline agreements, no frequent flyer schemes and no alliances.

Today there is no agreed definition of LCCs. Ryanair and Southwest Airlines are the largest airlines in Europe and USA respectively, but otherwise are little different to the original LCC model – although the length of Ryanair's flights is gradually increasing and Southwest Airlines facilitates transfer passengers and has a frequent flyer scheme. In Australia, Tiger Airways and Jetstar follow a similar model. On the other hand, airlines such as Virgin Blue, Norwegian Air Shuttle, Air Berlin and AirAsia X have moved well away from the original model – some of them now offer many of the 'frills' that once distinguished network carriers from LCCs.

Middle-East and Asian airlines: in 2010, Emirates was the world's third largest airline (as measured by revenue passenger-kilometres) and was the fourth largest international carrier at Sydney Airport. Emirates is an exemplar for the rapid growth of airlines from the Middle East and Asia. This growth appears likely to result in these airlines significantly dominating large parts of long haul travel in the future, reflecting advantages of geography, government support, population and lower labour costs.

Airline consolidation: the long-overdue consolidation of the airline industry has gathered some pace over the past decade, through a combination of airline collapses, rapid growth of the strongest airlines, airline mergers, closer airline co-operation and larger alliances. In addition to increasing the bargaining power of the airlines, airline consolidation also changes the operational requirements of the airport. For example, newly-aligned airlines will want to co-ordinate their flights to facilitate transfer passengers, which may result in changed passenger peaks through the terminals. They will also want to share airport facilities and services such as airline lounges, and will want the reallocation of gates and check-in to move closer together. In addition, for airports, commercial agreements need to be renegotiated with new parties, often with enhanced countervailing power.

2.4 Airport-specific changes

Security: additional security requirements have been introduced on several occasions due to perceived risks in Australia following terrorist attacks overseas. The additional requirements increase queues and time for passengers, add to direct security costs for airports (and therefore indirectly for passengers), and potentially reduce the effective capacity of the terminal infrastructure. New measures have always been additional to existing measures, without reviews to identify redundancy, and as Qantas argues:

…there are a number of regulations that have no security outcome or with which compliance is impractical, but nonetheless place an obligation on us[4].

[4] Productivity Commission, "Annual review of regulatory burdens", 2009, Chapter 6, page 260

Landside access: road congestion getting to and from Sydney Airport has substantially increased over the past decade, due to a lack of investment in roads, buses and rail by the NSW government outside the airport's boundaries. In addition to directly impacting the passenger experience, congestion on the surrounding roads can cause congestion within the airport boundaries, as well as continued growth of medium and high density residential areas around airports. The impact of off-airport road traffic congestion is to reduce the efficient movement of passengers and freight and to undermine the productivity contribution made by the aviation industry.

Operational regulations: as with security measures, additional operational regulations have been imposed over time to respond to specific issues – without consideration as to how they interact with existing regulations. For example, under the Liquid, Aerosols and Gels (LAGS) requirements, passengers carrying duty free arriving from overseas in Sydney could continue on to Melbourne on domestic flights whereas if the same passenger were to transfer to an international flight from Sydney to Melbourne the duty free LAGS would be confiscated. The accumulation of these regulations inevitably increases the operational complexity of the airport, often to the cost and inconvenience of passengers and airlines. Whilst new technologies ought to enable the simplification of airport operations, applicable regulations have never been critically reviewed to optimise outcomes.

Government support of aviation: over the past decade, some state governments have been increasingly active in attracting new tourism to their state by providing airlines with commercial incentives to fly to their state's airports. It is widely acknowledged in the air transport industry that Queensland and Victoria have affected competitive outcomes.

2.5 Competition between airports

The development of what might be described as low-cost network carriers, the emergence of the global network carriers in the Middle East and Asia, and the consolidation and diversification of the traditional network airlines have taken place concurrently. All these changes have increased the choices available to airlines when making route decisions and to passengers when making travel plans. Increasingly, airlines no longer serve primarily national catchments, but instead serve regional or global catchments. Examples of these changes are:

- The Middle Eastern carriers are able to fly directly to any airport in the world with the appropriate infrastructure. Emirates, for example, flies directly to every continent (except Antarctica) and to almost 100 destinations.
- The Asian carriers benefit from being within the most highly populated and fastest growing region of the world, with the potential to also reach any airport in the world directly with the appropriate aircraft with little or no regard for national boundaries.
- The LCCs optimise their route networks across multiple bases within geographic regions defined by the aircraft range rather than national borders. In Europe, for example, the larger LCCs such as Ryanair serve any viable city-pairing within Europe and North Africa. LCCs also run competitive processes to decide how to deploy their aircraft and where to establish bases, playing off offers from national and other levels of government.
- The consolidation of airlines has increased the choice for the focus of growth and deployment of aircraft between more bases. The same choice has also been achieved by other airlines which have diversified their product offerings (for example, offering both full service and LCC products) and geographic location.

The route decisions of these airlines are affected by passenger demand, airport charges and incentives, bilateral air rights and government support.

These developments have dramatically increased the level of competition between airports for traffic, in Australia as elsewhere. For example, in 2009 Qatar Airways chose to operate its inaugural Australian service from Melbourne rather than Sydney and, similarly, in 2010 Air India announced its intention to operate from Melbourne. AirAsia X is prevented from flying to Sydney due to the Malaysian Government not allocating it the necessary route rights – at Melbourne Airport, AirAsia X's operations have grown to 14 flights per week since commencing in November 2008.

In previous Productivity Commission submissions various parties claimed that competition between airports for traffic had no appreciable impact on overall behaviour of airports because:

- It is only at the margins, as airport costs represent a small proportion of airline operating costs
- It only affects the timing of airline decision
- Large sunk costs by the airlines when establishing operations at new airports enable the airport to extract monopoly rents at the expiry of the initial deal.

These claims were always oversimplified and overlooked the fact that business competition typically occurs at the margin and are now even less applicable.

Airports compete for larger aircraft, for increased frequencies, for new routes, and for selection as a base. The 'margin' is therefore best thought of as being most traffic growth. Whilst a single year's growth is, in fact, only a small proportion of total passenger traffic, several years' growth represents a significant proportion of total traffic. For example, a 2% pa increase in traffic growth over a decade represents a 22% increase in total traffic at the end of the period.

Moreover, given the high fixed costs (capital, operating and financing) of an airport a relatively minor change in passenger volumes can represent a much more significant change in returns to shareholders. Whilst competition is at all levels, it is significant to note that, since 2002, airlines new to Sydney Airport were responsible for 70% of the increase in international passengers and 17% of total international passengers in 2010.

Whilst some competition for airline seats may only affect timing, this is rarely clear to the airport and is subject to later events. Airline decisions frequently have longer term effects. For example, despite Sydney being a substantially larger city than Brisbane, Virgin Blue's Brisbane network was larger than its Sydney network for several years following its decision to be based in Brisbane – a decision which was supported financially by the Queensland Government. Similarly, four years after commencing at Melbourne Airport, Tiger Airways is yet to base aircraft at Sydney Airport.

The argument that airlines' sunk costs leave them open to monopoly rents needs to be seen in the context of LCCs and non-based airlines which routinely withdraw capacity and redeploy it elsewhere. In Europe, it is almost routine for LCCs to pull out completely of airports which are not successful and, conversely, Ryanair has cut capacity at some successful airports in Ireland, Germany and the UK to put pressure on government travel taxes, reallocating aircraft

to other airports. In Australia, Tiger has similarly reduced its operation in Adelaide Airport and has refocused its growth from Melbourne Airport to Avalon Airport. Similarly, there are a number of airlines which have flown to Sydney Airport in the past decade which have subsequently stopped and redeployed services to other markets – for example, Sydney lost a daily service when Emirates decided to redeploy the Sydney aircraft onto a Dubai-Houston route.

An argument might be put that Qantas in particular has no option but to remain in Sydney, Melbourne and other Australian airports. This is true – at least in terms of the existing traffic. However, the Qantas Group now includes Jetstar and Jetstar Asia and can therefore choose to deploy its new aircraft in a region much larger than Australia. In fact, the fastest growth in the Qantas Group is within the Asian region[5]. Likewise, Tiger Airways, with its principal operational base in Singapore, can deploy its aircraft from a wide range of Asian or Australian airports.

The above examples illustrate the true nature of competition between airports. All airports globally are competing for the new generation aircraft which are being delivered to airlines – deliveries which are predominantly to Asian, Middle Eastern and LCC airlines.

In contrast to an airline's largest fixed assets - aircraft, which are the most mobile of assets - airport infrastructure is completely immobile. The increased flexibility of airlines, alongside lower sunk costs, has been the result of the new airline business models as well as the development of new technologies (for example, internet check-in, which substantially reduces staff-related sunk costs) and the provision of common-use domestic terminals.

2.6 Increased need for flexibility

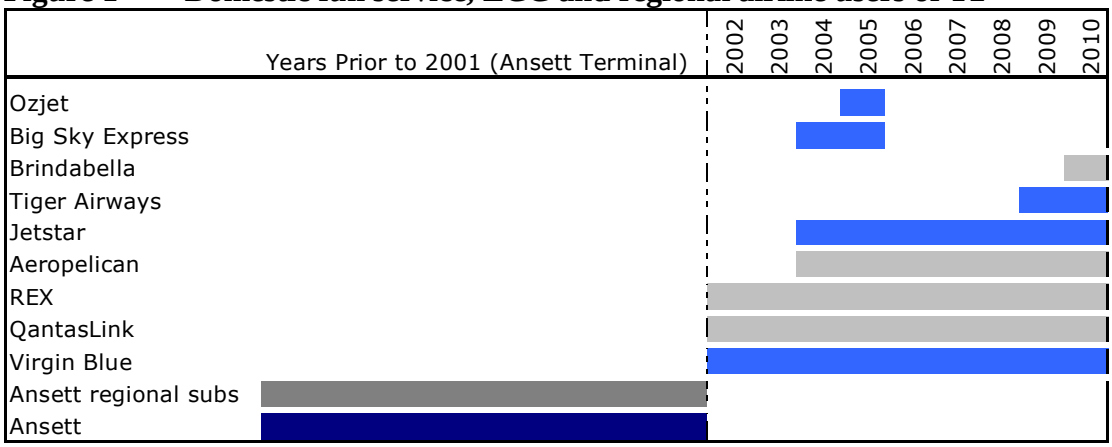
The continual changes in the aviation industry require much greater flexibility and constant adaptation from airports and other service providers. Whilst sudden changes in traffic volumes, new security requirements or operational regulations, and competition happen in the short term, airports are planning and investing for the very long term in the knowledge that the aviation industry will continue to evolve and will be profoundly different from the industry today.

Over the past decade, the operation of T2[6] at Sydney Airport illustrates the need for a commercial and pragmatic approach. Prior to 2001, this terminal had been used only by one full service network carrier (Ansett) and its regional airline subsidiaries – serving up to 6.5 million passengers and providing an extensive lounge complex. Subsequently, T2 has been adapted for use by many LCCs and regional airlines (see Figure 1)– with more than double the passengers and less need for lounges. During this period, the prioritisation and urgency of investments has been influenced by changes in traffic growth, the entries of Jetstar and Tiger, and the GFC. In response and in consultation with the airlines, Sydney Airport has continually refined the investment program and adjusted the charges for use of this terminal as appropriate. Virgin Blue's new strategy of deploying larger aircraft (for example, A330s on domestic routes) is changing terminal requirements once again – requirements that will be met through investment designed to be flexible for potential future uses.

[5] Qantas Airways, Financial results presentation half year ending 31 December 2010, slide 68

[6] T2 (Terminal 2), owned and operated by Sydney Airport, is the common user terminal now used by airlines including Jetstar, Virgin, Rex and other domestic and regional airlines.

Figure 1 Domestic full service, LCC and regional airline users of T2



Source: Sydney Airport analysis

It can expected that the airports of the future will, through the use of technology, be very different to the airports of today, both in the experience offered and their operation and expansion. Ensuring that the long term vision is delivered through innovation and incremental investment in the short term is a challenge best met through the collaborative partnership of airports and airlines, supported by strong commercial relationships.

2.7 Responding to competition and uncertainty through commercial relationships

Over the past decade, and particularly in the five years since the expiry in 2006 of the previous Australian Competition and Consumer Commission (ACCC) approved prices, Sydney Airport has been pursuing additional commercial relationships with the airlines. This process has included increased consultation on the design and pricing of investments, the progressive development of service level agreements, and increased focus on attracting additional growth.

However, the single largest development has been the negotiation of pricing and commercial agreements with all scheduled international and domestic airlines. Sydney Airport has in place a number of separate commercial agreements with various international airlines in addition to the standard agreement taken up by other international airlines and has agreements with all scheduled domestic airlines. These agreements differ according to the needs of the airlines and the facilities and services used. The agreements also include a variety of methods for charging – many designed to encourage more efficient use of the relevant infrastructure. The majority of these agreements are for five years, although some are of 17 years duration. They all include dispute resolution clauses negotiated with the airlines. However, to date, there have been no disputes that have required the use of this process.

Sydney Airport believes that the progress made towards individualised agreements over the past five years has been significant, and was only made possible by the current 'light-handed' regime which created space for greater commercial (as opposed to regulatory) interaction. It is the airport's expectation that these agreements will become even more sophisticated over time and promote a level of competition, efficiency and flexibility that would not otherwise be possible in a more regulated environment.

2.8 Investing in the face of uncertainty and competition

Critical to meeting the aviation needs of the Sydney region and the community will be both the efficient operation of Sydney Airport and the confidence of the airport to undertake investments in assets with a useful life of up to 100 years, such as a taxiway or road bridge. Both of these objectives benefit from a regulatory regime that facilitates the collaboration of airports, airlines and other stakeholders. Both objectives could be stifled by regulation that prescribes specific behaviours, however well intentioned.

Given the increased commercial uncertainties associated with large and long term investments, particularly over the last decade, it is even more important that investment is not also subject to regulatory uncertainty.

Investment decisions are made by assessing the expected return over the life of the investment, taking into account all of the opportunities and risks relevant to that investment. It is therefore particularly important to consider the reasonableness of returns over periods of time consistent with the life of the investments so that airports are able to earn a reasonable return over the long term. This would include periods of both above-average and below-average returns. Whether an investment decision is 'good' or 'bad' cannot be assessed simply by looking at the returns after the event, but only at the reasonableness of the assumptions and acceptance of risk made at the time of the decision. Confidence to invest is therefore reliant on stability in the regulatory regime and the reasonableness of judgements made. The greater the extent to which the airports are left to manage the commercial risks of their investments, over appropriately lengthy periods of time, the greater the likelihood of the right investments being made at the right time.

Achieving the Government's goal for an open, competitive and innovative aviation market, over a period of change, will be best supported by continuing the process of de-regulation to promote collaboration between airports and airlines and by the flexible adaptation of operational regulations to reflect the aviation market and technology of the day.

2.9 Conclusions and recommendations

Sydney Airport Recommends that:

To achieve the Government's goal for an open, competitive and innovative aviation market over a period of change will be best supported by the continuing the process of modern light-handed regulation to promote collaboration between airports and airlines and the flexible and responsive adaptation of operational regulations to reflect the aviation market and technology of the day.

3. Regulatory and operating environment

Key points

- Airports and airlines facilitate Australia's integration into the global economy, while providing direct benefits to passengers and wider economic benefits to the community through aviation's positive impact on productivity and economic development.
- It is estimated that in 2007 economic activity derived from Sydney Airport contributed around $16.5 billion to NSW Gross State Product (GSP) or 6% of the NSW economy and approximately 2% of the Australian economy.
- There is evidence that the use of Sydney Airport's runways is more heavily regulated than at any of the other top 50 airports in the world.
- Whilst the Master Plan demonstrates that Sydney Airport is able to meet demand until at least 2029, it is in the interests of Australia that the most efficient use is made of the nation's most important international gateway. This will benefit the community in both the short and long term and ensure:
  - More efficient use of Sydney Airport to attract new airlines, new routes and new services
  - Sydney Airport is able to meet demand well beyond 2029, avoiding or substantially deferring the need for enormous investment in a potential new airport.
- The aviation industry has changed profoundly since the operational regulations were introduced. For example, new technology has resulted in reductions in aircraft noise despite increased passenger volumes and use of larger aircraft.
- Sydney Airport recommends that the artificial constraints in place at Sydney Airport be reviewed to ensure that the Government's overall objectives are met, balancing the interests of all stakeholders and reflect the recent and continuing changes to the aviation industry.

3.1 Benefits of aviation

Airports are essential to the transport and communication networks upon which successful modern economies rely. Airports and airlines facilitate the nation's integration into the global economy, whilst providing direct benefits to passengers and wider economic benefits to the community through aviation's positive impact on productivity and economic development.

Sydney Airport is the gateway to Australia, handling almost half of all flights to or between Australian airports. Sydney is served by more airlines, operating to more destinations and with higher frequency than any other Australian airport. The expansive route network and its location positions Sydney Airport as the primary aviation hub in the Southwest Pacific region.

Sydney is the iconic Australian tourist destination. Almost half (45%) of all international visitors and 51% of first time visitors arrive at Sydney Airport[7]. The airport also handles half of all international freight. The airport underpins vitally important tourism, events and

[7] Tourism Australia, TRA International visitor Survey for 2009/2010 financial year.

conference industries and creates jobs and economic growth for Sydney and NSW. International air services are also an essential factor in the development of high value service industries such as education, finance, legal services and commerce as they provide timely and efficient access to new customers, markets and opportunities.

Sydney Airport is one of NSW's major job generators and an engine room of economic activity, contributing billions of dollars annually to Sydney households and the NSW economy. A report by URS Australia[8] estimated Sydney Airport's contribution to direct employment (full time and part time) to be 75,580 jobs in 2007, plus indirect employment of 130,550, together representing about 6% of the Sydney labour force. This represented 120,162 full time job equivalents.

The URS report estimated that economic activity derived from the airport contributed around $16.5 billion to NSW Gross State Product (GSP) or 6% of the NSW economy and approximately 2% of the Australian economy. In simplest terms, a typical A380 arrival (with and average of 400 passengers) will contribute an estimated $1 million to the economy[9]. The GSP contribution of Sydney Airport is forecast to grow to $27.2 billion by 2015/16 (in 2007 dollars).

Around 650 businesses and other organisations operate in and around Sydney Airport, relying on the airport to generate jobs and incomes. The interdependent activities are varied and include airlines, aircraft maintenance, air traffic control, cargo terminals, car rental and parking, ground transport such as rail, taxis and buses, freight forwarders, fuel services, ground handlers, hotels, in-flight catering, cleaning, maintenance, security, retail operators, and government functions such as customs, immigration, quarantine and policing.

In addition, there are many international businesses that establish themselves or their regional offices in proximity to an international airport with strong connections. For example, Sydney is the head office location of 80% of domestic and foreign banks in Australia and 60% of all finance and insurance businesses in the top 500 companies in Australia are based in New South Wales. Multinational corporations with a major presence in NSW span all industries and include IBM, Coca-Cola Amatil, ING, Nestle, Allianz, Vodafone, Nokia, SingTel, Pfizer, Sony and Norske Skog[10].

3.2 Government support of aviation

Capital city airports are major economic drivers and contributors to their state economies. As previously indicated, in Sydney's case, the airport is responsible for 6% of the NSW economy and it provides or generates 206,000 jobs. Sydney Airport also plays a crucial role in supporting NSW's tourism industry. In other states – such as Queensland, Victoria and Western Australia – state governments have clearly recognised the important economic role that airports play and support them accordingly. However, successive governments in NSW have been slow to do so and have also failed to properly integrate the future requirements of Sydney Airport with the various metropolitan planning, development and transport strategies.

[8] The Economic Impact of Growth at Sydney Airport – Report prepared by URS Australia Pty Ltd – 9 January 2008.

[9] Australian Bureau of Statistics (ABS), Average international visitor consumption – Page 20 table 8: http://www.ausstats.abs.gov.au/Ausstats/subscriber.nsf/0/99AE2E9D9B5EB2C3CA2577F9000F2CC0/$File/52490_2009-10.pdf

[10] NSW Governement Trade and Investment - Location of Top 500 Companies in Australia by Revenue, 2010 - http://www.business.nsw.gov.au/invest-in-nsw/about-nsw/trade-and-investment

This is illustrated by the ongoing failure of the NSW Government to provide adequate land transport infrastructure and services to access Sydney Airport, despite passenger numbers continuing to grow. With some exceptions in more recent times, successive governments have also been slow to support new tourism activity through working with Sydney Airport in providing airlines with commercial incentives to fly to Sydney. As a consequence, Sydney and New South Wales have lost significant business opportunities, such as Air India and Qatar Airways, to those states which have publicly and financially supported their capital city airports.

3.3 Current economic and operational regulations

The broader community would also benefit from an update of the operational regulations governing Sydney Airport to reflect developments in technology and aviation.

Sydney Airport operates under a range of economic and operational regulations that are numerous, complex and intrinsically connected. These regulations are more onerous than those applying to other Australian airports or to large international airports (see Appendix D). These regulations restrict the economically efficient and timely operation and use of Sydney Airport, and reduce the airports contribution to the economy.

Sydney Airport is subject to both international aviation regulations and standards and to general legislation and regulations applying to all businesses in NSW. In addition, it is subject to many separate pieces of Commonwealth legislation or regulation specific to Sydney Airport, Australian airports or aviation, including:

Legislation and regulations specific to Sydney Airport
Sydney Airport Curfew Act 1995
Sydney Airport Curfew Regulations 1995
Sydney Airport Demand Management Act 1997
Sydney Airport Demand Management Regulations 1998

Legislation and regulations applying to all major Australian airports
Airports Act 1996
Airports Regulations 1997
Airports (Building Control) Regulations 1996
Airports (Control of On-Airport Activities) Regulations 1997
Airports (Environment Protection) Regulations 1997
Airports (Ownership Interests in Shares) Regulations 1996
Airports (Protection of Airspace) Regulations 1996
Aviation Transport Security Act (ATSA) 2004
Aviation Transport Security Regulations (ATSR) 2005
Environment Protection and Biodiversity Conservation Act 1999
Civil Aviation Act 1988
Civil Aviation Regulations 1988
Civil Aviation Safety Regulations 1998
Civil Aviation Safety Regulations - Manual of Standards – Part 139

Whilst the *Master Plan 2009* demonstrates that Sydney Airport is able to meet demand until at least 2029, it is in the interests of Australia that the most efficient use is made of the

nation's most important international gateway. This will benefit the community in both the short and long term and ensure:

More efficient use of the airport to attract new airlines, new routes and new services
Sydney Airport is able to meet demand well beyond 2029, avoiding or substantially deferring the need for enormous investment in a potential new airport.

There is evidence that the use of Sydney Airport's runways is more heavily regulated than at any of the other top 50 airports in the world[11]. These restrictions reduce the airport's economic contribution and benefits for the local community and broader economy. Whilst Paris Orly has a similar number of airport-specific regulations and constraints on the use of its runways, the city of Paris is served by several unconstrained and non-curfew airports including the largest airport in Paris, Paris CDG.

Regulations impact most heavily on the use of 'peak' capacity at Sydney Airport. This is precisely the capacity which is most scarce and therefore of greatest economic value to airlines, Sydney residents, passengers and businesses. Regulations also, in some circumstances, unnecessarily dilute pricing signals, thus impacting on the better use of runway capacity through the operation of larger aircraft.

Good regulation minimises any undesirable side-effects whilst maximising the benefits to the wider community. The operational regulatory objectives should permit the allocation of scarce resources to their highest use, while promoting aviation for all Australians, including providing essential services to regional communities, and mitigating noise and emissions for a given level of travel. Good regulation will therefore adapt over time to reflect and accommodate improvements in technology and changes to the aviation industry in order to continue to maximise the benefits to the wider community and minimise any undesirable side-effects.

The next three sections briefly consider the application of airport regulations specific to Sydney Airport and the practical constraint they have on the efficient operation of the airport.

3.4 Management of night-time aircraft noise

Description of the regulations

The *Sydney Airport Curfew Act 1995* (the Curfew Act) establishes the curfew between the hours of 2300 and 0600 with limited exceptions. This curfew restricts use of the airport for the majority of jet aircraft movements overnight.

Due to a legislative anomaly the *Sydney Airport Curfew Regulations 1995* prescribe eleven fewer take-offs and landings per week during the 'shoulder' curfew than those permitted by the provisions of the Curfew Act. Under the Curfew Act, these landings would take place with the approach over Botany Bay between 0500 and 0600. It is also noted that the Curfew Act allows for an evening shoulder period between 2300 and 0000 for international passenger aircraft, while the accompanying regulations remove this allowance.

Impact of the regulations

[11] L.E.K. Consulting Pty Ltd report for Sydney Airport Corporation, 28 June 2008: Artificial Constraints at the Top 50 Airports. A summary table is included in Appendix D

The curfew both limits the growth of long-haul and domestic LCC services and concentrates international passenger services in the early morning and late afternoon peaks. These limitations are reflected in the operation of Sydney Airport in the following ways:

- The growth potential of long-haul services is particularly constrained because of the interaction with other overseas curfews, the length of the flight sector to Sydney and traveller preferences for flight times.
    - Several airlines have indicated they would either begin new services or increase capacity to Sydney if they were able to fly at times restricted by the current curfew. To put this into perspective, if Sydney Airport was able to attract an extra 11 A380 arrivals per week, the economic benefit to NSW would be around $500m per annum – for little or no additional investment in infrastructure.
- The number of aircraft turnarounds feasible for domestic LCCs is reduced by the curfew, reducing Sydney's attractiveness relative to other Australian airports
- The concentrated international peaks coincide with the domestic and regional peaks and increase the demand for aircraft parking positions and terminal facilities.
- The restrictions on aircraft departures by even a few minutes past 2300 (often due to legitimate but otherwise unforseen reasons) means that airlines routinely cancel flights and passengers are forced to stay overnight, resulting in significant passenger inconvenience, financial penalties and operational disruption on airlines.

Developments over the past decade

The Productivity Commission 2009 review of regulatory burdens[12] suggested that performance-based regulation, based on a permissible level of noise for all aircraft using the airport between certain hours could provide a more effective means of protecting the amenity of surrounding airport communities than the current prescriptive arrangements. This would ensure that a specified noise level was met during the late evening / early morning hours, provide an incentive for the operation of lower noise aircraft and remove the anomalies in the current arrangements.

Aligning the Sydney Airport curfew regulations with the relevant provisions of the Curfew Act would allow additional international aircraft to land with approaches over Botany Bay between 0500 and 0600.

The Board of Airline Representatives of Australia Inc (BARA)[13] has also suggested amendments to the curfew regulations that would provide greater operational flexibility and efficiency for the international airlines that use Sydney Airport, better allowing for weather conditions en-route.

As shown in Appendix D, Sydney Airport is one of only three airports in the world's largest 50 airports that have a 'hard curfew'. The curfews applying to most airports are 'soft curfews' that allow passenger movements under certain circumstances – most commonly for delays or for quiet aircraft.

3.5 Management of day-time aircraft noise

[12] Productivity Commission, Annual Review of Regulatory Burdens on Business: Social and Economic Infrastructure Services, Chapter 6, page 272, 15 September 2009

[13] Board of Airline Representatives of Australia (BARA), "Airline Views" newsletter October 2010

Description of the regulations

The *Sydney Airport Demand Management Act 1997* established the maximum limit as 80 scheduled aircraft movements per hour.

The Long-Term Operating Plan (LTOP) for Sydney Airport, implemented by Airservices Australia, varies the use of runways and airspace for arrivals and departures to share the noise over many residents, using a range of different combinations of flight paths ('modes'). An Implementation and Monitoring Committee, which includes community representation, reports directly to the Federal Minister for Transport on how the LTOP is being implemented.

Impact of the regulations

The arbitrary limit of 80 aircraft movements in an hour is below the demonstrated capabilities of Sydney Airport and artificially limits the effective capacity of the airport. As a consequence:

- The theoretical long term capacity of the airport is limited
- Strategic slot hoarding by airlines in the morning and evening peaks results/occurs
- Capacity constraints increase in morning and evening peaks, when the majority of international and domestic services wish to arrive at and depart from Sydney Airport.

A recent increase in focus by the Federal Minister of Transport on the actual movements per hour, rather than the scheduled movements per hour, also has the potential to reduce the efficient use of the airport and to increase actual noise impacts on the community. If actual aircraft movements are managed to minimise the number of hours in which actual movements exceed 80, then there is the likelihood that the 81st aircraft will be required to defer its arrival or departure into the following hour. This will necessarily result in increased fuel burn and higher aircraft noise (for delayed arrivals) or increased congestion on the taxiways and aprons (for delayed departures) with no offsetting benefit except a reduction in the number of reported hours above 80 movements. With current aircraft and navigational technologies, movement capacity above 80 is eminently possible and at a rate of say 85 movements an hour, a flight would arrive or depart every 42.4 seconds as opposed to one every 45 second for 80 movements, noting that flights would arrive and depart on different flight tracks.

The operation of the LTOP does not constrain demand since it has effect during the off-peak hours as well. However, during changeovers between the modes of operation, the runways are not in use, resulting into delays for passengers and airlines and consumption of fuel for aircraft 'held' in the air, which has both cost and environmental implications.

Developments over the past decade

As with the curfew arrangements, these regulations were introduced more than 15 years ago when aircraft were noisier than the current generation of aircraft. As evidenced by the Airbus A380 (with an average passenger load of 400), which is quieter than the smaller Boeing 747 (with an average passenger load of 280), aircraft technology is continually reducing aircraft noise. In fact, despite aircraft movements forecast to nearly triple over a 53 year period from 1976 to 2029, Sydney Airport's noise footprint is expected to shrink[14]. In many areas, the

[14] Sydney Airport Master Plan 2009, figures 14.7b and 14.8

reduction is significant. Other technologies including air traffic control improvements – not yet used at Sydney Airport – are capable of further reducing noise impacts. It is expected that improved technology will continue to reduce future noise impacts.

During the 2006 Productivity Commission inquiry[15], Geoff Breust of Regional Express (Rex) advocated the exclusion of curfew-exempt turbo-prop aircraft from the movements cap. This proposal would ensure continued access for regional services in peaks without impacting on larger more efficient aircraft, and recognises that propeller aircraft are quieter than jets and do not create the same noise concerns that the movement cap is intended to address. It would also allow more efficient use of the airport infrastructure.

3.6 Promoting intra-NSW access and domestic competition

Description of the regulations

The 2001 Amendments to the *Sydney Airport Demand Management Regulations* 1998 established Permanent Regional slots. The absolute number of 'Regional Ring Fence' slots was capped in the peak hour at those in the Northern Winter 2001 scheduling season levels – being 26% of peak morning slots and 28% of the peak evening slots. While some modifications have been made to this arrangement to require minimum aircraft sizes for new services, these slots are 'ring-fenced' and cannot be reallocated to larger, non-regional aircraft or international services.

Sydney Airport remains formally price regulated under Declaration 92 and Part VIIA of the *Competition and Consumer Act 2010*[16] for aeronautical services provided to regional users. Under Direction 32, the ACCC is encouraged to limit the approval of increases in charges for regional services to annual inflation. The opportunity costs of this restriction are rising every year.

In 2003, the responsible Minister under the powers of the *Sydney Airport Demand Management Act 1997* suspended the reallocation of the former Ansett slots, creating a pool of protected slots ('Ansett protected slots'). These slots can only be allocated to new entrants, although they can be used on an ad hoc basis pending their allocation to new entrants.

Impact of the regulations

In combination with the 80 movements cap, the 'Ansett protected' and regional regulations have the following effects:

- The peak slots are less efficiently used than their scarcity would suggest they should be, with corresponding economic loss to the state
- Failure to ensure the continued access of many regional communities to Sydney Airport (since airlines are free to use the 'regional' slots for any intra-NSW destination)
- Investment in facilities for regional airlines at Sydney Airport is discouraged since there is no basis for remuneration of the investment
- The growth of airlines at Sydney Airport is reduced due to the ring-fencing of slots
- Any incentive for regional airlines to use larger aircraft is removed.

[15] Price Regulation of Airport Services, Public Hearing Transcripts, Melbourne, 24 October 2006
[16] On 1 January 2011 the Trade Practices Act 1974 was renamed the Competition and Consumer Act 2010

- Inefficient practices of some regional airlines are facilitated , such as the prolonged parking of aircraft on the scarce apron at Sydney Airport, which increases the need for investment and therefore increases charges for international and domestic passengers
- Inter-state and international passengers cross-subsidise intra-NSW passengers.

Developments over the past decade

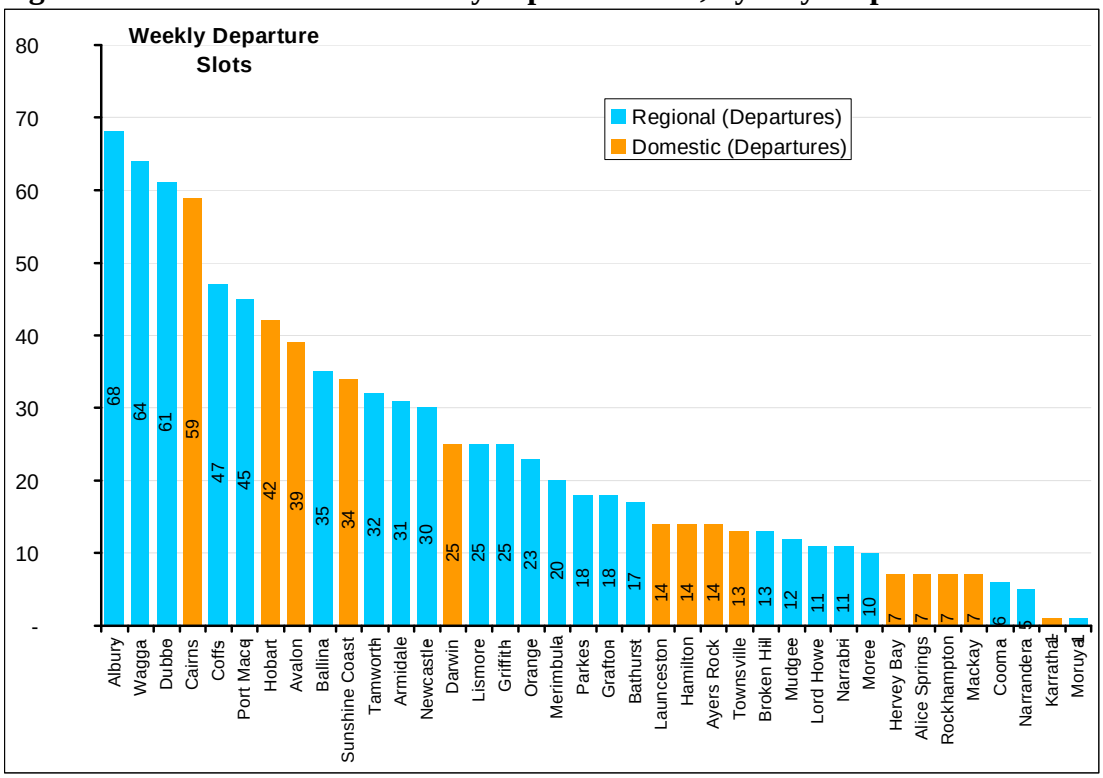
Over the past decade the domestic market has changed profoundly. Prior to Ansett's collapse in 2001, this market was almost exclusively served by two full service carriers (Qantas and Ansett) and their subsidiaries. Immediately following Ansett's collapse, the market was dominated by Qantas. The intra-state market is now served by six airlines: two network carriers, one LCC and three independent regional airlines.

Clearly the 'Ansett protected' regulation, designed to promote new entrants, has fulfilled its policy objective. There is now broad industry support to withdraw this direction, which the Minister can do without legislation.

The competition on intra-state routes has varied. Some routes, particularly to coastal leisure destinations, are now better served than some domestic routes (see Figure 2). Other routes, largely to smaller inland communities, have not received these benefits. This market segmentation mirrors the NSW *Air Transport Act 1964*, which licences and regulates air transport on routes servicing smaller communities to encourage stability, route development and continuity of services to regional areas. With the exception of Newcastle, routes that operate at or below 50,000 passengers per year are licensed under the state legislation to one operator only. Whilst the majority of intra-NSW routes are licensed, 87% of intra-state passengers flew on deregulated routes[17].

[17] NSW Government, Quarterly Passenger Statistics for NSW Air Routes to and from Sydney Airport, http://www.transport.nsw.gov.au/air/passenger-stats.html

Figure 2 Destinations of weekly departure slots, Sydney Airport



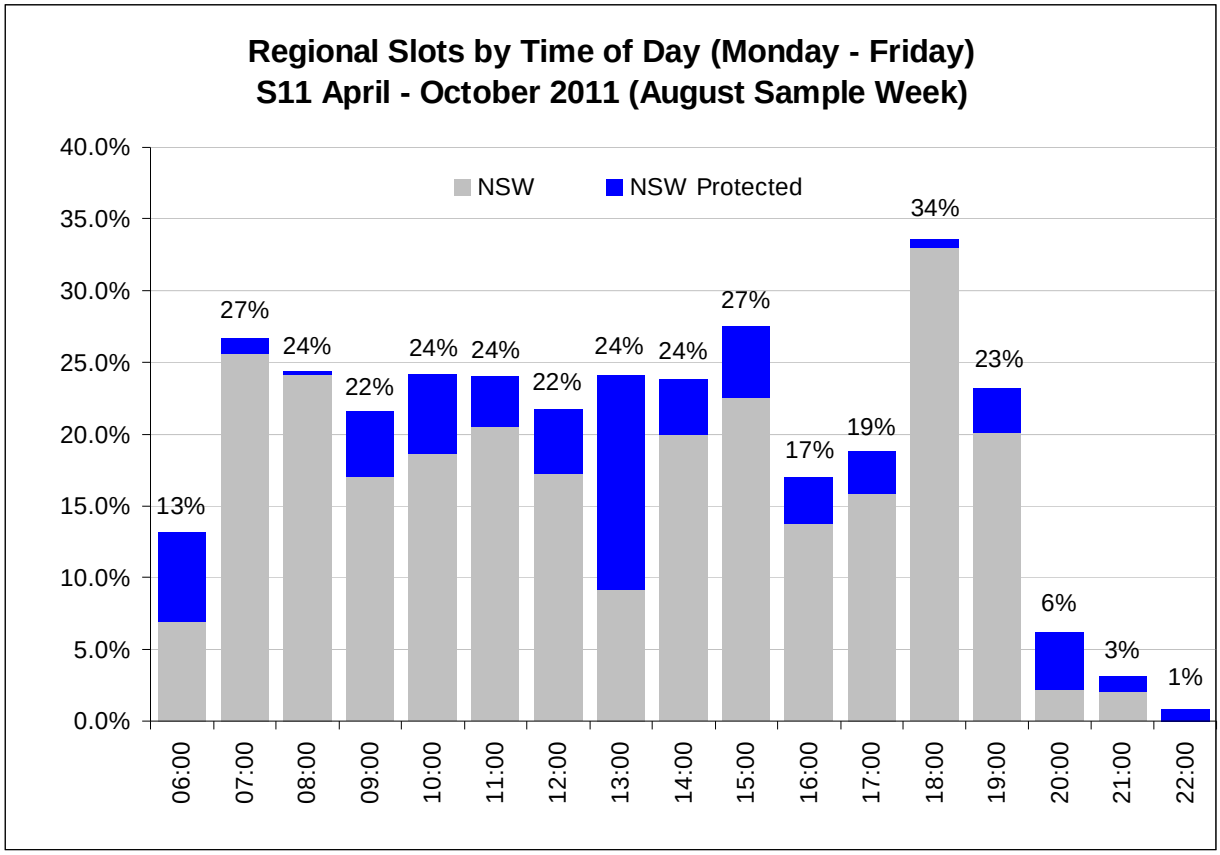
Source: Airport Coordination Australia (ACA) Northern Winter 2010 November Sample Week

Regional services make a positive economic contribution to regional communities, Sydney Airport and the broader economy. They are also vital for providing regional communities with access to essential services. Sydney Airport continues to support the development of this market segment, but believes these benefits could be further promoted if:

- The regulations directly benefited regional communities
- The regulations reflected the level of protection required for different communities, in a manner similar to the NSW *Airport Transport Act 1964*
- The regulations were holistic. Of the more than 200 airports in Australia only Sydney Airport is subject to regulation governing the prices and access of regional services. As a result, there have been continuous increases to charges at many regional NSW airports, while Sydney Airport has not increased its regional charges since 2001. Sydney Airport now has amongst the lowest comparable airport charges for regional airlines[18].

[18] Regional Airport Benchmark study – E&Y, attached as annexure 11

Figure 3 Regional slots by time of day, Sydney Airport



Source: Airport Coordination Australia (ACA) Northern Summer 2011, sample week

3.7 Demand for Airport Facilities and the Master Plan

As outlined in the Master Plan 2009, Sydney Airport expects to be able to accommodate forecast traffic for at least the next 20 years. The Master Plan 2009, which provides Sydney Airport's vision for the operation and development of the airport to the year 2029 and the strategies required to sustainably meet Sydney's future air transport needs, is based on:

- No changes to aircraft flight paths
- No changes to the curfew
- No changes to the aircraft movement cap
- No new runways
- No change to access arrangements for regional airlines.

The level of aviation activity is forecast to grow over the next 20 years as follows:

- Aircraft movements by 1.8% per year to 427,400 in 2029
- Passengers by 4.2% per year to 78.9 million in 2029
- Air freight by 2.5% per year to 1,077,000 tonnes in 2029.

Catering for the demand as forecast in the Master Plan relies on a combination of:

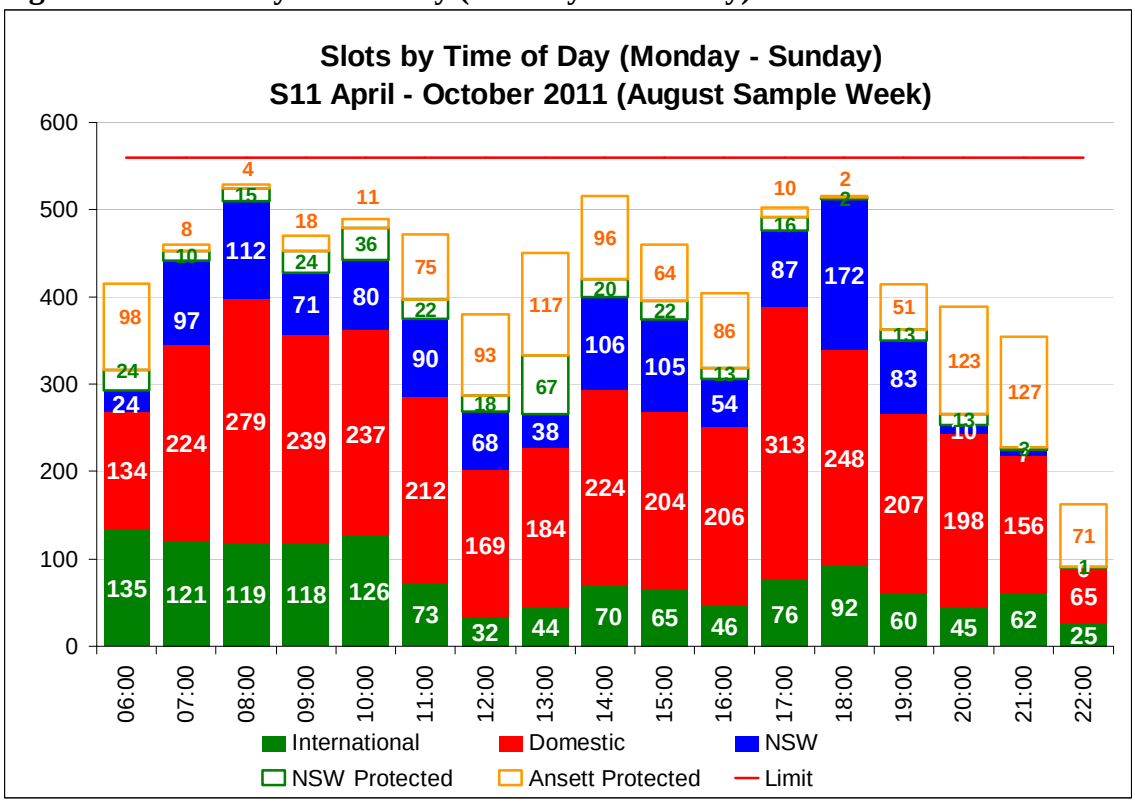
- Airlines' use of larger capacity aircraft will drive an increase in the average number of passengers per aircraft from 127 in 2009 to a forecast 196 in 2029, an increase of 54%
- The use of more slots, both in peak and particularly outside the peak
- Faster growth of aircraft movements at the airport on off-peak days.

These trends are consistent with past trends. For example, average passengers per aircraft increased by 21% between 2002 and 2010, despite the various constraints imposed on Sydney Airport.

As shown in Figures 4 and 5, it is anticipated that:

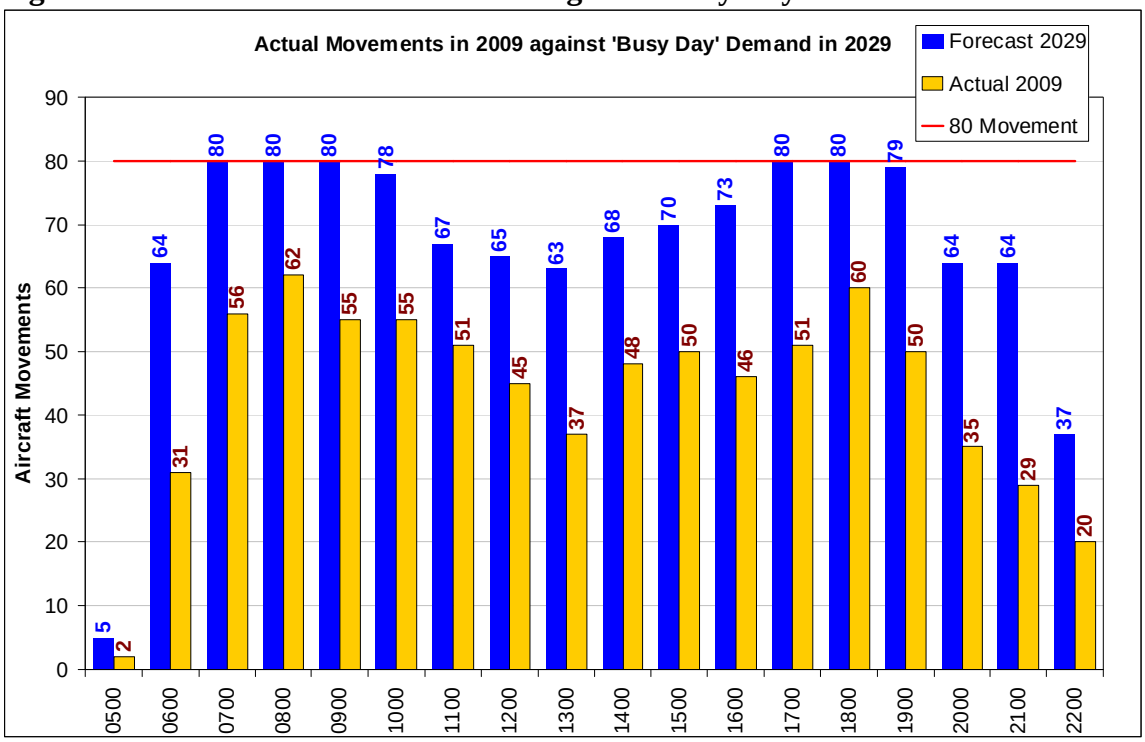
- There are relatively few unprotected slots available for allocation in the peak hours
- All the peak hour slots, both 'protected' and unprotected, will be allocated by 2029
- The peak hours will broaden by 2029
- There will be strong growth in activity in the off-peak hours

Figure 4 Slots by time of day (Monday – Saturday)



Source: Airport Coordination Australia (ACA) Northern Summer 2011

Figure 5 Actual movements in 2009 against 'Busy Day' demand in 2029



Source: Sydney Airport analysis and Sydney Airport Master Plan 2009

3.8 Conclusions and Recommendations

Sydney Airport is Australia's premier international gateway.

Whilst the *Master Plan 2009* demonstrates that Sydney Airport is able to meet demand until at least 2029, it is in the interests of Australia that the most efficient use is made of the nation's most important infrastructure asset and international gateway.

Sydney Airport recommends that:

The artificial constraints in place at Sydney Airport be reviewed to ensure that the Government's overall objectives are being met, balancing the interests of all stakeholders.

These changes would both attract new airlines and services, for the benefit of the community, and will also ensure that Sydney Airport is able to meet demand well beyond 2029, postponing the need for the government to spend substantial sums to construct additional capacity elsewhere. It is important that the regulations governing Sydney Airport are as responsive to the changing technology and competitive environment as the airlines and airport themselves are.

With each additional daily A380 contributing $300-400 million to the NSW economy, the benefit forgone of the current regulations could easily exceed $1 billion each year and will increase over time[19].

[19] Australian Bureau of Statistics (ABS), Average international visitor consumption – Page 20 table 8

4. Achievements under light-handed regulation

Key points

- The aim and key principles of the light-handed regulatory regime are to promote the economically efficient operation of airports.
- Under light-handed regulation, Sydney Airport has delivered
  - Commercial agreements with all international and domestic airlines, including individualised multi-faceted agreements for many airlines
  - Continuing investment
  - Improvements in service quality resulting from a range of initiatives
  - Stable and reasonable charges.
- The light-handed regime remains the most beneficial, flexible, and economically efficient method of regulation for major Australian airports because:
  - Continuing the deregulation of the aviation sector in response to the more competitive business environment, in which airports are required to be more flexible and manage a wider array of risks, will enhance the benefits to the community.
  - The increased need for flexibility also raises the costs of inappropriate regulation.

4.1 Aim of light-handed regulation

The aim and key principles of the light-handed regulatory regime[20] are to promote the economically efficient operation of airports – primarily through commercial agreements and in a commercial manner. Airports and airlines should have the appropriate incentive to negotiate in good faith and conclude commercial arrangements, whilst airports should have sufficient certainty to undertake ongoing investment at the airport.

The intention of the light-handed regime was not to enforce compulsory commercial agreements between airports and airlines. However, such commercial arrangements assist to demonstrate the ability of airport operators and their airline customers to reach agreement without regulatory intervention on price, service quality or investment.

The light-handed regime remains the most beneficial, flexible, and economically efficient method of regulation for major Australian airports. Continuing the deregulation of the aviation sector in response to the more competitive business environment, in which airports are required to be more flexible and manage a wider array of risks, will enhance the benefits to the community. The increased need for flexibility also raises the costs of inappropriate regulation.

Any increase in regulation would potentially give rise to substantial costs (depending on the regulation), including:

[20] Review Principles outlined by Government in response to the Commission's 2002 inquiry into Airport Price Regulation, http://www.treasurer.gov.au/DisplayDocs.aspx?pageID=&doc=pressreleases/2002/024.htm&min=phc

- Direct costs: increased costs of staff and auditors to prepare financial information and ongoing reports, as well as staff and consultants for preparation of documents relating to any regulatory decisions
- Cost of uncertainty: increased regulatory uncertainty may undermine investment and long term planning
- Market distortions: increased focus on regulatory processes may distract from collaboration between airports and airlines reduce the flexibility of the airport and airlines to respond to change, and give rise to regulatory gaming.

4.2 Achievements of Sydney Airport under the light-handed regime

The light-handed regime at Sydney Airport has delivered:

Commercial agreements

- Evolution from traditional 'conditions of use' agreements to multifaceted commercial user agreements with all scheduled international and domestic passenger airlines
- Renegotiation of commercial user agreements to reflect changes to the economic environment and airline business models
- No disputes with airline users requiring mediation, despite an agreed mediation process
- Collaboration with airlines on a number of non-aeronautical projects such as car parking commission agreements, branding and advertising, and premium ground transport services.

Continuing investment

- High levels of investment to meet passenger and airline needs
- Extensive and continuous consultation on the timing and design of capital expenditure
- Reprioritisation of capital investments to meet evolving airline business models and to reflect changes to the economic environment.

Quality of service

- Consistent high quality of airport facilities and services, reflected in passenger surveys
- Increased customer focus and the introduction of collaborative service level commitments

Charges stability and innovation

- Underlying price stability, and returns on capital that are clearly reasonable for an airport business with the characteristics of Sydney Airport
- Innovation in airline agreements such as off-peak pricing, growth incentive models and the inclusion of a broad array of non-aeronautical components.

Significantly, improvements in the financial performance of Sydney Airport since the introduction of the light-handed regime have been driven by increased internal cost control, increased passenger numbers, broader commercial product offerings and efficiency gains, rather than by increases in charges that are not cost-related. These are the types of outcomes expected from the introduction of private sector innovation and discipline through the airport privatisation program.

4.3 Commercial Agreements

At the time of privatisation Sydney Airport enforced a Conditions of Use (COU) which had been developed from the former Federal Airports Corporation (FAC) by-laws. The COU included both price and non-price terms, and use of the airport constituted contractually binding acceptance of the terms and conditions – in much the same way as those entering a commercial car park do so on the basis of the terms and conditions displayed at the point of entry.

After privatisation, Sydney Airport negotiated COUs with a number of parties:

- A COU for the use of T1 was agreed with BARA on behalf of the international airlines. This also included a commercial agreement for the use of check-in-counters.
- Non-standard COUs have been negotiated with Qantas (later extended to Jetstar), British Airways, Air New Zealand, and the Virgin Blue group of airlines.
- Only casual users of Sydney Airport and some dedicated freight operations use the international facilities under the provisions of Sydney Airport's standard COU..

Similarly, Sydney Airport has negotiated commercial agreements with all domestic operators in T2, which was acquired from Ansett Australia following its collapse. These commercial agreements extend to 2019 with Virgin Blue, Qantas and Jetstar for T2, and licence arrangements for varying periods with other domestic and regional carriers for the use of that terminal.

In 2004, once the Government accepted Sydney Airport's 2003/4 Master Plan, negotiations began on the prices and terms to apply to domestic and international use of the airfield and to the international passenger terminal (T1). As was noted in the 2006 Productivity Commission review, different views on the value of land made reaching an agreement difficult – and both Virgin Blue's declaration application and the process of the Productivity Commission review itself acted as disincentives for the airlines to reach an agreement.

Once the arrangements to apply to the second period of light-handed regulation were confirmed, Sydney Airport was able to relatively quickly conclude commercial agreements. By the end of calendar year 2007, agreements were in place with all international and domestic scheduled passenger airlines servicing the airport.

The light-handed regime provided the flexibility to include items in negotiations such as alternative runway charge structures, innovative pricing models and a broad array of non-aeronautical components. In this regard, a light-handed environment also provided the possibility to negotiate different compromises with different parties, which best meet mutual preferences.

These agreements established a negotiated 'base' level and structure of aeronautical charges for a five year period, with provision for recovery of the cost of new investments over the period, specific discounts, and a range of aeronautical and non-aeronautical terms. The costs associated with providing government mandated security services are recovered on a separate cost pass through basis.

The standard 2007 international agreement provided for:

- Five year price certainty on the base passenger charge
- One-off discount of $2.9 million against total capital costs

- A discounted Weighted Average Cost of Capital (WACC) on future investments
- Sydney Airport assumed all traffic risk associated with the recovery of new investments
- Increased airline consultation on capital investment decisions[21] (see Section 4.6)
- Agreement on the major redevelopment of T1 (see Section 4.7)
- Agreement on specific investments requested by airlines (for example, construction of an aerobridge for Code C aircraft at Gate 55 in T1)
- Service level undertakings with financial rebates where they are not met (for example, international airlines prefer contact aircraft parking positions. Those passengers on non-contact positions are bussed and airlines receive a discount between $2 and $3 per passenger)
- Commitment not to introduce any fees and charges associated with provision of ground handling services
- Up to 50% discount for new off-peak services, including services to new destinations, increase in frequency, positioning or training flights, and rescheduling peak flights[22]
- Simplified, plain English contracts for the use of the facilities.

Following the conclusion of the commercial negotiations on 6 September 2007, the Executive Director of BARA, Warren Bennett, recommended its member airlines formally accept the agreement and later welcomed the commencement of construction works for the upgrade and expansion of T1 redevelopment project. In a media release, Mr Bennett was quoted:

Airports and airlines have to work together to take advantage of the opportunities for sustained growth that are emerging. I am very pleased that the upgrade to Sydney Airport is now underway. There has been extensive consultation between BARA and Sydney Airport on this project. The consultation process was valuable in producing an outcome that meets airlines' ongoing operational requirements. As well as providing upgraded passenger facilities the project will provide much needed operational improvements to the baggage handling system. [23]

Additional commercial terms were reached with a number of other airlines that extended beyond the standard agreements[24]. The scope and range of terms covered by these agreements are extensive and customised to each airline's requirements, and they have been adapted to changes in the airlines' business models and route networks. The individual agreements include tailored multi-part pricing and non-aeronautical activities. These enhanced and multi-faceted agreements have significantly increased Sydney Airport's commercial focus and collaboration with all airline customers since 2007[25] and may not have been possible under a more interventionist regulatory regime.

During the economic downturn in 2009 that resulted in falling passenger demand, a number of airlines approached Sydney Airport to renegotiate and amend the terms and conditions in those agreements. Despite the known commercial risks that eventuated and contracted terms in place, Sydney Airport positively responded by renegotiating several key contractual terms

[21] ACICG – Aeronautical Capital Investment Consultative Group, Sydney Airport ongoing airline consultation forum discussing new capital investments
[22] Schedule 8 – Sydney Airport Conditions of Use
[23] Media release BARA Welcomes Upgrade Sydney Airport International Terminal, 16 October 2007, http://www.sydneyairport.com.au/SACL/DownloadDocument.ashx?DocumentID=583
[24] Commercial-in-Confidence
[25] Commercial-in-Confidence

including the need for lower investment due to lower traffic volumes[26]. The resulting arrangements underscore the collaboration and close commercial partnership Sydney Airport now enjoys with several airline partners.

During the economic downturn, Sydney Airport also took various steps itself to limit the impact of declining demand by reviewing its own costs and undertaking a comprehensive review of capital investments in consultation with all airport users. Sydney Airport deferred a number of capital projects by extending the life of existing assets and/or deferring projects due to slower passenger demand. The net effect will be slower increase in airport charges in the years between 2009 and 2012 than previously advised.

The structure of passenger based charges aligns the airline and airport commercial interests to increasing passenger demand. As such, when airlines suffered a decline in passenger demand and load factors, Sydney Airport shared in the risk by charging proportionately less per flight. The flexible approach to capital investments and greater collaboration with users on prioritising those investments considerably improved the working relationship Sydney Airport enjoys with the wider airline community and representative bodies.

Further examples of collaborative partnership arrangements include the provision of Common User Terminal Equipment (CUTE) and aircraft Ground Power and Pre-Conditioned Air (GPPCA) in T1.

Sydney Airport assumed responsibility for the provision of CUTE services in 2009 in T1. The CUTE price agreed with the airlines represented a significant saving over the previous arrangements made between the airlines and the incumbent service provider. The CUTE services negotiated by Sydney Airport enabled a significantly lower price to be fixed for five years, provided upgraded equipment with enhanced system capabilities, and a comprehensive user service agreement.

Similarly, Sydney Airport, in partnership with the airline community, invested over $26 million to install GPPCA. GPPCA provides a more cost and environmentally efficient energy supply to aircraft parked on the apron than the use of aircrafts' auxiliary engines. As a result, although these investments increased the Sydney Airport passenger service charge, they reduced the overall cost of doing business for the airlines, while also delivering an environmental benefit.

4.4 Negotiation and dispute resolution

The overarching principle of the light handed regime is that airport charges and terms and conditions should be commercially negotiated with airlines. Sydney Airport conducts its commercial negotiations with its airline customers and industry representatives substantially on an open-book basis. During the ACICG process and price negotiations, Sydney Airport provides detailed cost and methodological information to its airlines. That information includes copies of models, workings and any supporting documentation. In addition, for large capital projects (for example, T1 redevelopment) or technically complex projects (for example, baggage handling systems), specialised forums are constituted to consult with stakeholders and their respective experts.

[26] Commercial-in-Confidence

Bi-lateral commercial agreements have been negotiated with all of the domestic airlines and some of the international airlines. These agreements more closely reflect the individual circumstances of the airline, are generally more complex, and reflect the airlines' increased negotiating leverage. The majority of the international airlines chose to negotiate a multi-lateral agreement, with BARA collectively bargaining on behalf of its members.

There are adequate dispute resolution procedures and deterrents to misuse of market power

In Sydney Airport's view, there are adequate deterrents from the misuse of market power arising from joint and interdependent interests and, moreover, remedies for concerned parties to follow. The reasons underlying/supporting this view are:

- There is a high level of competition - both nationally and internationally - for the deployment of airlines' aircraft
- The standard COU contains a process for dispute resolution by mediation[27], and dispute resolution clauses have been negotiated in all of the commercial agreements. This arrangement has been in place from the start of commercial agreements and in recent years there have been no commercial disputes or the requirement to invoke the dispute resolution process. Furthermore, there is scope for airlines to negotiate different dispute resolution arrangements
- Negotiations with airlines have included the sharing of cost-related information, ensuring that the airlines can assess the reasonableness of the price within the context of the broader commercial negotiation
- Sydney Airport receives a high level of public attention, as do many large airports. As a result, it is certain that any attempt to misuse market power would receive public attention. This would damage the reputation of the airport, with an immediate impact on profitability
- If there were strong evidence of the use of market power, the Government will always have the power to intervene. For example, it could do so via Part VIIA or through legislative change (which could include deemed declaration)
- The airlines have legal remedies available through contract law and the *Competition and Consumer Act 2010*[28].

'Binding arbitration' undermines the objectives of the light-handed regime

'Show cause' and 'binding arbitration' processes effectively amount to the reintroduction of shadow regulation. The shortcomings of the previously proposed 'show cause' framework are well documented and one about which both Sydney Airport and its airline partners expressed concerns.

It is difficult to conceive of an externally imposed dispute resolution procedure – in effect, the appointment of an umpire – that will not present an opportunity for one or both parties to recreate the outcomes of a more heavy-handed regulatory framework and undermine the benefits of the light-handed regime. Such a dispute resolution procedure would need to avoid several difficulties:

[27] Sydney Airport Conditions of Use, Clause 16, available at http://www.sydneyairport.com.au/SYDNEY AIRPORT/DownloadDocument.ashx?DocumentID=1158

[28] On 1 January 2011 the Trade Practices Act 1974 was renamed the Competition and Consumer Act 2010

Regulation by stealth: without careful design any dispute resolution procedure is likely to create a 'common law' regulation as a result of the accumulation of regulatory decisions being interpreted as precedents. On the other hand, an express requirement that new arbitrators are used for each dispute without reference to previous decisions will lead to increased risk and reduce the likelihood of investment

Regulatory escalation: international evidence is clear that both airports and airlines can 'game' any regulatory systems put in place. As a result, repeated use of arbitration over time will require increasingly detailed involvement of the arbitrator in the operation of the airport, which is likely to progressively undermine the efficient use of and investment in the airport

Proliferation of disputes: there is likely to be a proliferation of disputes if arbitration decisions are widely interpreted as being favourable to either airports or airlines. This could intervene with commercial negotiations and with the dispute resolution procedures that have been negotiated. Materiality thresholds and other hurdles (exhaustion of commercial mediation, evidence of 'course of conduct' and a clearly defined scope) could reduce this issue but are unlikely to remove it.

Breakdown of commercial relationships: as might be expected it is common for collaboration and commercial relationships to break down during legal or regulatory processes. Given the length of arbitration processes, this could substantially undermine the promotion of the more efficient use of and investment in the airports

Delayed investment: arbitration processes are rarely quick and, as a result, investment could be significantly delayed.

4.5 Benefits from reduced regulatory intervention

Regulatory intervention risks displacing commercial agreements and the benefits that flow from them. This is partly because of the additional uncertainty that flows from inevitably lengthy process (including the present Productivity Commission review) but also because of the focus on regulatory theory rather than commercial practicalities and the discovery of mutual preferences.

Likewise, the regional price cap has impinged on the negotiation of commercial agreements with the dedicated regional airlines[29] – the only group of airlines with which Sydney Airport has not been able to negotiate individual airline agreements. Without the ability to negotiate, it is impossible to estimate mutual benefits foregone, but they could be substantial over time. For example, during 2010, Sydney Airport was in advanced discussions with a dedicated regional airline as part of the consideration to notify declared regional charges to the ACCC. With the prospect of a small price increase, Sydney Airport presented a proposal including peak and off-peak charges, volume discounts, efficiency incentives and other non-aeronautical business initiatives to mitigate and potentially even lower the airlines' costs. Substantive negotiations took place between the airport and the airline. However, the ACCC decision to not allow the first price increase since 2001 removed any perceived incentive for the airline to conclude a commercial agreement and discussions stalled.

[29] Sydney Airport has negotiated commercial agreements with Qantas, Virgin Blue, Jetstar and Tiger Airways for their domestic and regional operations.

More broadly, passenger and aircraft related aeronautical charges are playing a reduced role in the evolution of commercial agreements. Considering the rapid evolution in airline business models and changes to airline alliances, aircraft fleet types, passenger demand and level of service offering, Sydney Airport is taking a flexible and adaptive approach to all these increasingly complex commercial considerations. In this context action by the airport to assist its airline partners can assist with the airlines' focus on costs overall, rather than simply on airport charges and can potentially grow traffic volume.

The evolution of Virgin Blue at Sydney Airport is a case in point. Over a short period of time it has moved from a pure low cost point-to-point airline into an airline offering a virtual global network in co-operation with alliance partners, a full service offering, and increased fleet mix. Sydney Airport has responded accordingly by customising its service offering, providing premium lounges and other property, accommodating a greater range of aircraft types across its terminals, and providing the opportunity to establish a new maintenance base.

The benefits of growth in air services under the liberalised regime include distributional benefits. Flexibility has introduced lower cost services, enabling many more people to travel who could not have previously afforded it. The enrichment of new routes and destinations has also provided benefits to communities outside capital cities (although existing restrictions at Sydney Airport limit the developments in this area – see Section 3). As to the distribution of income between airlines (and passengers) and airports (and shareholders), , in theory, efficiency could be compatible with varying outcomes. In practice, the commercial reality is that where potential market power is not exercised, the outcomes will be of mutual benefit to the interdependent businesses, their dependent businesses, their customers, their employees and their shareholders.

The demonstrated benefits and potential future improvements resulting from enhanced, wide ranging and customised commercial agreements is dependent on the continuation and certainty of the light handed regulatory regime.

4.6 New Investments at Sydney Airport (ACICG process)

The Government's Review Principles[30] stipulate that consultation mechanisms should be established with stakeholders to facilitate the two way provision of information on airport operations and requirements. Sydney Airport has engaged in extensive consultation with its airline partners in relation to each of the new investment projects it has contemplated under the light-handed regime.

This ongoing consultation on new investments is facilitated via the monthly Aeronautical Capital Investment Consultative Group (ACICG) meeting to which representatives of all airlines are invited. New aeronautical capital investments are presented and discussed. Furthermore, the commercial agreements struck with the airlines also contain contractual obligations for comprehensive consultation processes, including development and implementation of the new investments.

This process is comprehensively documented and a broad range of airlines and industry representatives participate. The process is supported by a 'building block' approach to

[30] Review Principles outlined by Government in response to the Commission's 2002 inquiry into Airport Price Regulation,
http://www.treasurer.gov.au/DisplayDocs.aspx?pageID=&doc=pressreleases/2002/024.htm&min=phc

pricing new investments with parameters substantially negotiated and governed by the airline commercial agreements. Each project is presented in detail and on an open book basis. Typically, Sydney Airport will seek explicit support from participants for the project and the associated charge before commencing any substantive capital works. If support is not provided, projects have in all cases been modified, delayed or discontinued.

The level of consultation has been more extensive than it previously was under heavy-handed regulation. As a result of the extensive consultation:

- The level of investment has been better attuned to economic circumstances, ensuring that airlines do not have to pay for under-utilised investments (for example, the investment program was re-prioritised following the GFC to reflect lower traffic volumes)
- The design of investments has been improved through collaboration
- The lack of a formal regulatory process has generally resulted in a shorter approval process and more timely subsequent delivery of investment in most cases.

4.7 Timing of Nature of Capital Investments

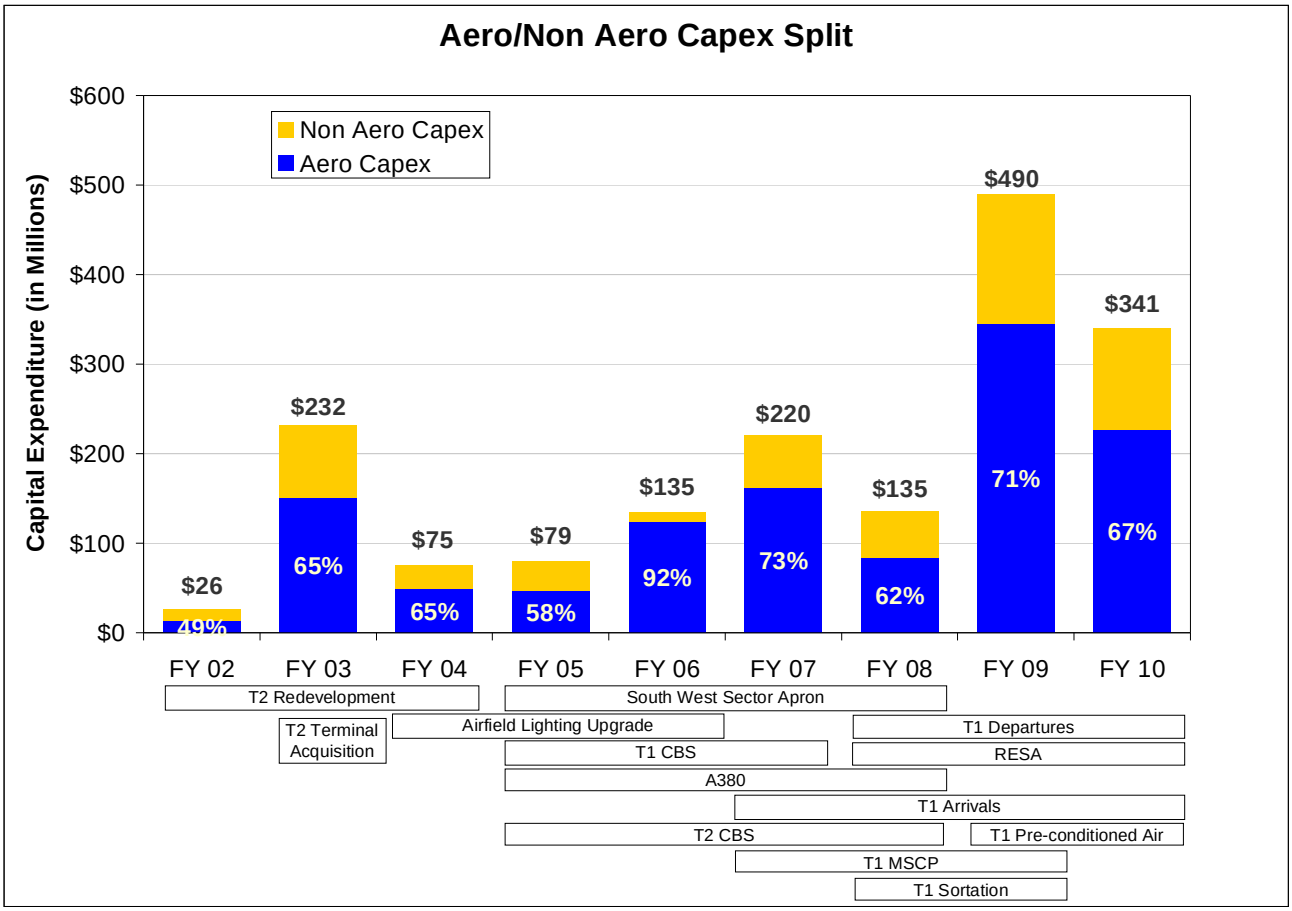
The light-handed regime has been characterised by a continued commitment to new investment in aeronautical assets to meet the needs of the aviation industry, airlines and the travelling public. In all, Sydney Airport invested $1.8 billion from July 2002 to December 2010 (see Figure 6), compared to total revenues of $6.8 billion over the same period. Approximately 70% of this capital investment has been on aeronautical facilities. Information on significant recent aeronautical investments is given in Table 1.

Table 1 Top 10 investment projects, Sydney Airport (five years ending December 2010)

No.	Project Description	Investment Type	Investment
1	T1 Departures Development	Shared	$214m
2	A380 Project	Aeronautical	$120m
3	Runway 25 runway end safety area (RESA)	Aeronautical (safety)	$100m
4	Check Bag Screening	Aeronautical (security)	$90m
5	Airfield lighting upgrades	Aeronautical (safety)	$67m
6	T1 multi-storey car park	Car parking	$65m
7	T1 baggage handling system building works	Aeronautical	$53m
8	T1 arrivals - Southern reclaim	Aeronautical	$29m
9	Ground power & preconditioned air	Aeronautical	$26m
10	Aircraft apron parking (southwest sector)	Aeronautical	$20m

Source Sydney Airport Analysis

Figure 6 Capex spilt – aero/non aero, Sydney Airport (FY2002- FY2010)



Source: ACCC Accounts and Sydney Airport analysis

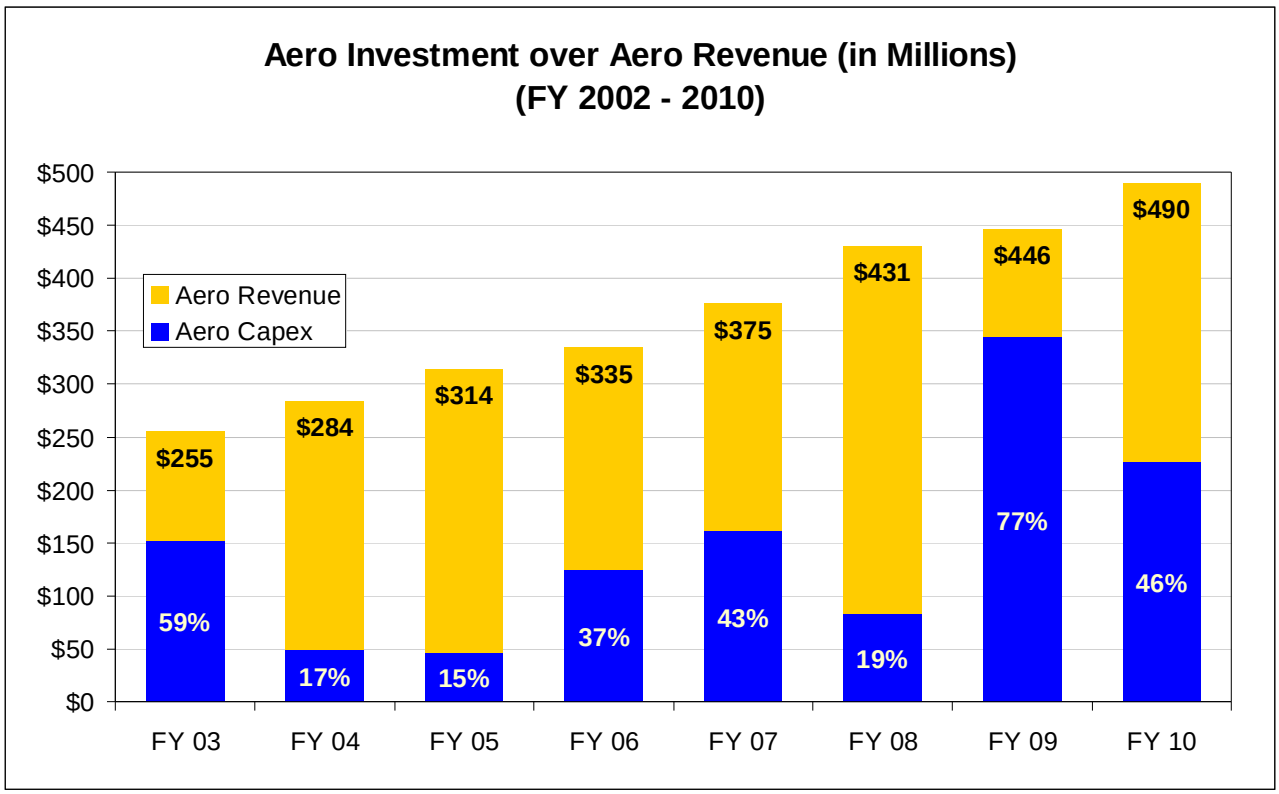
The planning and timing of major capital investments at Sydney Airport is undertaken to comply with government mandated requirements such as the Runway 25 RESA, or to provide sufficient capacity to facilitate forecast demand, for example, T1 Departures development. While all investments are made with reference to the approved Master Plan and in consultation with airline users, the light handed regulatory framework means that adequate incentives are available to airports to invest in providing sufficient capacity to meet forecast demand – not least because the opportunity cost of not providing sufficient capacity is significant for airports such as Sydney with half of revenue derived from non-aeronautical services (see Figure 7). But airports also need to take due account of airline caution about airports investing and increasing passenger charges before the investment is needed. Commercially oriented consultation processes help this balance to be achieved.

A determining factor of airport runway and terminal capacity is an assessment of peak day and/or peak hour performance. In 2000, around 25.3 million passengers used Sydney Airport. By 2010, total annual passenger volume had grown by nearly 41 percent to 35.6 million passengers with a peak day of 120,275 passengers. Over the same period the number of all aircraft using Sydney Airport increased by less than one percent – from 307,058 in 2000 to 308,914 in 2010[31]. While the average number of passengers per aircraft movement has significantly increased from 94 to 125, Sydney Airport has invested considerable sums in a

[31] Airservices Australia and Sydney Airport – An Overview Fact Sheet: http://www.sydneyairport.com.au/SYDNEY AIRPORT/Fact-Sheets.html

timely manner to accommodate the growth in aircraft size and improved the airport's utilisation during off-peak periods.

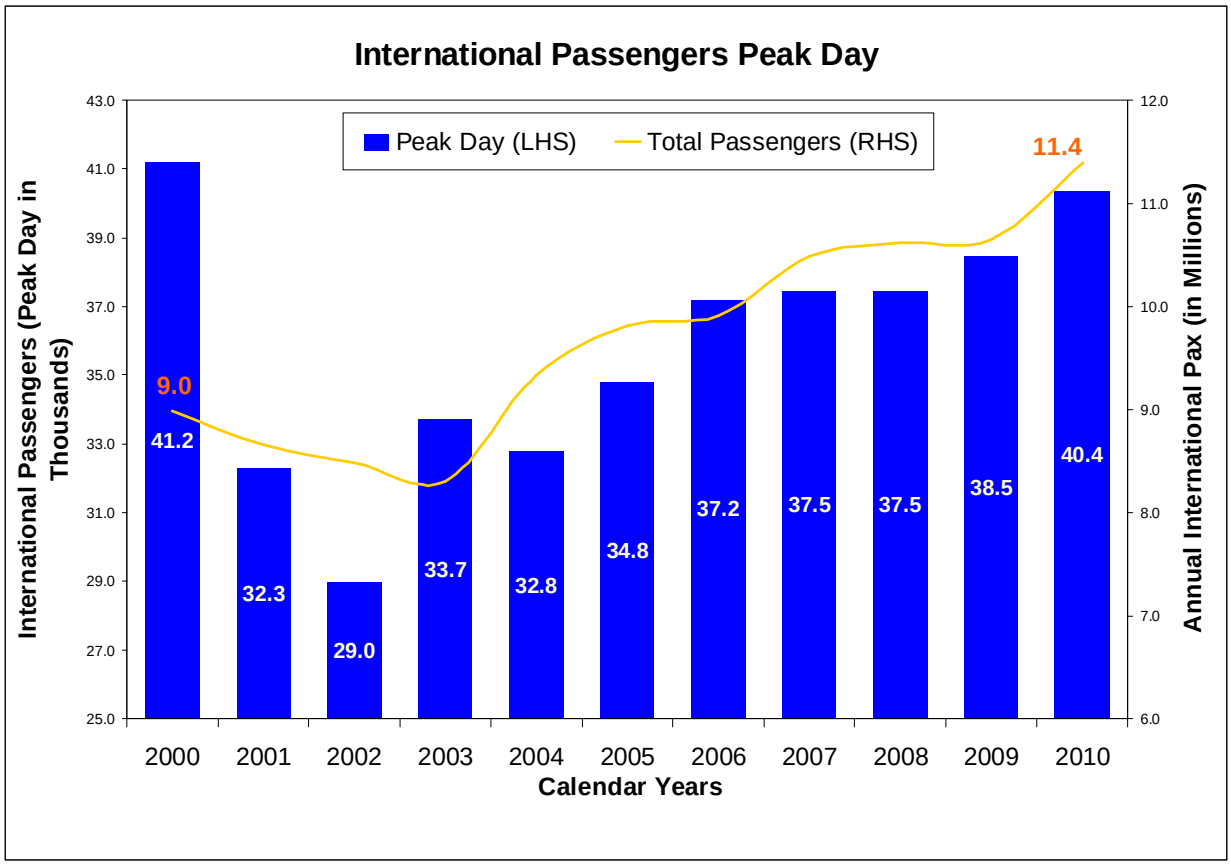
Figure 7 Aero Investment over Aero Revenue (in Millions) (FY2002- FY2010)



Source: ACCC Accounts and Sydney Airport analysis (includes security)

In 2000 on the peak day there were 41,200 international passengers (see Figure 8). The International Terminal Building (now known as T1) was specifically designed to handle that peak day during the Sydney Olympics. Since then, the 27% growth in annual international passenger volumes has been easily accommodated by filling the excess capacity – the peak day for international traffic in 2010 was still lower than the Olympics-related peak recorded a decade ago and for which the terminal was designed.

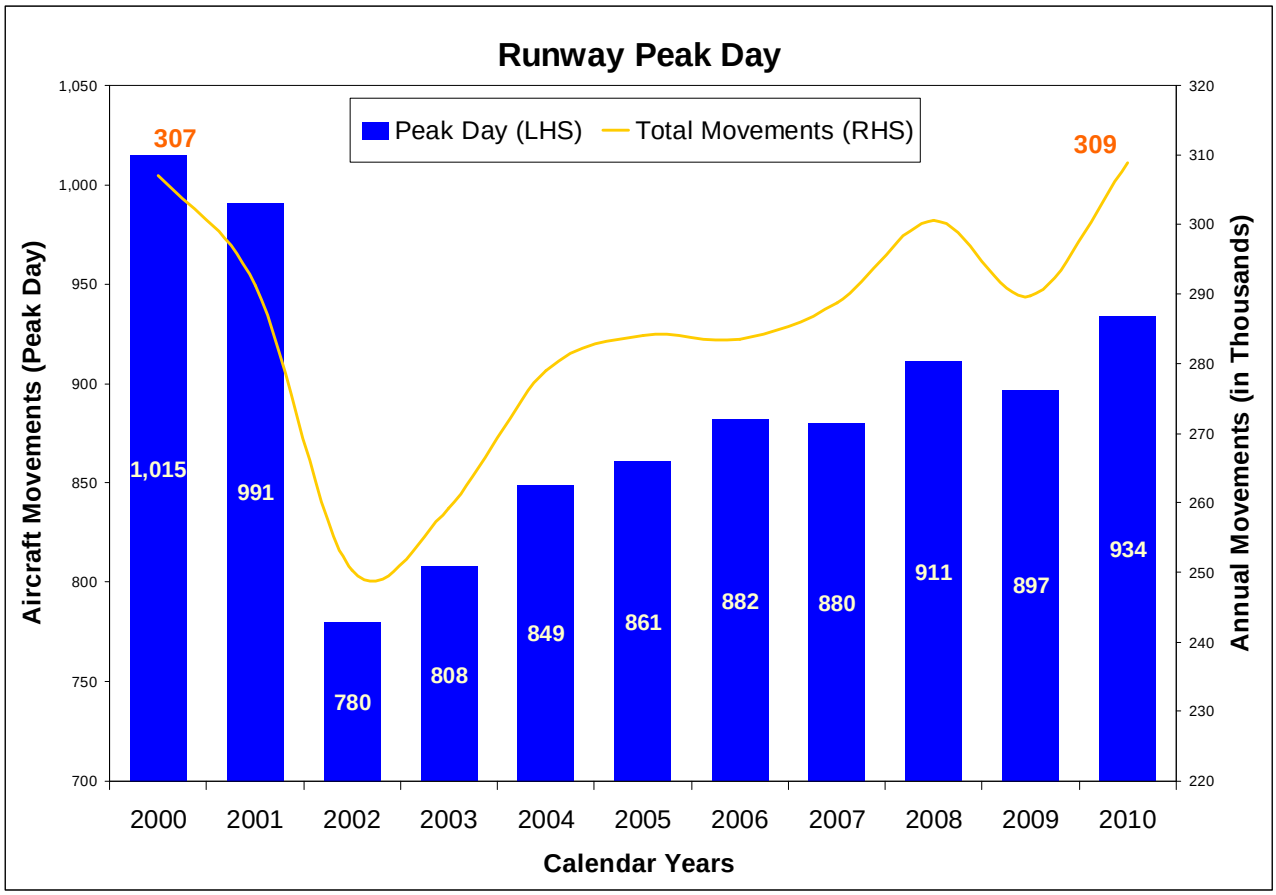
Figure 8 Sydney Airport – internation passengers peak day (2000 – 2010)



Source: Sydney Airport Analysis

Similarly, in 2000 on the peak day there were 1,015 runway movements and 307,058 in total (see Figure 9). By 2010, peak day runway movements are still 8% below that 2000 peak with only 934 movements, while total annual volumes increased by less than one percent. As stated in the *Master Plan 2009*, Sydney Airport has ample runway capacity during shoulder peak and off-peak periods to accommodate future demand with timely new capital investments.

Figure 9 Sydney Airport – runway peak day (2000 – 2010)



Source: Air Services Australia (ASA); Sydney Airport Analysis

The ACCC's *Airport Monitoring Report 2009-10*[32] stated - without evidence - that Sydney Airport had potentially under-invested in maintenance and aeronautical services, and specifically that it had delayed the investment in T1:

[Sydney Airport]…*appears to have increased profits by increasing prices and permitting quality of service provided to airlines to fall below a satisfactory level over several years — especially at the international terminal. This appears to have been achieved through cost-saving measures (such as inadequate maintenance and delaying investment in services provided to airlines).*

…

Further, it is noted that a proportion of the investment undertaken by Sydney Airport in its international terminal was for non-aeronautical services, such a new retail, food and beverage outlets. Indeed, the airport receives almost half of its total revenue from such services. That the airport appears to have undertaken significant investment in non-aeronautical services, while potentially undertaking insufficient investment in aeronautical services, is consistent with the airport having a higher degree of market power in aeronautical services.

Sydney Airport considers that these comments are unfounded because:

[32] ACCC Overview of the monitoring results for aeronautical services Airport monitoring report 2009-10, pages 45 and 47-48

- As evidenced in this submission, Sydney Airport has invested more than $1.8 billion since privatisation in enhancing the passenger experience, meeting the needs of airlines, providing additional aeronautical capacity, and complying with government mandated safety and security requirements.
- Whilst the non-aeronautical investments may be more apparent to passengers, approximately 70% of the investments were on aeronautical assets. This is a significantly higher proportion than the aeronautical revenue share.
- The T1 redevelopment was opened when peak international passenger volumes remained lower than the peak Olympic volumes for which the terminal was designed – there was no delay in the T1 redevelopment
- Peak day international passenger volumes are still below the highest recorded level set in 2000
- Peak day runway movements are still below the highest recorded levels set in 2000 and 2001
- Sydney Airport commenced consultation with BARA on the T1 redevelopment by 30 September 2005. As previously presented, BARA acknowledged the extensive consultation and supported the timing of the T1 redevelopment when an agreement was finally reached in October 2007, several years prior to the observations made by the ACCC
- Consecutive ACI ASQ quality surveys show that Sydney Airport is ranked as high as or higher than comparable international airports
- Airline stakeholders and industry representative bodies were continuously consulted on and supported the timing and nature of capital projects (ACICG process)[33]
- In any event, Sydney Airport cannot increase its profits and has no financial incentive to delay investment since, under the commercial airline agreements; it is remunerated for investments once they are completed.

4.8 Service quality

Sydney Airport is committed to providing passengers and visitors with a high quality travel experience and, since 2002, has implemented a comprehensive program to improve the travel experience for passengers.

The program includes:
Investing in upgraded facilities and new services
Extensive and ongoing passenger surveys to identify priorities and track performance
An airport-wide Service Quality Improvement Program (SQIP)
Participation in Airline Operators' Committees
Negotiation of collaborative service level commitments with individual airlines

The overall experience of the passenger will depend on the level of service provided by the airline, government agencies such as Customs and Australian Quarantine and Inspection Service (AQIS), the airport operator and contractors such as those which undertake passenger security screening.

<u>Investing in upgraded facilities and new services</u>

[33] Commercial-in-Confidence

As noted in Section 4.7, since 2002 Sydney Airport has invested in excess of $1.8 billion in new facilities for passengers, airlines and other stakeholders. In addition to projects to expand capacity or meet new regulatory requirements, Sydney Airport has offered a wide variety of new services such as:

Passengers
- Introduction of a SMS flight information service and a new public address system
- Flight information screens upgraded with LCD screens throughout both T1 and T2
- Free wi-fi installed in both T1 and T2
- Introduction of a bag strapping service
- More airside food and beverage outlets, and a new landside food court
- Provision of undercover parking in both the international and remote long term car parks
- Provision of a covered and expanded waiting area for taxi passengers
- Free 15 minute parking at T1, and free 10 minute parking in the Domestic terminals, and new parking products including E-park (internet booking)

Airlines
- Ground power and pre-conditioned air for airlines which reduces the overall costs for the airlines and reduces environmental emissions
- Centralised contracting of CUTE, reducing overall costs
- Express-path security and immigration, for both arrivals and departures, introduced for the airlines' premium passengers

Border control authorities
- New outbound hall for the Australian Customs and Border Protection Service
- New security screening area
- Enhanced secondary screening facilities on arrivals
- Smart Gate introduced for Australian and New Zealand passport holders

Taxi drivers
- Introduction of a short fare taxi system at all terminals
- Upgraded facilities

The environment
- Recycling introduced into both T1 and T2
- A water recycling plant which provides recycled water for use in T1

Extensive and ongoing customer surveys

An integral part of Sydney Airport's commitment to improving the travel experience for passengers is the investment in a number of research programs designed to measure passenger satisfaction, identify priorities and track performance. These programs include:

Airport Service Quality*:* Sydney Airport participates in international benchmarking research known as the Airport Service Quality (ASQ) program. This program is facilitated by Airports Council International (ACI) and a total of 154 airports participated in the main ASQ Survey in 2010. This research program invites passengers to rate their levels of satisfaction with some 37 elements of the airport experience at T1 and 32 areas at T2. Passengers rate both overall service level (which is also separately reported for business and leisure passengers) and specific facilities and services including car park facilities; check-in, customs and

security processes; departure gate areas; washrooms; flight information screens; WiFi facilities; and food and beverage and retail offerings. The full list of parameters assessed is included in Appendix E.

The fieldwork for this program is conducted by a specialist market research company, Sweeney Research, which is AS:ISO 20252 accredited. A total of 2,200 passengers are asked to complete the survey each year and the completed surveys are sent to Geneva for processing by the program manager.

Results for the ASQ survey show that, for both T1 and T2, the average rating for the surveyed aspects at Sydney Airport over the four quarters of 2010 was higher than in any of the preceding five years.

Additional quantitative research: Sydney Airport supplements the ASQ program with an ongoing quantitative research program that was developed by Sweeney Research in 2005. The program is similar to the ASQ program in that it measures passenger satisfaction around the end-to-end airport experience. A total of 500 surveys are completed each month (6000 per year) at both T1 and T2 and a report is produced every second month.

Results from this program are shared with the Australian Customs and Border Protection Service and key performance indicators have been developed for internal Sydney Airport departments along with key contractors, such as those that undertake security and cleaning. Sydney Airport works with all areas of the business and contractors to identify ways in which the airport's performance can be continuously improved.

Results from the most recent survey results show high overall satisfaction with T1 – 42 per cent of passengers rated their satisfaction at 9 or 10 out of 10 and a further 44 per cent rated their overall satisfaction at 7 or 8 out of 10. In total, 86 per cent of passengers rated their overall satisfaction with T1 between 7 and 10 (out of 10).

Results from both programs are reported to Sydney Airport's senior management and board along with comprehensive advice on priorities for further improvement.

These ongoing programs cost in excess of $250,000 per annum. In the past two years, Sydney Airport has commissioned eight additional research programs for specific facilities or services.

The key objective of these specific research programs has been to obtain passenger feedback on particular aspects of service and to identify opportunities to further improve services. For example, a research program was conducted in 2009 to evaluate the public response to the new T2 pick-up area. This research found that 75% of users were satisfied or very satisfied with the new free 15 minute pick-up area and that 83% of users would definitely or probably recommend it to others. As a result of the survey, the free pick-up arrangements were extended to T1.

Airline Operators' Committees (AOC)

To ensure that it is directly aware of the concerns and views of airline customers, Sydney Airport attends meetings of the Airline Operators' Committee that were established by the airlines for both T1 and T2. The airlines' representatives are typically station managers, reflecting the AOC's strong operational focus.

The AOC meets monthly in relation to the efficient running of T1 and matters of concern to the station managers. Typical concerns are operational issues such as passenger facilitation provided by government agencies, air traffic control issues under the responsibility of AirServices Australia and any Sydney Airport related matters. Sydney Airport participates as a guest and responds to operational issues that the airlines may raise from time to time. Typical topics for discussion that touch on Sydney Airport's areas of responsibility could include use of the public address system, development of areas such as taxi-rank waiting zones, and participation of airlines at relevant meetings of interest chaired by Sydney Airport.

The AOC for T2 is chaired by a Sydney Airport representative and the work of the Committee is more narrowly focussed given that there are seven airlines operating from T2 compared to the 38 currently operating from T1.

Sydney Airport's Manager for Airline Relationships has responsibility for engaging with the AOCs and coordinates the airport's response to operational issues relating to facilities, services and special events.

Service Quality Improvement Program (SQIP)

Sydney Airport also established the Service Quality Improvement Program – commonly known as SQIP – in an endeavour to improve the passenger experience.

SQIP was developed from the insight that many different organisations are responsible for a passenger's journey through an airport terminal. As noted the overall experience of the passenger will depend on the level of service provided by the airline, government agencies such as Customs and AQIS, the airport operator and contractors such as those which undertake passenger security screening.

SQIP involves all relevant organisations being invited to work collaboratively to identify ways in which the passenger experience can be improved. Sydney Airport chairs the SQIP committee and invites representatives from airlines, government agencies, retailers and contractors including cleaners, security service providers and kerbside management companies to participate.

Some of the achievements from the SQIP to date include:
- The introduction of airport-wide service standards to encourage all staff to understand the importance of customer service matters
- The introduction of an airport-wide service recognition program for staff
- An airport-wide induction program for new staff
- Improved systems to report cleaning and maintenance issues.

Collaborative service level commitments

Since 2008, Sydney Airport has been developing collaborative service level commitments with a number of airlines. These are joint initiatives developed with individual airlines with the objective of jointly delivering a high service standard appropriate to the priorities of each airline and its passengers.

So far, service level commitments have been agreed with Qantas, Air New Zealand and Virgin Blue. Discussions for service level commitments are currently underway with Singapore Airlines, United Airlines, Cathay Pacific, Emirates and AirCalin.

The program involves both Sydney Airport and each participating airline recognising that:
- The terminals (T1 and T2) are multi-user facilities and that their efficient operation requires the cooperation of all users
- The airport and airlines are delivering a joint product to passengers
- Different airlines and their passengers have different priorities.

The program identifies processes relating to international passenger services and defines the scope of those services, sets targets or goals for providing these services and proposes measurements for reporting and reviewing the services.

The program includes service commitments and reporting by both parties to the agreement. Success requires a collective effort. The program is passenger oriented and is transparent, consultative, mutually agreed and measurable.

The processes are monitored regularly and monthly reports are provided to the Service Level Working Group which is composed of representatives of the airlines and Sydney Airport management. The program typically involves the following regular steps:
- Data collection and monthly reporting and review of achievement of targets by the Working Group
- Follow up and problem identification by Working Group members in relation to events as they arise on a daily basis
- Development of responses and solutions by the Working Group in relation to negative performance against service level targets
- Quarterly reporting by the Working Group to a Sydney Airport management and the Airline Operating Committee (AOC) or a designated airline representative
- Development of solutions by the Steering Committee or a designated airline representative to issues that cannot be resolved by the Working Group
- Escalation of any outstanding issues to the CEO of Sydney Airport and the nominated airline senior representative.

The service level commitment program does not have an adversarial tone and is structured around airlines and Sydney Airport working together to develop solutions and improve common goals. Its success demonstrates that Sydney Airport and airlines can freely negotiate and agree on the service levels that are appropriate to them without the intervention of third party regulators. It is a flexible tool that can respond to the particular requirements of airlines, noting that competing airlines, whether full service or low cost, will have some common requirements and some areas of product differentiation. The flexibility is important, and one of the service level commitments has recently been updated to incorporate a new priority which had been identified by the airline. The ability of airlines to negotiate service monitoring programs with airports that reflect these wider corporate competitive strategies is important and should be encouraged.

Finally, it is noted that the service level commitments also typically agree on the form of monitoring and reporting that is appropriate to each airline. It is relevant information reflective of the airline and airport's needs that is produced in a timely manner. Again, this

monitoring and reporting is negotiated between the airport and the airline on a normal business to business basis without the intervention of third party regulators.

These are innovative instruments that show the willingness and the ability of Sydney Airport to negotiate service commitments that are tailored to the specific requirements of an individual airline.

4.9 Financial performance

Airlines and passengers at Sydney Airport have received good value for money since the commencement of the current regulatory regime in 2002. Sydney Airport has earned, at best, a reasonable return on capital considering the commercial risks and underlying prices have generally increased more slowly than inflation.

Returns have been reasonable

The cost of capital represents the minimum return that investors need to expect to achieve over the long term, allowing for risks, if they are to continue investing. Achieved returns on individual investments and in individual years will vary from the cost of capital – sometimes being higher and sometimes lower.

To date, Sydney Airport's return on capital has been below its cost of capital since privatisation. The pre-tax real Weighted Average Cost of Capital (WACCs) agreed with the airlines since privatisation have varied between 7.7% and 9.5%, and a pre-tax nominal WACC of 12-12.5% was suggested in a recent broker report[34] on the ACCC Monitoring report for 2009/10.

Assessing Sydney Airport's financial performance from the ACCC Airport Monitoring Reports is made more difficult both by the changes in the reporting methodology following the Productivity Commission review in 2006 and by the expiry of the ACCC's May 2001 pricing decision. Nevertheless, the only conclusion that can be drawn from the ACCC Monitoring Reports is that Sydney Airport is not earning excessive returns. This conclusion is supported/demonstrated as follows:

2002/3 – 2005/6. As Sydney Airport presented in its submission to the 2006 Productivity Commission Review, aeronautical revenues (excluding NNI[35]) from 1 July 2002 to 30 June 2006 were $35 million below the forecast allowable revenues (which excluded NNI) in the ACCC's pricing decision of May 2001[36].

2006/7. In 2006/7 the reported pre-tax nominal return in the ACCC Monitoring Report was 7.6%[37]. Although this report preceded the use of the 'line-in-the-sand', the reported

[34] Macquarie Equities Research, 9 February 2011, "MAp Airports. ACCC – another criticism of Sydney".
[35] NNI refers to Necessary New Investments. The ACCC pricing decision of May 2001 set charges for Sydney Airport based on forecast costs (including capital costs) which excluded any capital expenditure to provide additional capacity or increase service quality. Any NNI capital expenditure was to be remunerated by a separate charge.
[36] Sydney Airport Submission to the Productivity Commission, Inquiry into Price Regulation of Airport Services, 21 July 2006, page 15
[37] Average pre-tax nominal return on capital refers to the EBITA on average tangible non-current assets for aeronautical services

accounting return was only 0.2% lower than the 'line-in-the-sand' return in the 2007/8 report (and was higher in both 2008/9 and 2009/10).

2007/8, 2008/09, and 2009/10. Sydney Airport's average pre-tax nominal return on capital for aeronautical services over this period using the 'line-in-the-sand' methodology was 8.1%; being 8.6% in 2007/8[38], 8.0% in 2008/9 and 7.8% in 2009/10. These returns include an under-recovery of Necessary New Investment of $4.2 million due to lower passenger volumes than forecast between July 2007 and December 2010[39].

The commercial agreements with the airlines use a pricing methodology which is not consistent with the returns reported above. Specifically, the commercial agreements:

- Use a real cost of capital, applied to an inflation-indexed asset base
- Use the 'line-in-the-sand' methodology, adjusted to include the landfill[40] (as a 'discovered' asset) which was erroneously excluded from the 'line-in-the-sand', and to reflect the non-land asset valuations determined by the ACCC in 2001.

Underlying price increases have been broadly in line with inflation

In May 2001, the ACCC approved new charges for Sydney Airport that reflected the ACCC's view on the actual costs of operating Sydney Airport. The costs and, hence, the charges will have reflected the particular characteristics of Sydney Airport compared with other major Australian airports, such as:

- A higher proportion of long-haul international passengers. These passengers typically use more facilities of the airport than domestic or short-haul international passengers. For example, they are likely to travel with more baggage and to spend more time inside the terminal.
- A higher proportion of transfer and transit passengers. This results in a need for more complex baggage handling infrastructure
- Operational regulations at Sydney Airport that drive traffic volumes in peak periods and increase average aircraft sizes
- A location within Australia's most expensive city, reflected in both the value of the land and in the costs of labour and other inputs
- A relatively small and congested site compared to some major airports, which increases the costs of construction. The $100 million construction cost for the RESA at the Western end of the cross-runway (which had to be built over a canal, road tunnels and other utility infrastructure) is a recent example – the construction cost for the other five RESAs was a total of $3 million.
- Three separate terminals in two distinct terminal precincts, which results in the duplication of some facilities and costs of transfers between the terminal precincts.

[38] ACCC issued correction to the Airport Monitoring Report 2007-08 for returns on assets for Sydney Airport. The reported EBITA on average tangible non-current assets for aeronautical services under the 'line-in-the-sand' was reported as 9.2% on page 213, but later corrected to 8.6%. The version accessed 4 April 2011 on the ACCC website remains uncorrected, but a correction to Chapter 8 is noted separately http://www.accc.gov.au/content/index.phtml/itemId/865718

[39] Additional information Appendix B – Historical aeronautical charges, NNI passenger volume risk

[40] The landfill assets were erroneously excluded from the airport's asset base in 1998 through the approach taken to accounting for land assets. This error was identified and corrected as part of the transition to A-IFRS accounting standards; however was not part of the asset base from which the line-in-the sand asset base was derived.

From 2001/2 to 2009/10 underlying revenues per passenger at Sydney Airport[41] have generally increased more slowly than inflation (see Appendix B):

International: CPI+0.4%
Domestic: CPI-1.4%
Regional: CPI-4.9% (despite increased security and safety requirements)
T2 domestic: CPI-2.5% (from 2003/4), reflecting the 17 year commercial agreements.

The evolution of the charges reflects the impact of various factors including inflation (on asset values and operating costs), the recovery of $1.2 billion of new aeronautical investments (between July 2002 and June 2010) and increased operating costs arising from increased traffic volumes – offset by the increased traffic.

Headline charges have increased slightly faster than this[42], as a result of:

- New security and mandated safety regulations
- New services, such as GPPCA and CUTE. In both of these cases, the airport is providing a new service which is replacing an activity previously undertaken directly by the airlines. The overall cost to the airlines has been reduced, even though the airport charges have been increased. The shifting of these costs therefore improved overall economic efficiency.

It should be noted that Sydney Airport's charges are not applied to international-to-international transfer and transit passengers. These passengers are neither charged nor reported but represent 10% of total international passengers using the airport. The charge per passenger is therefore overstated compared to many benchmark airports. Similarly, charges include a range of services such as express path facilities and other services for premium passengers, passenger and crew airside bussing, airline signage and way finding, airfield lighting and aircraft guidance systems – many of which would not be included within aeronautical charges at other airports.

Sydney Airport's strategic shareholders – MAp Airports and HOCHTIEF AirPort[43]– have in the past participated in several benchmarking exercises with other airports. Whilst at a detailed level, the airports have been able to identify specific opportunities; all attempts to draw conclusions at high levels have failed due to the substantial differences between the airports. Furthermore, identification of and agreement on benchmarks is made difficult by large fluctuations in exchange rates – which would, for example, make Australian airports appear significantly more expensive than they did only a few years ago for no reason other than the appreciation of the Australian dollar.

4.10 Conclusions

Under light-handed regulation, Sydney Airport has delivered commercial agreements with all international and domestic airlines, including individualised multi-faceted agreements for

[41] Excluding charges relating to government mandated security and safety projects, and charges related to the transference of airline direct costs to airport charges (GPPCA and CUTE). Includes all charges related to other investments including all capacity-related projects, and all commercial agreements. CPI used is ABS All Groups, Sydney.
[42] Appendix B, History of aeronautical charges , provides more details on the actual charges
[43] MAp Airports have investments in Copenhagen and Brussels airports; HOCHTIEF AirPort Concessions (including associate company HTAC) have investments including Dusseldorf, Budapest and Athens airports.

many airlines, continuing investment, made improvements in service quality resulting from a range of initiatives, and offers stable and reasonable charges.

There are adequate dispute resolution procedures and deterrents to the misuse of market power and that 'binding arbitration' undermines the objects of light-handed regulations.

Sydney Airport continues to extensively consult its airline customers on the timing and nature of new capital investments and on the evidence presented did not delay the upgrade of the international terminal.

Sydney Airport financial returns have been reasonable, with underlying price increases broadly in line with inflation.

On evidence presented none of these factors are consistent with the exercise of market power for the supply of aeronautical services.

5. Land transport

Key points

- Land use and transport planning by the Commonwealth, State and local governments needs to respond to the scale and importance of the users of Sydney Airport and their importance to community and economic welfare.
- The existing land transport linkages to Sydney Airport need significant improvement, in particular:
  - The rail service to the airport is expensive with inadequate luggage facilities
  - A single public bus route to the airport fails to meet passenger demand
  - Road investment should reflect potential returns from reduced congestion to commercial and commuting traffic.
- Sydney Airport shares the use of the surrounding land transport infrastructure and services with Port Botany (which is located approximately 5 km to the east of Sydney Airport) and commuters, including many travelling past the airport's boundary to the Sydney CBD. In common with Sydney Airport, Port Botany underpins much growth and prosperity for both the state and the nation.
- The NSW Government is responsible to travellers and tourism and other businesses for providing land transport infrastructure to Sydney Airport and Port Botany.
- Sydney Airport recommends that:
  - The NSW Government prepare a Land Transport Access Plan in consultation with the community and other key stakeholders (including Sydney Airport). Given Sydney Airport's proximity to Port Botany, the Land Transport Access Plan for Sydney should address both airport and port-related access needs.
  - In NSW's case, the Land Transport Access Plan should include a commitment to remove the station access fee from the Domestic and International rail stations on the Airport Link as has just been accomplished for Green Square and Mascot stations.
  - Infrastructure Australia has an important role in the development of Land Transport Access Plans.

5.1 Importance of land transport links

Australia's air transport infrastructure and services connect people and businesses regionally, nationally and internationally. This is why Australia's major airports – including Sydney – generate significant economic activity and employment in our cities.

However, for a city to be economically efficient, people and businesses within that city also need to be able to easily interact with each other. The ease with which this occurs will, in large measure, depend on the quality and effectiveness of the land transport infrastructure and services provided by governments to connect people and businesses. A city's economic efficiency will be undermined by ineffective land transport infrastructure or services even if it is well served by high quality and efficient air transport infrastructure and services – limiting its ability to generate productivity growth.

For these reasons, and given the significant economic activity and employment generated by Australia's aviation industry, the provision and quality of land transport facilities providing access to major capital city airports is an important productivity-related issue which, for the first time, the Productivity Commission has an opportunity to examine.

As will be shown, the existing land transport linkages to Sydney Airport need significant improvement. More effective road and public transport linkages to the airport will improve the efficiency of airport operations, boost productivity and achieve positive environmental and community outcomes. The *Master Plan 2009* states that Sydney Airport is committed to increasing the public transport mode share by 5% by 2024.[44] This can only occur if more effective public transport linkages are provided. Provision of such links is the responsibility of the NSW Government, not Sydney Airport.

Historically, government planning for and delivery of land transport infrastructure and public transport services at Sydney Airport has been sporadic, with inconsistent priorities and major gaps in delivery. Some supply and pricing decisions have also failed to take account of wider community interests and, in one case, has been anti-competitive.

5.2 Economic importance of Sydney Airport and Port Botany

The NSW Government's *Metropolitan Plan for Sydney 2036* (the Metropolitan Plan) identifies Sydney Airport as being a part of the Global Economic Corridor, which stretches from Macquarie Park in the north, through Chatswood, North Sydney, the Sydney CBD, Green Square to Sydney Airport and Port Botany in the south. The NSW Government states that the Corridor '…will remain the powerhouse of Australia's economy'"[45]

Sydney Airport's direct and indirect contribution to the NSW economy is $16.5 billion per year and is forecast to rise to more than $27 billion by 2015/16 (see Section 3). This is equivalent to 6% of the NSW economy and 2% of the Australian economy. This economic activity generates substantial tax revenues to governments including corporate, income, payroll and GST.

This substantial economic contribution translates into well paid jobs. It is estimated that Sydney Airport provides or generates more than 75,000 jobs directly and about 131,000 jobs indirectly, making a total of around 206,000 jobs. Airport-related employment is expected to increase to more than 338,000 jobs by 2015/16[46]. These jobs are estimated to deliver around $286 million in payroll tax revenue to the NSW Government in 2010/11.

Sydney Airport is also the largest transport interchange in NSW. In 2010, it handled a daily average of around 140,000 passengers, meeters and greeters, and staff. , This throughput makes Sydney Airport significantly busier than Central Station – CityRail's busiest passenger station (see Appendix C, table 3.1). People accessing Sydney Airport use a variety of public and private transport modes including train, taxis, bus and shuttle bus services, limousine services, rental cars, private coaches, airport and off-airport parking, and private vehicle pick-ups and drop-offs. It is this interchange of people which underpins the economic benefits.

[44] Sydney Airport *Master Plan 2009*, page 89.
[45] See *Metropolitan Plan for Sydney 2036*, NSW Government, December 2010, page 18.
[46] The Economic Impact of Growth at Sydney Airport – Report prepared by URS Australia Pty Ltd – 9 January 2008.

The land transport access task will grow as the number of airline passengers grows, noting that the *Master Plan 2009* forecasts the airport reaching 78.9 million passengers in 2029. While no forecast is available for meeter/greeters or airport workers, total throughput in 2029 at Sydney Airport will, at around 250,000 passengers per day, likely exceed the combined 2010 throughput of CiytRail's five largest stations.

Sydney Airport shares the use of the surrounding land transport infrastructure and services with Port Botany (which is located approximately 5 km to the east of Sydney Airport) and commuters – including many travelling past the airport's boundary to the Sydney CBD. In common with Sydney Airport, Port Botany underpins much growth and prosperity for both the state and the nation. The port handles about one-third of Australia's container trade, worth about $50 billion each year, and directly or indirectly employs 10,000 people in port-related industries. It is forecast that trade through the port will double over the next 10-15 years.

Growth in demand for the use of the land transport will therefore be generated by the increased activity at Sydney Airport, substantial growth at Port Botany and increased commuter travel. This will occur even if Sydney Ports Corporation meets the NSW Government's target to double the proportion of containers carried by rail to and from the port from 20% to 40%.

Achieving the forecast growth in jobs and economic activity at the airport and port will clearly rely on the quality and effectiveness of the land transport linkages provided to access both. Hence the primary beneficiary from providing land transport infrastructure to Sydney Airport, Port Botany and to the Sydney metropolitan area more generally is the NSW Government. The primary responsibility to provide these linkages lies with the NSW Government.

As was stated in a report prepared by Booz & Co. for the Tourism & Transport Forum (TTF):

In the past, the (false) perception was often that any state/territory government investment in land transport infrastructure - directly or indirectly related to airports - supported the airports' commercial interests. However, this class of land transport investment by state/territory government should be focused on supporting or facilitating the economic benefits associated with airport activity, as they accrue to the state/ territory as a whole. [47]

Infrastructure Australia also considered the responsibility for land transport infrastructure provision and reached the same conclusion. [48] It described the responsibilities for the various types of such infrastructure in Australia as follows:

[47] *Accessing Our Airports: Integrating city transport planning with growing air services demand,* prepared by Booz & Co. for TTF, April 2011, page 6

[48] Infrastructure Australia, *A Report to the Council of Australian Governments*, December 2008 pages 12, 13.

Level of Government	Economic infrastructure
Commonwealth	Railways (shared) Roads (national, local) (shared)
State	Railways (shared) Roads (urban, rural, local) (shared) Public transport
Local	Roads (local) (shared)

It is pleasing to note that the Australian Government, through Infrastructure Australia, is playing an increasingly active role in land transport-related issues, both in terms of planning and funding.

It should be noted that Airport Drive/Qantas Drive, which forms the northern boundary of the Airport, is located on airport land. This road is maintained by Sydney Airport and forms an important element of the southern Sydney arterial road network, which is used on a daily basis by large numbers of non-airport vehicles. Sydney Airport is also responsible for the construction and maintenance of all roads within the airport's boundaries, with maintenance and operating costs of landside roads recovered from non-aeronautical activities.

5.3 Sydney Airport is poorly served by public transport

Land transport access to Sydney Airport (including by public transport) is required for a number of specific market segments, each of which has its own set of requirements that will determine the current and future preferred mode of travel. These market segments include:

- **Passengers**: a group with diverse needs depending on factors including the purpose of travel, the time of travel, the mobility of the passengers, the number of passengers travelling together and the amount of luggage carried
- **On-airport employees**: need travel modes to cater to both 'normal business hours' and shift workers
- **Meeters and greeters**: includes those who spend time inside the terminals with the passengers travelling, as well as others who leave/welcome the passengers in the forecourt
- **Suppliers**: including many small businesses, who need timely and reliable access to customers at Sydney Airport.

To serve all these user groups, a holistic approach to transport planning is needed.

The fact that Sydney Airport is located so conveniently to the Sydney CBD (approximately 8km to the north), to motorways (such as the M4, M5 East and Eastern Distributor) and to Sydney's CityRail network should, in theory at least, result in land transport access to the airport being of a high standard.

However, this is not the case. The existing land transport infrastructure and public transport services provided by the NSW Government to access Sydney Airport are either non-existent, inadequate or too expensive for many users. For example:

- Train fares are overly expensive for many users, and the carriages have inadequate luggage storage for airport passengers
- There is inadequate bus access – there is only one government bus route to the airport
- There is congestion on the surrounding arterial roads, particularly during peak hours when the roads are being used heavily by urban commuters (travelling past the airport) as well as by vehicles accessing Port Botany.

The poor quality of public transport services provided to access Sydney Airport contrast sharply with those provided by the NSW Government to support major or special events elsewhere in Sydney. For example:

NRL Grand Final, Stadium Australia (82,000 spectators) – additional bus and train services
Ashes Test, Sydney Cricket Ground (36,000 spectators per day) – additional bus services
Large concerts at Entertainment Centre – special bus and train services.

Sydney Airport, with an average of 140,000 users per day, has only one bus service (and no 'special event additional services') and an expensive train service.

Rail services need to be cheaper, more frequent and traveller-friendly

The two train stations at Sydney Airport's Domestic and International Terminals are on CityRail's Airport & East Hills Line. The rail tunnel that connects the Sydney CBD and Sydney Airport to this line was built between 1995 and 2000 as a joint venture between the NSW Government, which built the line and operates the trains, and Airport Link, a private company which built and owns the stations serving the domestic and international terminals[49]. As part of its agreement with the NSW Government, Airport Link charges a 'station access fee' on top of the normal CityRail fare. This makes accessing Sydney Airport by train overly expensive for many users. Normal commuter trains are used so carriages have inadequate luggage storage room, making them difficult and inconvenient to use for many travellers.

There will also be a need over time to increase the frequency of trains as the number of passengers and on-airport employees travelling to and from Sydney Airport by train increases. These increases will arise naturally from the growth of airport activity, but would be substantially accelerated if improvements to rail fares and luggage facilities were made. For this reason, Sydney Airport supports the continued implementation of the NSW Government's 'Clearways' program, which aims to facilitate growth in rail patronage on the Airport & East Hills line (and other lines) by allowing for an increase in the number of train services. During the preparation of the *Master Plan 2009*, consultations between Sydney Airport and the NSW Government indicated that the number of rail services to the airport could, over time, increase from 12 to at least 20 trains per hour in each direction.

However, the largest barrier to increased rail usage by passengers and on-airport employees is the high cost of the total fare. The total fare paid by passengers is made up of the 'station access fee', which is set by Airport Link and is not subject to regulation by the NSW Independent Pricing and Regulatory Tribunal (IPART), and the standard CityRail fare. The 'station access fee' is paid by rail passengers using the Domestic and International stations at Sydney Airport and is currently $11.80 per adult. The 'station access fee' paid by passengers who use the other two Airport Link stations at Green Square or Mascot was, until recently,

[49] Airport Link also owns Mascot and Green Square stations which, like the stations at Sydney Airport, are located within the Global Economic Corridor.

only $2.60. However, following an agreement reached between Airport Link and the NSW Government, the 'station access fee' to use these two stations was abolished on 7 March 2011.

As a result, there are now only two train stations in NSW where passengers have to pay a surcharge to catch the train – the ones at Sydney Airport's Domestic and International terminals. There is no public policy reason why workers at the airport are now the only commuters in NSW who have to pay a surcharge for using public transport to get to work. It is notable that no 'station access fee' is charged to users of the three recently opened stations on the Epping to Chatswood rail link, nor is there any plan to charge a station access fee on the planned Parramatta – Epping line that is to be partially funded by the Australian Government.

As the charts in Appendix C (sections 3.2 and 3.3) illustrate, the rail fares to Sydney Airport are at odds with the rest of the CityRail network, for example:

- From Central Station, for a 'standard ticket' it is cheaper to travel to distant regional centres such as Bathurst (231km), Goulburn (217km), Newcastle (161km) or Bomaderry/Nowra (153km) than it is to travel the mere 8km to Sydney Airport
- The fare paid to travel to Sydney Airport ($15) is almost five times higher than the fare paid ($3.20) to travel to Ashfield, Bondi Junction and St Leonards – which are, on average, the same distance from Central Station.

The cost of the 'station access fee' is a particularly important issue for on-airport employees because they are more likely to want to purchase multitrip tickets. Whilst the cost of weekly access per trip is cheaper than adult singles, the annual cost of the 'station access fee' still adds almost $1000 to the normal CityRail fare. As a result, on-airport employees are actively *discouraged* from travelling to work by public transport. They are, in fact, encouraged to drive, worsening both congestion on the road network around Sydney Airport and Port Botany and environmental quality.

The impact of rail fares on rail usage generally has been investigated by IPART which noted that:

…there is a negative relationship between demand for CityRail services and the level of CityRail fares (eg, demand tends to come down as fares go up)….. a 10% increase in fares would be associated with a fall in patronage of around 2-3% (all other factors being equal).

It is likely, therefore, that a 10% reduction in fares would increase use of rail by around 2-3%. If rail fares were to decrease, rail patronage should increase.

The impact on rail patronage of the 'station access fee' would be much larger however, because the 'station access fee' is such a significant part of the overall fare: it increases the ticket price from Central Station to Sydney Airport from $3.20 to $15.00. Booz & Co estimated that if the 'station access fee' were removed and the rail fares aligned with normal CityRail fares, then rail usage to Sydney Airport would jump by 23%. Table 3.4 in Appendix C shows how rail patronage would progressively increase over the next 20 years. The full Booz & Co. report is also included at Annexure 4 (section 4.5).

Reforming the fare structure for users of the two Airport Link stations at Sydney Airport by equalising its fares with normal CityRail fares should therefore be a high priority because it will:

- Quickly increase the number of people travelling to and from Sydney Airport by train
- Result in the more efficient use of existing rail infrastructure: existing infrastructure should be efficiently maximised ahead of investing extra sums of capital to new infrastructure projects with long lead times
- Help to alleviate existing (and future) traffic congestion on roads such as the M5 East Motorway, reduce greenhouse emissions and improve local air quality.

However, it is not only the 'station access fee' that is discouraging people from using the train to access Sydney Airport. Since 1995, the NSW Government's Cashback scheme has reimbursed motorists for the toll paid on the M5 Motorway.[50] As this motorway is within the same transport corridor as the Airport & East Hills line, this road subsidy further discourages rail travel to Sydney Airport and elsewhere. The NSW Government expects to pay 600,000 Cashback claims in 2010/11 at a cost of $85 million.[51] After deducting an estimate for the cost of the now redundant M4 component of the Cashback scheme[52], it is reasonable to assume that the NSW Government is subsidising the use of the M5 by around $60 million per annum. This compares to the estimated $40 million per annum it would cost to abolish the station access fee for users of the two on-airport stations.[53] From a public policy perspective, it makes little or no sense to be discouraging rail travel and encouraging car travel in this manner.

Rail can often provide the most reliable form of access to an airport – and does so at many airports overseas. Providing effective and economical rail access for passengers is therefore particularly important for airports where, at times, the surrounding road network is congested This is because it reduces the need for the passenger to make a large time provision for the uncertainty of the road congestion. For this reason, it is also common for airport rail links to be 'express', recognising the importance of time to travellers. To make rail the preferred option of passengers, it is also important for the luggage facilities on the trains to reflect the amount of luggage carried by airport passengers.

<u>More bus services are needed to serve Sydney Airport</u>

Currently, 11.4% of all trips by residents in the East sub-region of Sydney are made by bus. In comparison, only 2% of airline passengers and 7% of on-airport employees travel by public bus to or from Sydney Airport.

The reason why so few airline passengers and airport workers travel to and from Sydney Airport by bus is simple – there is only <u>one</u> public bus route (Route 400) which stops at any of the airport's passenger terminals.

The major urban centres shown in the table in Appendix C (section 3.5) are a sample of those identified by the NSW Government in its *Metropolitan Plan* as 'strategic centres' many of which, like Sydney Airport, are located in the Global Economic Corridor. There is an obvious contrast between the large numbers of bus services provided to these urban centres –

[50] Until 16 February 2010, the Cash back scheme also applied to motorists using the M4 Motorway. The toll ended on that date.
[51] See 2010/11 NSW Budget Estimates, Budget Paper 3 (Transport & Infrastructure), page 13-26.
[52] While the toll to use the M4 Motorway ended on 16 February 2010, motorists were able to claim the cost of any tolls paid prior to that date for a limited period after the abolition of the toll.
[53] $40 million is the estimate made by the NSW Premier in response to media questions when she announced that the station access fee would be abolished for users of the Green Square and Mascot stations.

some of which are small compared to Sydney Airport – and the single bus service provided to Sydney Airport's terminals.

Further, as shown in the diagram in Appendix C (section 3.6), other major airports in Britain are also far better served than Sydney, for example:

- Heathrow Airport is served by 29 bus routes stopping at its passenger terminals for 183,000 passengers per day and 72,000 on-airport workers
- Gatwick Airport is served by five bus routes stopping at its passenger terminals for 90,000 passengers per day and 23,000 on-airport workers
- Manchester Airport is served by eight bus routes stopping at its passenger terminals for 60,000 passengers per day and 19,000 on-airport workers

Sydney Airport notes that, as long ago as November 2003, new strategic bus corridors were considered by the NSW Government. It is estimated that around 34% of on-airport workers live in the St George – Sutherland area. Two of the then proposed new corridors would provide a direct link between Sydney Airport and this area. Sydney Airport has recommended to the NSW Government on numerous occasions that actual bus services should be provided in these corridors as soon as possible. However, to date, this has not occurred.

The NSW Government's new Metrobus services are intended to provide high-frequency, high-capacity links between key employment and growth centres across Sydney. Characterised by cross regional routes, Sydney Airport supported their introduction. The recent introduction of the new Metrobus Route 20 service therefore provided a major opportunity to improve bus access to Sydney Airport which, as has been demonstrated, is an employment and growth centre in Sydney.

In March 2009, the NSW Government announced that Sydney Buses would commence a new Metrobus service (Route M20) which would operate from Lane Cove through the CBD and then on to Mascot (suburb) – clearly an important new bus route servicing the Global Economic Corridor. Sydney Airport entered into negotiations with Sydney Buses seeking to have the route extended by a kilometre to stop at the airport's Domestic Terminals and made it clear that it would fund and provide any additional road and kerbside infrastructure that was required to allow this to happen. However, negotiations collapsed and the route change was rejected by Sydney Buses.

Similarly, the M30 bus service, which originates in Mosman, also travels through the Sydney CBD to terminate at Sydenham Station, only 1.5 km from Sydney Airport.

The map shown in Appendix C (section 3.7) shows that extending these two bus routes a very short distance to the passenger terminals would be a simple obvious way to improve public transport access to Sydney Airport.

The stumbling block appears to be the commercial agreement entered into between the then Airport Rail Link company and the NSW Government. It states, in part, that certain 'material events' can trigger a process which ultimately may see the agreement terminated and, presumably, the possibility that compensation would need to be paid. Two of the 'material events' relate to any decision made by a State or Commonwealth body to:

- Develop or substantially upgrade or grant a concession for another person to develop or substantially upgrade an alternative subsidised land based public transport route between

the CBD and the Airport (other than a route for motor traffic or car parking at or near the Airport); or

— Take actions relating to servicing the transport or commuting needs of the public along or around the Airport Line which discriminate against ALC in its operation of the Stations.

A decision to extend these bus routes to Sydney Airport's terminals, where Airport Link stations are also located, may have been seen by the Government as a possible 'material event'. The loss of this easy opportunity to improve bus access to Sydney Airport is deeply frustrating and disappointing and represents a clear loss of economic efficiency and welfare.

This example clearly demonstrates how the existing framework used by the NSW Government to make transport planning and related operational decisions affecting Sydney Airport can produce poor quality land transport and environmental outcomes.

Competition is being reduced because of the abovementioned contractual provisions and, as a direct result, of the 140,000 people who need to access Sydney Airport every day, only a person who lives on or near the 400 bus route can choose to travel conveniently to the airport by public bus. If they find the train too expensive (as many airport workers in particular do), they have no choice than to drive or be driven by someone else. This, of course, results in more cars on the road network generally and exacerbates congestion on the road network surrounding Sydney Airport and Port Botany in particular. This congestion is especially apparent during the morning and evening peak periods, when the daily peak in aviation activity coincides with the metropolitan-wide peak in commuter traffic. Port-related container truck movements are also caught up in this congestion, thus eroding productivity at the port and adding to costs.

It recommended that the Productivity Commission enunciate principles to guide governments in relation to land transport around Sydney Airport and Port Botany to ensure that wider community benefits are properly taken into account. Economic efficiency would be promoted if State and Territory Governments could not enter into agreements that restrict competition between the various modes of land transport used to access capital city airports. As with the recommendation to prepare Land Transport Access Plans, this could be achieved as part of the *National Urban Policy*. The importance of this issue would be made clearer if the Productivity Commission were able to estimate the benefits of welfare gains achieved if anti-competitive restraints on land transport were removed.

5.4 Road infrastructure also needs to be expanded

There are essentially three main types of traffic that are evident on the road network in and around Sydney Airport. These are:

— Trucks travelling to or from the Port Botany Container Terminal (which carry freight)

— Trucks and cars that are directly associated with the day-to-day operation of Sydney Airport (which carry passengers, meeter/greeters/farewellers, freight, in-flight catering, aircraft maintenance, terminal transfer buses and other airport workers)

— Commuter and small business traffic that passes through or around the airport.

Currently, these three types of road traffic all tend to converge at the airport itself, especially during the morning and afternoon peaks, thus causing traffic congestion.

Currently, the M5 East Motorway, Eastern Distributor, Southern Cross Drive, General Holmes Drive and O'Riordan Street are the main vehicular access routes to Sydney Airport. Arterial road access to the International precinct is provided by Airport Drive, Marsh Street and to the Domestic Precinct by the Qantas Drive/Joyce Drive/O'Riordan Street intersection.

Airport Drive/Qantas Drive – which forms the northern boundary of the Airport, is located on airport land and is maintained by Sydney Airport – forms an important element of the southern Sydney arterial road network and is used by large numbers of non-airport vehicles. According to the latest RTA data for 2006 provided by the RTA to Sydney Airport, an average of more than 53,000 vehicles use Qantas Drive and Airport Drive per day, including 2,580 during the peak morning hour. In conjunction with the provision of airport road user access within the passenger terminal precincts themselves, Sydney Airport is committed to maintaining public access to Airport Drive/Qantas Drive.

Over the last 20 years, road infrastructure around Sydney and to Port Botany, Sydney Airport and the surrounding areas has been significantly improved by a number of important projects undertaken by the NSW Government. These include the M4 Western Motorway (1992), the Sydney Harbour Tunnel (1992), the M5 South West Motorway (1992), the M2 (1997), the Eastern Distributor (1999), the M5 East (2001), Cross City Tunnel (2005), Westlink M7 (2005), and the Lane Cove Tunnel (2007). These nine major pieces of road infrastructure were all undertaken by the NSW Government in line with its established constitutional responsibilities and it is to be commended for doing so.

Sydney Airport believes, however, that there are two other critically important and necessary road projects that need to be progressed – the M5 East Duplication and the M4 East Extension – together with the associated road way that would connect the M5 East to the M4 East.

The need for the M5 East and M4 East projects has already been recognised by the NSW Government. In 2008, the *State Infrastructure Strategy* indicated that the NSW Government is continuing to plan for the M4 East and M5 East corridor. Sydney Airport considers that the M4 East (which will improve road access from western and north-western Sydney to Port Botany and Sydney Airport) and the M5 East Duplication and associated road connection to the M4 East (which will improve road access from south-western Sydney to Port Botany and Sydney Airport) are both necessary to support economic and employment growth in the Global Economic Corridor, including growth associated with the expansion of the Port Botany Container Terminal and forecast growth in aviation activity at Sydney Airport.

The Australian Government also explicitly recognised the need to expand the M5 East when it announced that it:

…will also have Infrastructure Australia work with the NSW Government to explore private financing options for the M5 East widening …. The M5 corridor is the main freight, commercial and passenger route between Port Botany, Sydney Airport, and south west Sydney. The M5 East tunnel carries some 95,000 vehicles per day, with congestion issues impacting heavily on Sydney's economic productivity and competitiveness. It is clear that the

M5 needs widening and [the Gillard Government] will make available the expertise of Infrastructure Australia to progress this project. [54]

It is understood this process is underway. Sydney Airport will participate fully in planning and implementation as appropriate.

5.5 The way forward – a Land Transport Access Plan for Sydney Airport and Port Botany

This section proposes recommendations that, if adopted by the Commission and implemented by governments, would improve the effectiveness of the existing arrangements for the planning and operation of land transport linkages to Sydney Airport.

Airport Ground Travel Plan and Master Plan 2009

Sydney Airport has long argued that land transport access to the airport needs to be improved. With the publication of the *Airport Ground Travel Plan* (AGTP) in 2006, Sydney Airport demonstrated its commitment to exploring innovative ways to improve the sustainable transport options for passengers, airport staff and visitors travelling to and from Sydney Airport.

The existing transport mode share proportions for accessing Sydney Airport are shown in Appendix C (section 3.8). The AGTP and Sydney Airport's *Master Plan 2009* state that Sydney Airport is committed to increasing the public transport mode share by 5% by 2024.[55]

The *Metropolitan Plan for Sydney 2036*

The Metropolitan Plan is the NSW Government's key strategic plan for the Sydney metropolitan area, and builds on the Government's companion *Metropolitan Transport Plan* and its *...10 year funding guarantee.* [56]

While the adoption of a Metropolitan Plan is a welcome initiative to integrate land use and transport planning across Sydney, vitally necessary land transport facilities and initiatives in the vicinity of Sydney Airport and Port Botany – some of which would be relatively simple and inexpensive to provide – have not been funded through the *Metropolitan Transport Plan*. This is regrettable. As the NSW Government acknowledged in a June 2008 submission to Infrastructure Australia:

... [i]f the transport network around the Airport and Port Botany is not improved, congestion will limit the level of economic benefits generated from these two precincts with negative ramifications for the NSW economy and the national economy.

As noted above, the Metropolitan Plan identifies Sydney Airport as being a part of the Global Economic Corridor and it further designates 'Sydney Airport and environs' and 'Port Botany

[54] See "Infrastructure investment to move Sydney forward", media release issued by the Hon. Julia Gillard MP, Prime Minister, and the Hon. Anthony Albanese MP, Minister for Infrastructure and Transport on 11 August 2010.
[55] Sydney Airport *Master Plan 2009*, page 89.
[56] *Metropolitan Transport Plan: Connecting the City of Cities*, NSW Government, February 2010. The 10 year funding guarantee appears on pages 28 – 44.

and environs' as Specialised Centres, forecasting the creation of an additional 22,000 and 7,000 jobs in these centres respectively by 2036. The employment growth resulting from increased aviation activity at Sydney Airport outlined above will contribute significantly to the meeting of these targets.[57]

Recognising that ...*Sydney Airport will continue to serve as Sydney's major airport and Australia's major international gateway*[58], the Metropolitan Plan identifies a need to *build capacity and support economic growth in and around Sydney Airport.* [59] However, little or no detail is given concerning what supporting land transport infrastructure and services will be provided to facilitate this outcome. The only indication is that:

Transport NSW will work with the Department of Planning to prepare an Access Plan for Sydney Airport and Port Botany. Its key objectives will be to improve the efficiency of land transport access to Sydney Airport and Port Botany, facilitate economic investment and improve the local urban environment.[60]

This simply restates a commitment made to Sydney Airport almost 12 months ago. Despite recognising the importance of Sydney Airport, the NSW Government, to date, has not prepared the proposed Access Plan for Sydney Airport and Port Botany. It is hoped that work on preparing the Airport/Port Access Plan will now begin as a matter of priority. The enhancements to land transport infrastructure and public transport services proposed in this submission are recommended by Sydney Airport for inclusion in this Access Plan.

Sydney Airport believes that the role of the Australian Government in this process would be best articulated through the *National Urban Policy* process.

The *National Urban Policy*

Sydney Airport welcomes the Australian Government's decision to prepare a *National Urban Policy*, which is expected to be released in 2011. As part of this process, the Minister for Infrastructure and Transport released a Discussion Paper – *Our Cities: building a productive, sustainable and liveable future* – in 2010.

In parallel, the Council of Australian Governments (COAG) Reform Council has been asked to:

Review capital city strategic planning systems against agreed national criteria
Support continuous national improvement in capital city strategic planning
Build and share knowledge of best practice planning approaches.

COAG's nine national criteria for future strategic planning of capital cities includes the requirement to provide for nationally-significant economic infrastructure (both new and upgrade of existing) including transport corridors, international gateways and intermodal connections. Those criteria relevant to major airports are reproduced in Appendix C (section 3.9).

[57] Note that the location of these new jobs will not be confined to the 'Sydney Airport and environs' geographical area described in the Metropolitan Plan.
[58] *Metropolitan Plan for Sydney*, page 154. This view is consistent with the view of the Australian Government, which has accepted that Sydney Airport will remain Sydney's main airport.
[59] *ibid*, Action E6.2, page 154.
[60] *ibid*, page 154.

The COAG Reform Council's report on the review of capital cities strategic planning systems against these national criteria will be submitted to COAG in December 2011. COAG has also agreed that by 1 January 2012 all States will have in place plans that meet the criteria and noted that the Australian Government will link future infrastructure funding decisions to meeting these criteria.

In Sydney Airport's opinion, the *National Urban Policy* will provide an appropriate mechanism for the Australian Government to require State and Territory Governments to provide sufficient infrastructure and services to ensure an adequate level of land transport access to nationally significant economic infrastructure. This should include Australia's capital city airports. This would also promote the first of the Productivity Commission's general policy guidelines, which requires it to

...improve the overall economic performance of the economy through higher productivity in the public and private sectors in order to achieve higher living standards for all members of the Australian community.

The *Our Cities* Discussion Paper anticipates the Australian Government, through COAG, adopting a more interventionist role in this key aspect of infrastructure planning. It also states that:

Further realignment and reprioritisation of existing and planned funding for nationally significant economic infrastructure would seek to ensure that air and sea ports are well supported by connecting infrastructure.

Having regard to the Commission's consideration of the effectiveness of the planning and operation of land transport linkages to airports and ports, Sydney Airport therefore recommends that state and territory governments should be required to prepare Land Transport Access Plans for capital city airports and ports within their jurisdictions. The preparation of such plans should be undertaken in consultation with the community and other key stakeholders (including the airport and port operator) and be mandatory under the *National Urban Policy*. These Land Transport Access Plans should explicitly provide for effective implementation arrangements and supporting mechanisms, including clear accountabilities, timelines and appropriate performance measures.

In the case of Sydney Airport, this requirement would be met by the preparation of the Airport/Port Access Plan, as proposed in the NSW Government's Metropolitan Plan.

Infrastructure Australia could assist the preparation of these plans, for example by:

- Auditing the quality and effectiveness of existing land transport infrastructure and services provided by states and territories to access capital city airports.
- Identifying any gaps in the provision of such land transport infrastructure and services which, if not filled, will undermine the airport's ability to accommodate forecast growth in aviation activity.
- Ensuring Land Transport Access Plans contain the proposals necessary to upgrade land transport infrastructure and services to a sufficient standard that will allow the airport to accommodate forecast growth in aviation activity.

5.6 Recommendations

Sydney Airport recommends that:

Land use and transport planning by the Commonwealth, state and local governments needs to respond to the scale and importance of users of capital city airports. Therefore, having regard to the Commission's consideration of the effectiveness of the planning and operation of land transport linkages to airports and ports, State and Territory Governments should be required to prepare Land Transport Access Plans for capital city airports within their jurisdictions. The preparation of such plans should be undertaken in consultation with the community and other key stakeholders (including the airport) and be mandatory under the *National Urban Policy*. Given Sydney Airport's proximity to Port Botany, the Land Transport Access Plan for Sydney should address both airport and port-related access needs.

Consistent with the national criteria for future strategic planning of capital cities, Land Transport Access Plans for capital city airports and ports should explicitly provide for effective implementation arrangements and supporting mechanisms, including clear accountabilities, timelines and appropriate performance measures. In NSW's case, the Land Transport Access Plan should include a commitment to remove the 'station access fee' from the Domestic and International rail stations as has recently been accomplished for Green Square and Mascot stations.

Having regard to the Australian Government's intention to link future infrastructure funding decisions to States and Territories meeting the criteria for future strategic planning of capital cities, Infrastructure Australia should be consulted by States and Territories during the preparation of Land Transport Access Plans. Infrastructure Australia's role should be to work with State and Territory Governments to:

Audit the quality and effectiveness of existing land transport infrastructure and services provided by States and Territories to access capital city airports;

Identify any gaps in the provision of such land transport infrastructure and services which, if not filled, will undermine the airport's ability to accommodate forecast growth in aviation activity; and

Ensure Land Transport Access Plans contain the proposals necessary to upgrade land transport infrastructure and services to a sufficient standard that will allow the airport to accommodate forecast growth in aviation activity.

It would be beneficial if the Productivity Commission would enunciate principles to guide governments in this area to ensure that wider community benefits are properly taken into account. Economic efficiency would be promoted if State and Territory Governments could not enter into agreements that restrict competition between the various modes of land transport used to access capital city airports. As with the recommendation to prepare Land Transport Access Plans, this could be achieved as part of the *National Urban Policy*.

6. Car parking

Key points

- The market for access to Sydney Airport by car is very competitive, with competition from several car park operators and other means of access including taxi, and drop-off/pick-up, while competition would be enhanced by government action to reduce surrounding road congestion
- Sydney Airport has a small market share of airport access by passengers and car parking is a modest component of an interdependent business, so pricing distortions would have a cost elsewhere
- Sydney Airport has expanded car parking facilities and introduced new products. As a result:
  - Sydney Airport car parking prices are substantially below and have increased more slowly than CBD benchmarks
  - Sydney Airport car parking prices for the remote long term car park are below the average of 'off-airport' car parking prices
- Sydney Airport has also improved facilities and services for all competing access modes, and has publicly advocated for improved public transport where there are significant opportunities for government to improve rail and bus services and competition by substitution
- Whilst Sydney Airport has a higher market share of parking by staff, as a result of the limited public transport options, it has commercial agreements with airlines for staff parking that are at substantial discounts to the standard prices

6.1 Description of the car parking business

Sydney Airport offers a wide range of car parking facilities and services, providing choice to a wide range of airport users. The range of services has been expanded over time, and will continue to be so. The primary characteristics of the car parking business are:

Total Capacity: 12,148 spaces
Facilities: car parks are currently located in three precincts:
- International: at grade (ground level) and multi-storey for passengers, staff and other users
- Domestic: multi-storey for passengers, staff and other users
- Remote long term: at-grade for passengers, staff and other users

Products:
- Free pick-up: 10 minutes (Domestic), 15 minutes (International)
- Pre-booked (internet), long term parking sold at a discount
- Discount self-parking in the remote car park, with a free bus shuttle. Differentiated shade-cloth area in the remote car park
- Self-parking adjacent to the domestic and international terminals
- Valet parking, under cover, in the domestic and international precincts. Ancillary services such as car wash are also offered
- Staff parking is provided in all locations, under contracts with the employers

Channels to market:

- Drive-up
- Internet: frequently sold at a discount
- Airlines: Sydney Airport has agreements with some airlines to sell parking at the time of booking the flight

6.2 The market for airport access

The market for airport access by passengers is very competitive. There are several providers of car parks – on airport and nearby – as well as strong competition from taxis, limousines, rail, drop-off / pick-up and private hire mini-buses. The strength of that competition is reflected in Sydney Airport's share of the market for passengers' airport access – 10% for domestic passengers and 13% for international passengers[61].

More importantly, it is in Sydney Airport's broader interests to promote access to the airport by all access modes, even if they are in competition with its car parking business. Car parking is itself only one modest component of the very complex business components of running an airport, so pricing distortions would have a cost elsewhere. The lack of market power and importance of promoting access is demonstrated by Sydney Airport's activities over recent years:

- Sydney Airport has invested in all modes of access: car parks, taxi facilities, limousine facilities, pick-up / drop-off facilities and bus/coach facilities.
- Sydney Airport has consistently argued for improved public transport to serve the airport (see Section 5).
- Car parking capacity has increased more quickly than demand, without significant price increases.
- Car parking prices have increased substantially more slowly than commercial CBD prices and remain competitive with and often lower than off-airport car parks.

Sydney Airport is accessed by a wide variety of passengers, most of whom access the airport regularly and many of whom have different needs at different times. For a given passenger or group of passengers, the choice of access mode is affected by many factors including their length of stay, the time of day of departure (and arrival), the size of the group, the amount of luggage, the passengers' valuation of convenience and certainty, and the purpose of travel.

To understand the car parking business better, Sydney Airport commissioned a study[62] which demonstrated that most airport users (whether or not they used the car park) were aware of several different access modes and, on average, used 2.7 different access modes during the preceding 12 months. This use of alternatives was true regardless of where the users were travelling from within NSW. Choice of access mode varied according to distance but, even for the most remote air traveller locations, the average number of modes used was 2.2.

Car parking competition from off-airport car parks is very strong for long term parking. Several of the off-airport car parks offer cheaper prices than Sydney Airport for stays in excess of one day, although not all off-airport car parks are cheaper than Sydney Airport or for all time bands. The product offered also differs from Sydney Airport. Off-airport car parking is generally required to be booked in advance, the car may be parked by an attendant, the parking is often within a building or multi-storey car park and the passengers are

[61] *Sydney Airport Ground Travel Plan* 2006
[62] Sweeney Research, 2010 and Sydney Airport Analysis

transferred to the terminal in a minibus. In contrast, the on-airport car parking is not required to be booked in advance, is generally self-park, is at-grade in the remote car park and the passengers are transferred to the terminal in a large bus. Of course, passengers continue to have the option to park long term in the domestic and international multi-storey car parks, for a higher price reflecting the greater convenience of being immediately adjacent to the terminal.

Off-airport car parking competition is less strong for short term car parking since the absolute difference in car park prices is reduced (due to less time) and the time saved by being close to the terminal is a higher proportion of the total time of the journey. However, competition from other access modes is highest for users with short trip length (up to three days). Hence whilst these users are the least likely to use off-airport car parks, they demonstrate the highest degree of competition from non-parking access alternatives.

The Sweeney Research study also showed that car park users specifically are aware of and use other access modes. Of car park users (both on- and off-airport parking), in the previous 12 months:

- 54% had also used drop-off
- 50% had also used taxi
- 41% had also used the train
- Smaller proportions had used the various other access modes.

It is clear from the evidence above that the Sydney Airport car parking business faces strong competition from other access modes (in addition to off-airport car parking), reflected by the low market share of Sydney Airport's business. Decisions on prices and investment in additional capacity reflect this competitive environment.

While Sydney Central Business District (CBD) car parking is a different market, it serves as a useful comparison to parking at Sydney Airport because:

- It is a market in which many car parks are competing with each other
- Both the CBD and the airport have a scarcity of land in a 'must-go' location
- Car parks are not used as loss-leaders to attract business in either the CBD or at the airport
- It is noted that Sydney Airport operates its car parks on a 24 hour, 365 days basis while many CBD car parks close at night and do not open on public holidays.

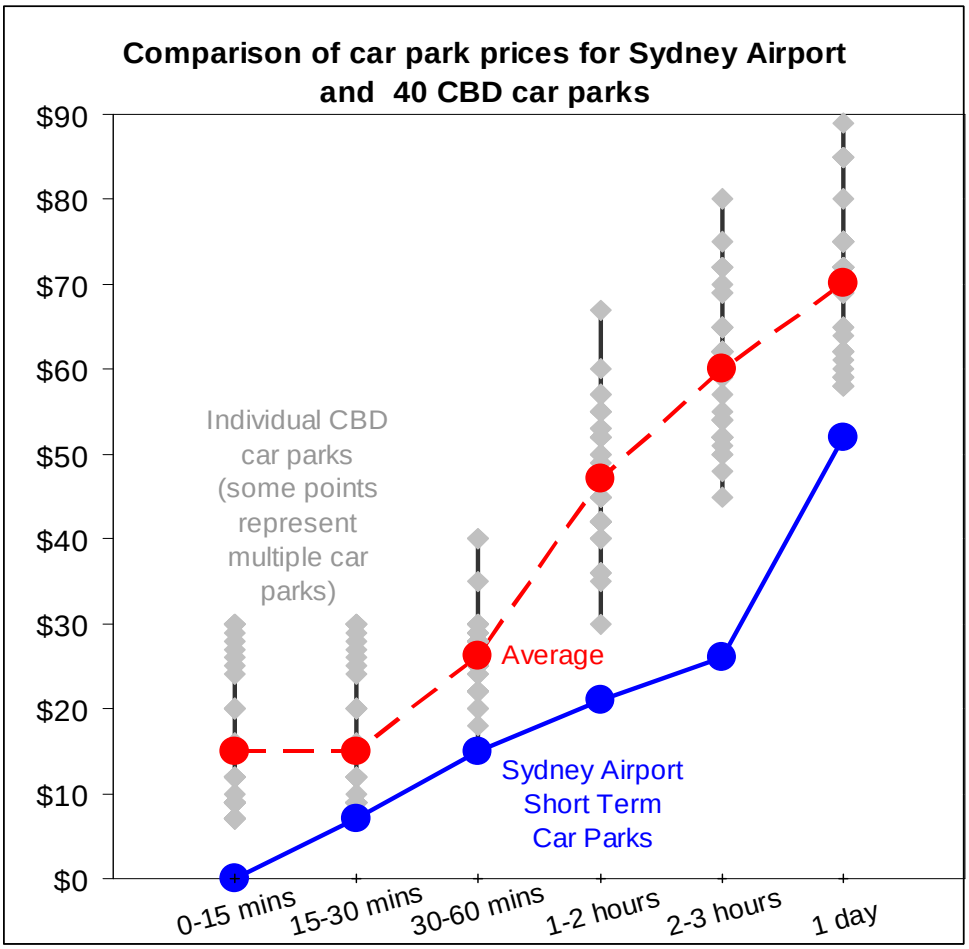
Sydney Airport's car park prices are competitive with off-airport car parks, are cheap relative to CBD car parks, and have increased only modestly since privatisation in 2002:

- As shown in Figure 10, the short term car park prices are 43% below the average surveyed CBD price for 1 hour and 26% below for 1 day
- As shown in Figure 11, the remote long term car park prices are cheaper than the average of the off-airport competitors
- Car park prices have increased more slowly than the surveyed CBD prices. As noted in the 2006 Productivity Commission Report, Sydney Airport's car park prices were only 28% below the CBD car parks in 2006 for 1 hour[63]

[63] Productivity Commission Review of Price Regulation of Airport Services, 2006, page 172

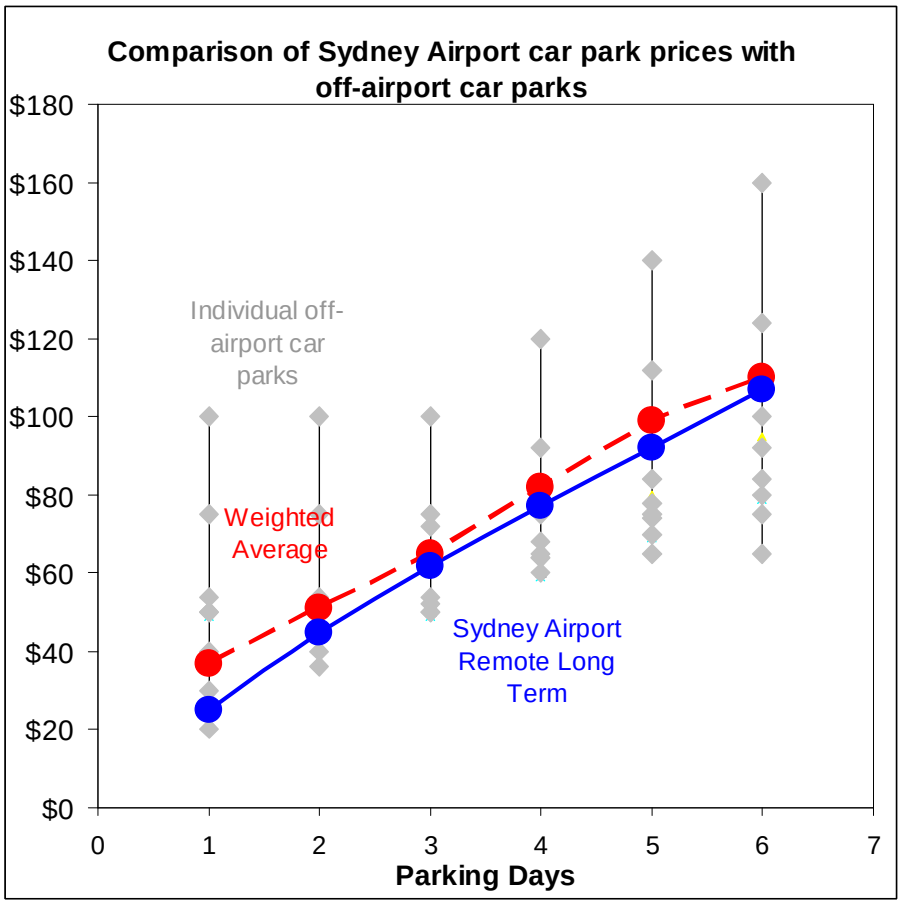
— Price increases have for most periods been modest. The 1 hour price increased by 3.0% per annum from 2001 to 2010, little different to inflation. By contrast, prices increased by 17% per annum between 1999 and 2001 prior to privatisation.

Figure10 Comparison of Sydney Airport car park prices with 40 CBD car parks



Source: Sydney Airport analysis, car park websites

Figure 11 Comparison of Sydney Airport long term car park prices with competitor off-airport car parks:



Source: Sydney Airport analysis, car park websites (weighted average is calculated based on estimated car park capacity)

Non-price competition is also important to consumers as indicated by the following examples:

- Sydney Airport's multi-storey and remote long term car parking products involve self-parking by the customer who retains the keys to their vehicle at all times. In contrast, many of the off-airport parking competitors require the customer to leave the keys of the vehicle with the parking attendant who may enter, drive and relocate the vehicle at anytime during the customer's absence. The peace of mind secured in not having others drive their vehicle can be an attractive non-price factor to many customers.
- Unlike many of its competitors, Sydney Airport operates its car parks on a 24 hour, 365 days basis. This provides more convenience and important flexibility for customers.

Perceived as providing a higher quality service, these non-price factors can be important to passengers and other customers in the decision to select Sydney Airport parking over a competitor's product.

Sydney Airport has a stronger market position for staff access to the airport, largely because of the inadequate public transport options available for staff. As described in Section 5:

- Staff are discouraged from using rail by the annual 'station access fee' of almost $1,000, in addition to the normal CityRail fare
- Only staff who live on or near Bus Route 400 can travel by bus

— For the relatively significant number of staff who start or finish work late evening or early in the morning, between the hours of midnight and 5am there is no public transport.

Sydney Airport recognises the importance of safe and reliable access for staff and has commercially negotiated staff rates in the car parks with BARA and some individual airlines. Staff are generally able to park in the car parks adjacent to the terminals at prices which are 71% below the remote long term car park prices and 76% below the prices that would normally apply to the domestic and international car parks. In addition, Sydney Airport has recently renewed a ground lease with Qantas in the Domestic Precinct which is used for staff parking, at a rate which is a small fraction of a commercial return, given the value of the site.

6.3 Promotion of all access modes by Sydney Airport

Car park capacity has increased substantially, particularly for short term and staff parking which increased by 7.5% and 85% respectively between June 2006 and June 2010. As a result, all of the car parks are larger than is required for the peak demand of the average day[64]:

— The international car park is 32% larger than average peak demand
— The construction of the international multi-storey car park structure provided significant capacity ahead of demand
— The domestic car park is 61% larger than average peak demand
— The remote long term car park is 61% larger than average peak demand

Concurrent with the increase in car parking, Sydney Airport has improved facilities and services for all competing access modes. These improvements have included:

T1 drop-off / pick-up: Introduction of 15 minutes free parking in the T1 car park
— Free parking was not available when Sydney Airport was privatised in 2002

T2 drop-off / pick-up: expansion of the T2 drop-off / pick-up from 7 to 51 car spaces in 2009. This expansion was accompanied by:
— An increase in the permitted waiting time from 2 to 10 minutes
— Reduced congestion in front of T2 and T3 as a result of the removal of parked cars from the left hand lane in front of T2
— Reduced congestion in the whole Domestic Precinct as a result of fewer cars circling whilst waiting for passengers
— A short under-cover walk from this parking to the terminals
— Free parking is not available at many large international airports. For example, at London Heathrow, while it is possible to drop off a passenger for free, all cars (including taxis) picking up passengers must use and pay for the car park.

Taxis: increased capacity and introduction of new services including:
— Increase in the T1 taxi pick-up area from 12 to 20 bays, with a doubling of the weather protected passenger queuing area
— 30% increase in taxi holding-bay area for both Domestic and International precincts
— 75% increase in T1 capacity for pre-booked taxis
— Introduction of a short-fare return system to encourage taxis to accept short fares and return to the airport for more passengers

Limousines: introduction of dedicated T1 pick-up areas for limousines including awnings to protect passengers in inclement weather

Buses and Coaches:

[64] NERA, "Economic analysis of car parking", figures 2.3, 2.4 and 2.5, included in annexure 5

- 40% increase in Domestic bus pick-up / drop-off bays
- Introduction of a new mini-bus / coach holding area in the long term car park, at the expense of 362 potential car parking bays

Trains[65]: improved terminal way-finding to the stations.

- the Airport Rail Link has an information counter in T1
- train FIDS screen in all terminals' arrivals areas

Bicycle: provided 20 bicycle storage racks, with showers available nearby (T1 only)

Communication with passengers:

- The Sydney Airport web site includes information on the transport options available and privides a comparison on the costs of parking, rail and taxi as well as information about the availability of bike rack and shower facilities
- The 'Travel concierge' service was introduced in T1 for arriving international passengers, providing quick and clear information on the transport modes available shortly after the passengers have passed through customs
- Gold Ambassadors have been introduced to T2 to provide assistance to passengers in the arrivals hall
- Investment in additional signage in all terminals

The implementation of free short term parking (15 minutes) at T1 and increased permitted waiting time at T2 is estimated to cost in foregone revenues of up 10% of car parking income per annum.

In addition, Sydney Airport's Master Plan 2009 includes a commitment to the achievement of a modal shift of 5% from motor vehicles to public transport by 2024[66]. In support of this, Sydney Airport has consistently advocated improved public transport, including lower train fares, increased luggage space on the airport trains and more public buses. Moreover, the implementation of Sydney Airport's suggestions for improving bus and rail services would substantially improve public transport access and provide on-going commercial constraint on parking prices.

The investments in improved car parking – both paid and drop-off / pick-up – are reflected in the steady improvement in the passenger satisfaction with car parking.[67]

6.4 Future car parking developments

Like all competitive businesses, Sydney Airport is continually reviewing and looking to expand the services provided. Over the next several years the services provided to passengers will change further and are expected to include:

- Increased use of the internet to book car parking in advance
- Off-peak discounts enabling better capacity management
- Development of joint products including car parking as one component. This is already advanced in other airport markets including the UK and at Auckland Airport. For example, Auckland Airport offers eight different car parking options and products to choose from. All of these products are sold on-line with full price transparency and service description.

[65] Sydney Airport has no influence over the operation of the train stations or trains as discussed in Section 5.
[66] Sydney Airport Master Plan 2009, page 89
[67] ACCC Airport Monitoring Report, charts 8.3.6 and 8.3.7

While car parking capacity currently comfortably exceeds the peak demand of the average day at Sydney Airport, there are day when the car parks approach capacity. This is particularly true for the Domestic precinct car park. Over time, Sydney Airport will need to progressively increase the capacity of all of the car parks and other landside access facilities. Given the relatively small site occupied by Sydney Airport, this will inevitably include additional multi-storey car parks with the investment decisions being made against alternative uses for the land.

The most difficult developments will be in the Domestic Precinct. The optimal long term development of this precinct is being considered, taking into account the needs of all access modes. It is clear that:

There is no immediate need for additional car parking capacity and even the peak day demand is well short of the demand required to justify a large increment to the capacity
There are no short term opportunities to efficiently add small increments to the car parking capacity – any such development would need to be removed and replaced in the medium term
The construction phases are likely to result in temporary reductions in service quality
The planning and phasing of the capacity increases needs to be consistent with the long term vision for the Precinct – there should be no interim developments that are not part of the long term plan, being both financially unviable and unnecessarily disruptive for passengers.

6.5 NERA car parking report

NERA Economic Consulting (NERA) has prepared an independent economic analysis of Sydney Airport's car parking and landside access charges (attached in Annexure A1). NERA considers whether Sydney Airport has a substantial degree of market power in relation to the provision of either car parking landside access services and whether it has taken advantage of any such power. It concludes that:

Sydney Airport neither possesses nor has exercised substantial market power in relation to the relevant services[68]

NERA notes that there are at least ten off-airport car parks in close proximity to the airport, that there are at least five other alternatives to car parking (drop-off, taxi, rail, bus and car rental) and that car parking represents only a small fraction of Sydney Airport's total revenue, all of which suggest that:

…Sydney Airport cannot reasonably be said to possess a substantial degree of market power in relation to car parking or landside access arrangements[69]

NERA also demonstrates using a variety of analyses that Sydney Airport's car parking and landside access fees are not excessive, that the airport has invested significantly in expanding its car parking and landside facilities, that service quality has improved over time and that the airport has repeatedly advocated for better public transport. It notes that:

[68] NERA Economic Consulting, *Economic Analysis of Car Parking & Landside Access Charges*, 7 February 2011, page i.
[69] ibid, page iii.

None of the factors set out above are suggestive of a monopolist seeking to exercise its market power by charging excessive prices, reducing its quality of service or hindering landside access[70]

NERA consequently concludes that the current monitoring arrangements serve no useful purpose. In explains that, at best, those arrangements provide data on prices and products that can be well out of date – up to 21 months – when current information is readily obtainable from Sydney Airport's website and, at worst:

…they can (and do) convey misleading impressions about the profits that the airport is making from car parking and landside access charges, which has the potential to harm the airport and its customers[71]

NERA therefore concurs with the view reached by the Productivity Commission in 2006, that there is no need for car parking and landside access charges to be monitored – at least at Sydney Airport.

6.6 Conclusions

The market for access to Sydney Airport by car is very competitive, with competition from several car park operators and other means of access including taxi, and drop-off/pick-up, while competition would be enhanced by government action to reduce surrounding road congestion. Sydney Airport has a small market share of airport access by passengers and car parking is a modest component of an interdependent business, so pricing distortions would have a cost elsewhere.

Sydney Airport has expanded car parking facilities and introduced new products. Sydney Airport car parking prices are substantially below and have increased more slowly than CBD benchmarks and car parking prices for the remote long term car park are below the average of 'off-airport' car parking prices.

Sydney Airport has also improved facilities and services for all competing access modes, and has publicly advocated for improved public transport where there are significant opportunities for government to improve rail and bus services and competition by substitution.

Whilst Sydney Airport has a higher market share of parking by staff, as a result of the limited public transport options, it has commercial agreements with airlines for staff parking that are at substantial discounts to the standard prices.

The NERA economic reports concluded that the rate of return that Sydney Airport has earned on its car parking land have fallen materially in real terms and the return per m^2 that Sydney Airport earns on its international car park is less than adjacent commercial property and other local parcels of land; and there is no indication that prices at the domestic car park reflect anything other than the locational attributes of the relevant land.

None of these factors are consistent with the exercise of market power.

70 ibid, page iv.
71 ibid.

7. Implementation of a monitoring regime

Key points

- Price and quality monitoring has been a key feature of the light-handed regime. Sydney Airport supports its improvement and continuation
- The recent ACCC Airport Monitoring reports fail to provide useful policy information and contain a large amount of data and commentary which is misleading
- Sydney Airport proposes an improved monitoring scheme which would provide more focussed, reliable and relevant information in a timely fashion, with lower administrative costs. Features of this proposed scheme are:
  - Publication of the international ACI ASQ survey results (replacing the ACCC monitoring of passenger service levels). The ACI ASQ results for each question should be attributed appropriately: to the airport, the airlines, Customs, Immigration and/or AQIS
  - Publication of the scope of the service level agreements and whether the airports and airlines are meeting the commercially agreed targets (replacing the ACCC monitoring of airline service levels)
  - Publication of the audited average return on capital earned by the airport since July 2002, calculated on a basis consistent with the commercial agreements (replacing the ACCC monitoring of financial performance)
  - Discontinuation of the ACCC monitoring of car park prices
  - All reporting to be compliant with relevant ISO standards
  - The Federal Government could play a reserve role to provide assurance that monitoring commitments were being met

7.1 Principles of effective monitoring

Price and quality monitoring has been a key feature of the light-handed regime. Sydney Airport supports its continuation. However, it is important that such monitoring is done well and serves its policy purpose. Moreover, monitoring needs to respond to changing competitive and commercial circumstances, as the costs and benefits of monitoring are not static.

The key principles of effective monitoring should include:

- **Consumer-focussed:** the airlines and airports have commercial relationships to provide a joint product to passengers. Monitoring should be designed to support consumers, particularly passengers, who have varying relationships with businesses and government agencies (which are all part of performance assessment)
- **Non-distortive**: monitoring should not distort collaboration to improve performance
- **Focused:** monitoring should concentrate on areas in which the airport has potential market power, should provide useful information concisely, and exclude extraneous information
- **Robust:** methodologies for obtaining, analysing and reporting data should be objective, unbiased, transparent and statistically robust

- **Comparable**: benchmarking should be against comparable airports in comparable circumstances
- **Timely and cost-efficient**: monitoring should be cost-efficient and the results published quickly.

7.2 Monitoring – overall commentary

The *Airport Monitoring Report* published by the ACCC each year is intended to support the policy objective of light handed regulation. The report is also a high profile and influential document that can affect the financial performance of the airports being monitored. The effect on corporate reputation and brand is appreciable. That the report can influence the decisions of governments is demonstrated by the timing of this review, which was brought forward by at least a year in response to matters raised in the 2008/9 report. This decision is not cost-free to the government, the airports or the airlines, including both the direct costs of the review and the uncertainty introduced into investment decisions.

The recent monitoring reports fail the contemporary policy purpose through the absence of useful, comparable and up to date information, and contain poorly founded data and unsupported and out of date commentary – some of which is contradicted by evidence presented.

Nonetheless, the ACCC follows all of its strongest criticisms with caveats that the

...monitoring results do not in themselves provide conclusive evidence as to whether or not the airports are earning monopoly rents[72].

Examples of unsubstantiated statements include:

- Sydney Airport made monopoly rents by delaying the investment in T1. As demonstrated in Section 4.7, Sydney Airport has invested over $1.8 billion since privatisation and completed the re-development of T1 when peak international travel volumes were below the levels of the Sydney Olympics for which the terminal had been designed
- Sydney Airport made monopoly rents by reducing service levels[73]. As demonstrated in Section 4.9, the return on capital of Sydney Airport does not exhibit a return that could be considered consistent with monopoly rents. Likewise, the majority of passenger ratings were 'good' or better, and the airline survey on which the ACCC exclusively relies in its claim is both methodologically unsound and contradicted by the objective service measures.
- the airports made monopoly rents in its car parking activities[74]. This statement was withdrawn for Sydney Airport in the most recent report, but as demonstrated in section 6.5 the statements in the 2007/8 and 2008/9 reports were not supported by evidence.

Given the real costs that can arise from unreasonable criticism, a good policy process (and natural justice) requires compelling evidence before critical comments are made, and not mere suspicion – the caveats used in the recent ACCC reports are not sufficient.

[72] ACCC Airport Monitoring Report 2009/10, page 44
[73] ibid, page 45
[74] ACCC Airport Monitoring Report 2008/9, page 65

The integrity and usefulness of the ACCC monitoring process would be supported if the airports were able to respond to the full draft report before it is published. This would allow airports the opportunity to correct errors or misplaced conclusions. The preparation of reports of the Commonwealth Auditor General follows this process, as do the Productivity Commission's own draft inquiry reports. The airports should also have the opportunity to incorporate within the ACCC report a response to any of the ACCC comments.

At present, the ACCC provides the airports with some, but by no means all, of the draft report but is under no obligation to include any or all of the comments made by an airport in response. For example, in reviewing the section dealing with the anonymous airline survey in the draft 2009/10 report, Sydney Airport suggested that the final report should include the following comment:

Sydney Airport noted that the Productivity Commission has stated that:
"An airline 'talking down' the performance of an airport in a quality of service monitoring survey to gain an advantage in negotiations with an airport operator is likely to be part and parcel of the commercial negotiations between those parties."
(Productivity Commission 2009, Annual Review of Regulatory Burdens on Business)
Sydney Airport also noted that it is their view that passenger survey results are a more reliable measure of performance.

Even though it was clearly relevant to the issue under consideration, this suggestion was not accepted by the ACCC and Sydney Airport's comment was not included in the ACCC's final report. Other comments made by Sydney Airport were similarly disregarded.

Most importantly, the monitoring reports should be compliant with the appropriate ISO standards – standards which are prepared by Standards Australia.

Finally, it should be noted that the recent monitoring reports are too long for most people to read and are published eight months after the reporting period ends, which further diminishes their public policy usefulness.

7.3 ACCC Monitoring process – financial

As with the overall ACCC monitoring report, the financial monitoring sections of the report fail to provide useful information and contain a large amount of data and commentary which is misleading. The principal difficulties with the existing monitoring are:

- The asset values and returns on capital reported are not consistent with the commercial agreements which have been negotiated. This inconsistency will increase over time.
- The report's focus on a single year's financial performance is inconsistent with the long investment horizons which are characteristic of airport development, and with the assessment of risks made at the time of investment.
- The financial report necessarily relies on ex-post results, which means the observed results (whether of over- or under-recovery) will reflect both fortune (good or bad) and ex-ante behaviour (exercise of market power or otherwise).
- Over 90% of the financial monitoring relates to data sources which individually provide no information on whether airports have exercised market power – although the ACCC attempts to infer conclusions from this data.
- The ACCC makes claims that are contradicted by the evidence, including the claim that Sydney Airport has exercised market power.

Consistency with the commercial agreements

The financial monitoring uses International Financial Reporting Standards (IFRS) accounts, or alternatively the 'line-in-the-sand' methodology, to report financial performance. This is consistent with the methodology prescribed by the Productivity Commission in 2006.

This methodology is, however, inconsistent with the charges which have been commercially negotiated between Sydney Airport and the airlines, which consistently applies a real WACC to an indexed asset base. In addition, the commercial agreements are consistent with the optimised depreciated replacement cost of the non-land assets as determined in 2001. The difference in values is increasing every year and will gradually reduce the meaningfulness of the reported numbers.

The effect of applying a real WACC to an indexed asset base is to reduce charges in the short term and increase charges in the longer term. As a result, the returns on capital reported by the ACCC would be expected to be below a nominal WACC in the short term and above the nominal WACC in the longer term.

For a reader who is aware of Sydney Airport's use of a real WACC and asset indexation, this will mean that the monitoring reports are:

- Inadequate in the short term
- Meaningless in the long term, since it will not be feasible to adjust the asset base for indexation with sufficient accuracy given ongoing investment.

In addition, the commercial agreements negotiated have recognised the value of the landfill – an asset which is used by the airlines and should therefore be paid for. Despite this recognition by the airlines in the commercial agreements and the recognition of the value of the landfill by the ACCC in its pricing decision in 2001, the 'line-in-the-sand' accounts exclude the value of the landfill. Regulatory precedent from New Zealand, the UK and elsewhere is that 'discovered assets' should be included in the regulatory asset base.

Monitoring long term uncertain investments with annual ex-post returns

All investments are by necessity made with uncertain outcomes over both the short and long term. This is true of all investments – from the $5.4 billion paid to the Commonwealth Government at the initial privatisation of Sydney Airport to the $1.8 billion invested subsequently as well as future investments in the airport.

Investments will be made only when the expected return achieved on the investment exceeds the cost of capital, with appropriate allowance for risk. When making investments it is certain that the outcomes will be different from any forecast – a good investment decision is made when the forecast represents an average outcome with as much chance of exceeding the forecasts as there is of falling short. It is also certain that the returns will not be constant every year, but will be better in some years than others – the relative performance of different years may or may not be predictable at the time of investment.

If investors are to invest then it is critical that this symmetry between out-performance and under-performance is maintained. If, in contrast, investors were expected to suffer all under-performance but were not permitted to enjoy any out-performance then no investments are viable. If out-performance is permitted up to an artificial ceiling then the average returns for all projects are reduced and some investments will no longer be viable.

Against this background, the reporting focus on annual ex-post returns risks distorting perceptions of the financial results made by the airports. In particular, there are two difficulties:

- **Ex-post**: any observation that ex-post returns are above the WACC could be consistent with either good fortune (of which there should be a 50% probability) or exercise of market power

- **Annual**: any observation that an individual year's ex-post returns are above previous years' could be due to good fortune, variations inherent in the commercial contracts, or exercise of market power.

The difficulty caused by the focus on annual returns is avoided by reporting the average return since the introduction of the light-handed regime, rather than the individual year's return – a period inconsistent with the longevity of investments made. The difficulty of interpreting ex-post returns is unavoidable in a monitoring regime – but, at the very least, any claim that an airport is exercising market power should require the average return on capital since 2002 to be significantly above the WACC.

The best assessment of appropriate charges is made during the negotiation of the commercial agreements. During these negotiations, both the airlines and airports have available audited information on the current costs and can both assess the future expectations. This avoids the difficulty arising from the use of ex-post returns and the potential to inappropriately interpret good fortune as the use of market power.

Monitoring exercise of market power through prices, passengers and investment

In the 2009/10 Monitoring Report, the financial monitoring for Sydney Airport is contained within sections 8.1 (Sydney Airport) and 2.2 (all airports). Of the 27.5 pages covering financial monitoring, only two pages (section 2.2.6 and page 264) relate to Sydney Airport's return on aeronautical assets.

These two pages report a return on capital for Sydney Airport of 7.8% ('line-in-the-sand'). The previous years' reports show similar returns for Sydney Airport in the vicinity of 8%.

It is not possible to interpret a pre-tax real return on capital of around 8% as being excessive for an Australian business with the risk profile of an airport.

Indeed, Sydney Airport's return on capital is significantly below those of Melbourne, Perth and Adelaide Airports – and yet it is Sydney Airport which the ACCC believes is earning monopoly rents:

The monitoring results, when considered within the context of the airport's market power, point to Sydney Airport earning monopoly rents from services provided to airlines.[75]

The remainder of the financial monitoring is focused on several partial measures, none of which provide clear information on the airports' exercise of market power on aeronautical activities. These measures are:

[75] Airport monitoring report 2009-10 page vii.

- Passenger volumes and aircraft movements.
- Aeronautical revenues.
- Average airport charges.
- Airport aeronautical costs (excluding costs of capital)
- Security revenues and expenses
- Aeronautical margins (excluding costs of capital).
- Asset values
- Return on total assets (using depreciated historic cost of all assets).

Use of these measures may lead to misinterpretation or misrepresentation of the actual position. For example, the increase in average airport charges and aeronautical margins has been misinterpreted by the ACCC as evidence that Sydney Airport has exercised its market power. As noted above, the reported return on capital demonstrates that Sydney Airport is not earning monopoly rents. The ACCC's interpretation of increased airport charges and aeronautical margins has omitted the need to earn a return on the substantial investments made over the period of the report.

The lack of information pertaining to exercise of market power contained in the movement of average charges is illustrated by both:

- The 97% increase in charges approved by the ACCC in May 2001. The ACCC-approved charges reflected the costs of operating Sydney Airport. Subsequently, the underlying charges have increased broadly in line with inflation – reflecting the increased costs resulting from inflation, regulation including new security requirements, higher activity and new investment, and offset by increased traffic volumes.
- The charges increase related to ground power and pre-conditioned air. This increase in airport charges related to the airport offering a new service which reduced non-airport airline costs by a larger amount. Far from being an exercise of market power, this charge increase reduced the overall costs of the airlines (see Section 4.3).

The higher charges of Sydney Airport relative to other Australian airports reflect higher costs associated with operating Sydney Airport arising from:

- A higher proportion of international passengers, which are substantially more expensive to process for a multitude of reasons relating to regulations, airline operations and passenger behaviour (see Section 3.3)
- Operational regulations unique to Sydney Airport which reduce traffic volumes outside of the peak and reduce the average aircraft size (see Section 3)
- A location within Australia's most expensive city – Sydney – for housing, wages and general costs of living
- A land congested site.

Future of financial monitoring

Sydney Airport believes the extent of the current financial monitoring is faulty, unnecessary, uninformative and misleading.

The best assessment of appropriate charges is made during the negotiation of the commercial agreements. During these negotiations, both the airlines and airports have available audited information on the current costs and can both assess the future expectations.

With such agreements now demonstrated to be working, arguably there should be no need for financial monitoring by ACCC in the future. However, whilst there may be no need for ongoing financial monitoring, Sydney Airport would recommend the audited self-reporting of the average return on capital earned by the airport since July 2002, calculated on a basis consistent with the commercial agreements.

7.4 Monitoring of service quality

Sydney Airport has continued, since 2006, to raise its serious concerns about the value and appropriateness of the existing quality of service monitoring report which does not meet the generally accepted methodological standards for professionally conducted research. The reports are characterised by methodological flaws and fail to properly deal with conflicts of interest. According to the expert reviews conducted for Sydney Airport, they are ..*not interpretable*and are ...*of little value*.

Sydney Airport and other parties have expressed concern with the ACCC's methodology since 2006. Sydney Airport's comments included its submission to the Productivity Commission in 2009[76] and media statements in 2010 and 2011[77]. The Productivity Commission also expressed concerns in 2006[78]. These concerns have not been addressed by the ACCC.

To assist both the Productivity Commission undertake its examination of the ACCC's methodology and the ACCC in reviewing its own approach to methodology, Sydney Airport commissioned two expert professional reviews. As these are important documents, they are appended to this submission (attached as Annexures 2 and 3) but short summaries are provided below. These reports were provided to the ACCC in January 2011 prior to the release of the latest ACCC report.

University of Melbourne – Statistical Consulting Centre:
Methodological Review of the ACCC Airport Monitoring Report

The University of Melbourne's Statistical Consulting Centre was established in 1984 to provide high quality consulting services in statistics. The Centre's report identifies serious flaws in the ACCC's service monitoring methodology. The extracts below provide an indication of its findings:

Many so-called 'overall' measures combine information from responses to different questions, and also from different sources. These measures are not defined, and as such, are not interpretable. (p 2)

The ACCC report aims to support comparisons between airports and over time. Such comparisons cannot be reliably made without statistical information to support statistical inference. We recommend reporting standard errors or confidence intervals for estimates obtained from the surveys and for comparisons of interest."(p 2)

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[76] Annual Review of Regulatory Burdens on Business: Social and Economic Infrastructure Services (2009) Sydney Airport submission – Page 3 http://www.pc.gov.au/__data/assets/pdf_file/0003/90552/subdr56.pdf
[77] Sydney Airport press releases. 07 February 2011 - Questions for the ACCC, 03 February 2011- Expert Reviews of the ACCC's Airport Monitoring Methodology, 11 March 2010 - ACCC Report is Out of Date
[78] Productivity Commission 2006, *Review of Price Regulation of Airport Services*, Report no. 40, Canberra, page 117

The survey results do not have a clear interpretation. Even if a valid, robust and consistent methodology was used across airports, the results as presented are uninformative for several reasons: a continuous numeric scale is imposed on a set or ordered categories; survey items are combined in an unspecified way to produce an overall measure of passenger assessed quality of service, and there are no measures of precision to aid the interpretation and importance of observed differences between airports and across time. (p19-20)

The ACCC guidelines state that airport operators must consult them closely on the methodology and contents of the survey, and that a full description of survey methodology is provided to the ACCC with the results. However, consultation would need to go far beyond the current guideline; the requirements as implemented by the ACCC do not appear to be sufficient for ensuring the passenger survey is of sufficient quality. Without clear and consistent guidelines for all airports, and without transparent reporting on methodological detail, the results have little value. (p 20)

GA Research:
Independent Review of the 'Airport Quality of Service Monitoring' Section of the ACCC Airport Monitoring Report 2008-09

The Australian standard for market opinion and social research (AS:ISO20252) was published by Standards Australia in January 2007 and is internationally recognised as a quality management system to ensure the quality of staff, design, fieldwork, analysis and reporting of all research complies with professional standards. GA Research is a specialist market and social research firm and is AS:ISO 20252 accredited. The GA Research report assessed the ACCC's work against the provisions of AS:ISO 20252 and identified numerous serious flaws and deficiencies in the ACCC's approach to monitoring as indicated below:

It is GA Research's opinion that:

The level of detail reported in the published ACCC report does not appear to meet the accepted standards of the market and social research industry in Australia. The lack of information means that GA Research is unable to determine whether the research methods used to collect and analyse the findings are robust, reliable or valid.
There are significant questions around methodological issues including representativeness of the sample, the reliability and validity of the data collected and the appropriateness of the aggregation used to calculate the data, including the overall quality of service measure which is used to rank the five monitored airports. (p 5)

We have found the ACCC Report published on the ACCC website and supporting documents to be lacking in the detail required by Australian market and social research standards. (p 5)

Finally, we were unable to determine the details of the analysis that was conducted on the data to calculate the findings presented in the published ACCC report. The overall quality of service measure, which is the key measure used in the published ACCC report to judge the overall quality of service for each airport, is an aggregated measure, as there is no overall quality of service variable in the data sheet used for airport operators to provide the data. The analysis used to calculate this aggregated measure could not be determined from the published ACCC report. The lack of transparency raises questions about whether it is appropriately weighted, and consequently, questions about using it to judge the overall quality of service for each airport.(p 32).

In short, these independent reviews indicate that the ACCC's monitoring has failed to meet the standard required for policy purposes, and has thereby increased regulatory uncertainty for airports and thus future costs to airport users from increased financing costs. In addition to the flaws, errors and shortcomings identified in the two expert reviews, Sydney Airport has additional concerns about the ACCC's methodological approach, including:

- The airports are held responsible for services they do not deliver
- The ACCC fails to compare the airports against their international peers, but instead compares five airports which are very different
- The ACCC attempts to make comparisons between surveys which are conducted by different airports using different methodologies
- Weight is given to anonymous survey responses by airlines and border control agencies which have an inherent conflict of interest.

Incorrect attribution of responsibility

The Productivity Commission has stated that ....*regulation should not require business to take responsibility for matters over which it has no control or require business to provide information concerning other agencies.*[79]

Services to passengers at Australian airports are typically the result of cooperation between a number of different organisations including airport operators, airlines, Airservices Australia, Customs, Immigration and Australian Quarantine and Inspection Service (AQIS). A major weakness of the ACCC's approach is that it judges the performance of airport operators by monitoring services over which those operators have little or no control. For example, the ACCC reports on the length of time that passengers wait at check-in counters, at Customs and Quarantine, and for their baggage. In each case, it is reported as if the waiting time can be controlled by the airport operator. In reality, the waiting times are mostly determined by the number of people employed by the airline or government agency for the relevant tasks.

Far from assisting passengers, the inclusion of these measures in a report that purports to evaluate the performance of an airport operator creates confusion and may assist airlines and government agencies to avoid being held properly accountable for the level of service that they provide to passengers.

The ACCC, however, gives little weight to this issue believing that with respect to airport-related services not being delivered by the airport operator …*as owner of the head lease for an airport, [the] airport operator is in a position to at least influence the standard of services.*[80] This is an unreasonable claim – whilst it is true that Sydney Airport seeks to influence all areas of service quality, it cannot be held accountable for the resourcing and other decisions of the airlines or government agencies.

Comparison against Australian rather than peer airports

The Monitoring Report compares survey results for the five very different Australian airports, but makes no attempt to compare the airports against their international peers. It is not reasonable to compare Sydney Airport (with 11.1 million international passengers annually

[79] Productivity Commission, "*Annual Review of Regulatory Burdens on Business: Social and Economic Infrastructure Services*", 2009, p 218.
[80] *Airport quality of service monitoring guideline*, ACCC, (October 2008), page 5.

and 38 international airlines) with Adelaide Airport (with only 0.6 million international passengers annually and 6 international airlines).

Sydney Airport's peers for comparison purposes would include international airports with similar levels of activity, and Melbourne Airport to some extent.

Methodological inconsistencies

The current system provides for results across airports being ....*directly comparable through the ACCC's annual airport monitoring reports*.[81] Putting aside the large differences between the airports, there is no guarantee that the data on which the comparisons are made is genuinely comparable.

This is because the ACCC does not require a consistent methodology to be employed to measure quality of service. Different airports use different passenger surveys. The ACCC does not:

- Specify the questions that are asked in passenger surveys – meaning that different questions are actually posed to passengers at different airports
- Establish sample sizes or an acceptable margin of error – meaning that the results have different levels of reliability
- Specify whether the surveys should be conducted during peak hour or during the quietest hours of airport operations – which could decisively influence the passenger experience and hence the results produced
- Specify how representative samples need to be recruited to account for passenger demographics (for example, male/female or business/leisure traveller)
- Take account of issues such as establishing the views of non-English speaking passengers or passengers with special needs.

The ACCC's quantitative measures can also be somewhat crude and unhelpful. For example, the ACCC reported that the number of flight information display screens (FIDS) at Sydney Airport was reduced in 2006-07:

Since 2003–04 the number of FID screens within the international terminal has decreased from 1050 screens to 697 screens in 2006–07.[82]

However, what the ACCC did not acknowledge, and its calculations took no account of, was that this reduction was due to an *upgrade* from small, older CRT televisions to larger and clearer digital LCD screens. While the ACCC passenger survey showed an improvement for flight information display screens, the crude quantitative measure produced a perverse outcome that reported that passenger facilities had been reduced. The ACCC gave prominence in its commentary to the crude quantitative measure It is possible (but uncertain due to a complete lack of transparency which the Productivity Commission could remedy) that the lower number of FIDS screens (rather than the improved quality) is reflected in the ACCC's calculation of the overall service quality.

[81] Department of Infrastructure, Transport, Regional Development and Local Government, "Discussion Paper – Improving the passenger experience: Quality of service monitoring of airports", March 2009, p5.

[82] ACCC, Airport monitoring report for price monitored airports; Quality of service, price monitoring and financial reporting 2006–07, p 242.

Conflict of interest and lack of transparency in anonymous airline surveys

The ACCC recognises the potential incentive for airlines to deliberately under-report quality for the airports[83]. Nevertheless the ACCC makes extensive use of anonymous surveys that seek to record the opinions of airlines concerning the quality of service provided to them by airport operators. This presents two conflicts of interest, as follows:

- The airlines may have a commercial motivation to present negative views in order to influence the outcome of charges negotiations and/or regulatory reviews
- The airlines are motivated to optimise their own (short term) costs incurred in their delivery of the joint service, even where this does not optimise the (long term) joint costs of providing the service. For example, it is easier for the airlines to roster check-in staff if there is surplus check-in infrastructure. As a result, they may mark-down an airport which provides sufficient but not excessive capacity. Optimisation of the joint costs, on the other hand, will suggest that capacity is provided to meet but not exceed demand. In this respect the airlines are not customers of the airport but partners of the airport – the current surveys, which treat airlines as customers and airports as suppliers, are destructive of mutually beneficial partnerships.

This inherent conflict of interest is compounded by a lack of transparency. For example, when undertaking airline surveys the ACCC does not specify:
Whether or not all airlines using a particular airport were asked to participate in the survey and, if so, how many responded. Until 2005-06 this information was disclosed by the ACCC, but is not disclosed any more. This is important both because the number of airlines using airports varies and the response rate may or may not be representative.

- Which particular airlines responded to the survey? This information is important because it is important to know how significant a user of the airport an airline is. For example, if only smaller airlines responded to the survey, the results could be seen as being less reliable than had a mix of smaller and larger airlines responded.
- Whether or not a weighting is applied to a particular airline's responses based on how frequently that airline uses the airport. For example, a large airline could fly in excess of 100,000 passengers every week to numerous international, domestic and regional destinations. In contrast, a smaller airline might fly once a week to one destination and carry as few as 35 passengers per flight. The results would clearly be less reliable if the opinions of both airlines were identically weighted.

The reliability of the airline surveys is also questioned by the volatility of the reported results. In contrast to the passenger survey results, which tend to change only slowly over time, the airline survey results can vary widely over time and show little apparent relationship to the objective service quality measures.

Future of service quality monitoring

Sydney Airport welcomes effective service quality monitoring and collaborative service quality agreements which assist the airports and the airlines to improve the quality of their joint services. Sydney Airport recommends the publication of the ACI ASQ benchmarking results for passenger service quality, as well as the publication of information on the extent of service level agreements with the airlines and the performance under these agreements. Where appropriate, an auditor or regulator (such as the ACCC) could be asked to ensure that

[83] ACCC Airport Monitoring Report, 2009/10, page 16

an appropriate system for reporting is in place. The ACI ASQ survey is described in more detail in Section 4.8.

7.5 Monitoring of car parking

The car park monitoring report faces the impossible task of assessing whether the airports have exercised any market power they do have in the absence of the information necessary to form any meaningful conclusions. Nevertheless, the ACCC appears to have used its best endeavours to reach conclusions based on the information it has been able to collect. Unfortunately, in doing so, it has made unsubstantiated claims that the airports have exercised market power – and, in the process, potentially undermining the businesses of the airports.

In the 2007/8 and 2008/9 reports, the ACCC reaches the conclusion that ...*car parking prices at several airports are consistent with the airports achieving monopoly rents*. In the following paragraph the ACCC notes that it did not have the evidence to ..*conclusively* demonstrate what is little better than an assertion.

In fact, the conclusion reached – and the implication that while the evidence might not be 'conclusive', it does exist – is completely unsupported, misleading and damaging to the airports' businesses, brands and reputations. The ACCC conclusion rests on an analysis of whether the airports have market power in car parking and whether they have exercised any market power they might have.

As described in detail in Section 6.3, Sydney Airport does not believe that it has market power in the car parking business. Without restating all the arguments:

- It is inconceivable to Sydney Airport that it has substantial market power in airport access for passengers with a market share of little more than 10% - a market share that is a result of the strong competition that is available for all passenger segments
- Car park users are aware of and most also use other access modes
- It is not in Sydney Airport's interests to make access to the airport difficult for the almost 90% of passengers who do not park at the airport in order to improve the performance of its car parks – to do so would be to the detriment of the overall business.

Putting aside the argument over whether the airports have market power in car parking, the ACCC's analysis in the Monitoring Report 2008/09 on the exercise of market power is either lacking any evidence or is contradicted by the evidence that existed. The ACCC's conclusion was based upon the following observations or assertions:

- Car parking revenues were much higher than car parking costs
- Car parking prices had been increasing
- The airports had restricted competition from other access modes over a 12 month period
- Short term car park capacity had increased more slowly than had demand.

The erroneousness of these claims will now be demonstrated in turn.

<u>Car parking revenues at Sydney Airport do not meet total car parking costs</u>
The observation that car parking revenues were much higher than car parking costs is only meaningful if the costs of capital are included. This was not done by the ACCC.

While a detailed discussion of the car parking business is not appropriate or necessary, it is apparent that they should have high capital costs relative to operating costs, since car parks:

- Occupy a large amount of valuable land and include a large amount of concrete, asphalt and steel. For example, the T1 multi-storey car park built in 2008 at a cost of $65 million
- Require relatively little labour, maintenance or cleaning
- As a result of the high capital costs relative to operating costs, revenues would be expected to be significantly higher than operating costs.

NERA Economic Consulting (see Annexure 1) has also demonstrated that the use of land for car parking in the International car park is, in fact, less profitable than the use of that land for office accommodation.

Car parking prices have increased relatively slowly

Neither the level of car parking prices nor increases in them can be, *per se*, evidence for or against the exercise of market power. Rather, as the ACCC acknowledges, exercise of market power requires excessive returns on capital through the restriction of capacity (to create pricing power) or the restriction of competition (to create pricing power or increase volumes). If prices were useful as evidence, they would argue against Sydney Airport using market power. As demonstrated in Section 6.3, car parking at Sydney Airport is cheaper than in the Sydney CBD and Sydney Airport car parking prices have decreased relative to CBD car park prices since 2006.

While CBD car parking is a different market, it serves as a useful comparison because:

- It is a market in which many car parks are competing with each other.
- Both the CBD and the airport have a scarcity of land in a 'must-go' location.
- Car parks are not used as loss-leaders to attract business in either the CBD or at the airport.

In fact, as shown in annexure 6, it is neither possible nor appropriate for Sydney Airport to subsidise the car park costs from other activities at the airport.

Comparison to suburban shopping centre car parks is not meaningful because:

- Suburban shopping centres are not 'must-go' locations – there is often a wide choice of shopping destinations
- Suburban shopping centre car parks are loss-leaders which attract shoppers into the shopping centre with free or low cost/subsidised parking.

The prices in Sydney Airport's long term car park are competitive with the off-airport competitors, and are on average cheaper than the off-airport competitors. It would be unfortunate if some airport passengers have decided not to use airport car parks on the basis of the ACCC's assertions and instead chosen to use a more expensive alternative.

Sydney Airport has promoted airport access for all access modes

The ACCC's only evidence for its claim that Sydney Airport restricted competition from other access modes was that Sydney Airport moved the drop-off/pick-up for T2 further from the terminal. In fact, this move was part of an expansion of the drop-off/pick-up facility for T2[84], consistent with Sydney Airport's promotion of all access options to the airport.

Short term car park capacity has increased substantially

[84] See annexure 4 for more detail

The ACCC asserted that short term car parking capacity had not increased as quickly as demand. This statement was based on a comparison of the increases in short term car park spaces and short term car park demand, using the aggregate data for all five major Australian airports, comparing the results for 30 June 2004 and 30 June 2008. This claim is contrary to the evidence available at the time the report was written, namely:

- Although the number is not given in the report, the difference between the increase in capacity and demand at Sydney Airport was only 2%. This difference is hardly material.
- Sydney Airport opened the multi-storey international car park in July 2008 – that is, the month after the cut-off date and approximately 8 months before the ACCC issued its report. The international multi-storey car park increased the short-term capacity of all airports by almost 30% – the size and timing of the capacity increase is noted on page 59 of the Monitoring Report.

The ACCC's assertion that the car park prices are consistent with monopoly rents:

- Was contradicted by the evidence
- Has potentially reduced car parking revenue at the airports. Due to the perceived independence and authority of the ACCC, the comments are likely to have had a stronger impact than an equivalent amount of newspaper and radio advertising paid for by the airport.
- Contributed to the acceleration of this review - as noted in the Issues Paper.
- Increased inconvenience to passengers who might otherwise have made a different decision based on their opinion of the reasonable value of alternatives.

Future of car park monitoring

The costs of continued monitoring of the car parks at airports substantially exceed the potential benefits.

As has been demonstrated above, the monitoring of incomplete information does not permit any meaningful conclusions to be reached and therefore incurs costs without material benefit. There is no useful policy purpose in continuing it because:

- Airport car park prices per se provide little or no indication of any exercise of market power. The market is competitive and there are broad business constraints on the exercise of market power if it emerged.
- There is no directly observable opportunity cost of domestic car parking land since the entire site between the two domestic terminals at Sydney Airport is used for car parking. It is therefore not viable to independently assess the return on capital being made
- As the ACCC notes on page 64 of the 2009/10 report, the passenger survey results do not correspond to the empirical data. In any event, the ACI passenger survey – the international standard – incorporates passenger surveys of the value-for-money and quality of car parking, and additional monitoring is unnecessary.
- Over time the expansion of internet pre-booking will enable improved tailoring of the product to consumer requirements through increased differentiation of prices across the time of day, day-of-week and season and the provision of car parking within joint products. This will make monitoring of car parking prices both more difficult and even less meaningful.
- If monitoring of land access and car park capacity is to continue, it should take a holistic approach and monitor equally all aspects of land access both on and off-airport, namely - car parking capacity, taxi capacity, rail and bus capacity, and the capacity of the roads leading to and surrounding the airport.

The costs of monitoring will certainly continue to outweigh the benefits whilst the market share remains low. Closer scrutiny of car parking would not be warranted unless the airport's share of the market for passenger access was substantial (for example, 33%).

7.6 Conclusions and recommendations

Price and quality monitoring has been a key feature of the light-handed regime. Sydney Airport supports its improvement and continuation. The recent ACCC Airport Monitoring reports fail to provide useful policy information and contain a large amount of data and commentary which is misleading.

Sydney Airport recommends that:

The publication of the ACI ASQ benchmarking results for passenger service quality, as well as the publication of information on the extent of service level agreements with the airlines and the performance under these agreements. Where appropriate, an auditor or regulator (such as the ACCC) could be asked to ensure that an appropriate system for reporting was in place.

8. Recommendations for future airport regulation

8.1 Light-handed regulation

The National Aviation Policy recognises the benefits to Australia of an open, competitive and innovative aviation market that benefits tourism, trade and consumers – and which connects all Australians to the world, our major cities and our regional communities.

The process of de-regulation, of both airlines and airports, has been a catalyst for and taken place in parallel with increased commercial relationships between airports and airlines. It has delivered to Australia an aviation market that exhibits these features, supported by airports that have similarly promoted competition and innovation. For example, Sydney Airport has:

- Commercial agreements with all scheduled international and domestic airlines
- Invested over $1.8 billion between July 2002 and December 2010, of which 70% was in aeronautical-related facilities
- Passenger service levels have been maintained and improved
- Collaborated with airlines on a range of commercial initiatives.

Sydney Airport recommends that this path of progressive de-regulation is continued, to further promote commercial relationships and a competitive and innovative aviation market. Specifically, Sydney Airport recommends:

- Focused reporting of key financial and service quality information
- A scheduled Productivity Commission review in 10 years, if the Productivity Commission considers that further scheduled reviews are appropriate
- Publication of the international ACI ASQ survey results (replacing the ACCC monitoring of passenger service levels). The ACI ASQ results for each question should be attributed appropriately: to the airport, the airlines, Customs, Immigration and/or AQIS
- Publication of the scope of the service level agreements, and whether the airports and airlines are meeting the commercially agreed targets (replacing the ACCC monitoring of airline service levels)
- Publication of the audited average return on capital earned by the airport since July 2002, calculated on a basis consistent with the commercial agreements (replacing the ACCC monitoring of financial performance)
- Self-publication of car park prices on the website (replacing the ACCC monitoring of car park prices)
- All reporting to be compliant with relevant ISO standards
- To the extent that the ACCC continues to publish any monitoring report, that reporting conforms with monitoring principles to be set out by the Productivity Commission, including that the airports be able to respond to the full draft report with sufficient time to correct errors or unreasonable conclusions – and be able to incorporate within the report a response to any comment
- A framework for governments to address road, rail and bus transport and planning links with the airport to improve competition and consumer welfare
- An estimate of the benefits to economic welfare (including equity) of efficient growth in airport services under the improved regime.

In addition, Sydney Airport recommends that the historical constraints in place at Sydney Airport be reviewed to ensure that the Government's overall growth and distribution objectives are being met, balancing the interests of all stakeholders. This will both attract new airlines and services, for the benefit of the community, and will also ensure that Sydney

Airport is able to meet demand well beyond 2029. In so doing, it will promote the efficient operation and use of Sydney Airport, and will enhance the economy-wide benefits of the airport – consistent with the objectives of the Terms of Reference.

8.2 Service quality monitoring

Sydney Airport believes that, if done competently and professionally, quality of service reporting can be an important tool that enables airports and airlines to improve the performance of their joint service to passengers.

Any service quality reporting should be consistent with the following principles:

- **A focus on passengers' travel experience**. Sydney Airport believes that service quality monitoring should be focussed on the quality of the passengers' end-to-end journey to enable airlines and airports to understand where improvements need to be made.
- **Data collection, treatment and analysis must be methodologically reliable**. The Australian Standard for market opinion and social research (AS:ISO20252) was published by Standards Australia in January 2007 and is internationally recognised as a quality management system to ensure the quality of staff, design, fieldwork, analysis and reporting of all research complies with established professional standards for delivering high quality research outcomes. Any future reporting should be compliant with AS:ISO20252.
- **The regime must incorporate accurate accountabilities**. An effective quality of service reporting regime should accurately inform air passengers and other stakeholders which organisations are responsible for delivering the services provided during each stage of their journey. Clear information about organisational responsibility improves transparency and provides the correct signals to organisations to improve their services.

Sydney Airport believes this service quality reporting is best achieved through:

- Reporting and publication of the results of the ACI ASQ program, which provides information to the airport, airlines and general public about the service offered to passengers by airports. This reporting should be certified as AS:ISO20252 compliant
- As foreshadowed in the National Aviation Policy, any reporting required by airport operators should be accompanied by reporting that covers passenger terminals that are operated by individual airlines as, from a passenger's experience, it is the quality of service experienced, not the ownership arrangements, that are important.[85] The publication of this information should also be complemented by the publication of performance reporting by government service providers such as Customs, AQIS, and Air Services Australia that operate nationally as monopoly service providers at all airports and have a direct impact upon the passenger experience.
- Agreement of collaborative service level agreements between the airports and the airlines which address the priorities of each airline using objective measures
- As part of its commercial and service level agreements, Sydney Airport will continue to have regular engagement and consultation with airlines on priorities and actions so as to strengthen the overall partnership in the operation, development and promotion of the airport
- Publication of the scope of the service level agreements (SLAs) at each airport, whether the airports and airlines are meeting the commercially agreed targets, and the consensus priorities of the airlines.

[85] National Aviation Policy "White Paper", December 2009, p 177

Sydney Airport believes the existing regime fails to provide the information necessary to assist the airports and airlines to improve performance, lacks credibility in its assessment of the airports' contribution to joint service quality, lacks transparency, and should be brought up-to-date and significantly improved.

Airports Council International Airport Service Quality (ACI ASQ) program

As part of its normal business, Sydney Airport commits considerable resources to the Airports Council International Airport Service Quality (ACI ASQ) program. This is a benchmarking program for the global airport industry, and is explained on its website:

ASQ Survey is the world's leading airport customer satisfaction benchmark programme with over 190 airports in more than 50 countries surveying their passengers every month of the year. All airports use the same questionnaire and follow the same methodology. ASQ's highly detailed sample plan tailored to each airport's traffic ensures comparable results.

Each participating airport receives the data from all other participating airports allowing it to identify best practice and to measure its own performance precisely. Excellence in service is not a one-off, it is proven to be the result of continual effort and commitment to providing the best possible service. ASQ helps you understand where to focus that financial and human effort.[86]

It is, in part, through its participation in the ACI ASQ program that Sydney Airport has become aware of the extent of the flaws and shortcomings of the ACCC's approach to quality of service monitoring and reporting. While the ACCC's methodology lacks credibility, the ACI ASQ program is globally recognised as being a valuable management tool to evaluate and improve performance.

Collaborative service level agreements

Sydney Airport is progressively agreeing joint service level targets with each of its airlines – commencing with many of the largest airlines. The purpose of these agreements is to help the airport and the airlines to identify service priorities and improve their joint service levels. The different priorities and expectations of different airlines are reflected in the agreements.

Sydney Airport believes that audited self-reporting of the extent of these service level agreements and whether targets have been achieved will provide the most useful information on the airports conduct towards the airlines.

In addition, Sydney Airport will continue to conduct surveys of airlines to understand their expectations and priorities. Sydney Airport would support publication on an aggregated level of the top five priorities of the airlines.

Sydney Airport would be happy to see periodic independent audits of the information it proposes publishing.

8.3 Financial monitoring

Sydney Airport believes the current financial monitoring is unnecessary, uninformative and misleading.

[86] ACI ASQ website: http://www.airportservicequality.aero/content/survey.html

The best assessment of appropriate charges is made during the negotiation of the commercial agreements – not several years after the charges are agreed. During these negotiations both the airlines and airports have available audited information on the current costs of the airport. For example, Sydney Airport continues to employ the activity-based costing methodology (based on assumptions determined by the ACCC in 2001) which is audited and the outputs provided to the airlines. Whilst the airport and the airlines will have different expectations about the future, the consultation process includes the sharing of information about future expectations to narrow this gap.

The airlines are both well-informed and have increasing countervailing power. With commercial agreements now demonstrated to be working, arguably there should be no need for financial monitoring in the future.

However, whilst there may be no need for ongoing financial monitoring, Sydney Airport would recommend the audited self-reporting of the average return on capital earned by the airports since July 2002 (immediately following the commencement of the light-handed regulatory regime), calculated on a basis consistent with the commercial agreements. The long-term average return on capital incorporates all the relevant information on investment, costs, prices and volume growth, and is the single figure which can provide insight into whether an airport is earning excessive returns.

If, despite the evidence that the costs of financial monitoring have exceeded the benefits, ACCC financial monitoring is to continue, then Sydney Airports recommends that:

- The asset values used should be consistent with the commercial agreements (for example, indexed for inflation) and appropriately adjusted for 'lost' and 'discovered' assets.
- The average return on capital since 2002/3 should be reported instead of the annual return on capital
- There should be an explicit requirement that evidence of monopoly rents requires, as a minimum, that the average return on capital since 2002/03 is significantly higher than the appropriate WACC
- The monitoring report should not include any information which can be easily misinterpreted, or any inferences drawn on the overall performance from partial indicators.

8.4 Car parking monitoring

As demonstrated in Section 7.5, the costs of continued monitoring of the car parks substantially exceed the potential benefits.

The monitoring of incomplete information does not permit any meaningful conclusions to be reached, and therefore provides little benefit as evidenced by the following:

- Car park prices *per se* provide little or no indication of any exercise of market power. Since the car park prices at Sydney Airport are in the public domain, any abuse which would be detectable by the monitoring reports would have long since been reported in the media and brought to political attention.
- Over time the expansion of internet pre-booking will enable improved tailoring of the product to consumer requirements through increased differentiation of prices across the time of day, day-of-week and season and the provision of car parking within joint

products. This will make monitoring of car parking prices both more difficult and even less meaningful.

- Car parking returns are meaningless in the absence of definitive costs of capital. Since the location rents are observably different even within the car parks, and since scarcity of land at Sydney Airport and in Sydney more generally is causing rapid increases in land value, definitive costs of capital that are not implied from car parking returns are impractical.
- As the ACCC notes on page 64 of the 2009/10 report, the passenger survey results do not correspond to the empirical data. In any event, the ACI passenger survey – the international standard – incorporates car parking, and additional monitoring is unnecessary.
- Whilst monitoring of land access (including the capacity of the car parks) is arguably more fruitful, the evidence to date is that the information available is too incomplete and has as a result been misinterpreted by the ACCC. It is likely that this misinterpretation will continue. Hence continued monitoring of land access and car parking capacity carries greater costs than benefits.
- If monitoring of land access and car park capacity is to continue, it should take a holistic approach and monitor equally all aspects of land access both on and off-airport: car parking capacity; taxi capacity; rail and bus capacity; and the capacity of the roads leading to and surrounding the airport.

8.5 Operational regulations

Sydney Airport is Australia's premier international airport and is fundamental to the nation's ability to generate export income and economic growth.

Whilst the *Master Plan 2009* demonstrates that Sydney Airport is able to meet demand until at least 2029, it is in the interests of Australia that the most efficient use is made of the nation's most important international gateway. Sydney Airport recommends that the artificial constraints in place at Sydney Airport be reviewed to ensure that the Government's overall objectives are being met, balancing the interests of all stakeholders. This will both attract new airlines and services, for the benefit of the community, and will also ensure that Sydney Airport is able to meet demand well beyond 2029.

The redesign of operational regulations and practices based on international best practice in the medium term and encouraging more appropriate use of the constrained facilities will require a flexible pricing regime, a responsible charging policy that has appropriate regard to correct pricing signals, and strong commercial relationships with airlines.

Appendix A Sydney Airport's response to the Terms of Reference

The table below provides a cross-reference between each point in the Terms of Reference and the chapters or sections in this submission in which it is addressed.

Bullet	Terms of Reference text	Submission section
1 (1)	The Commission is to report on the appropriate economic regulation … in … promoting the economically efficient and timely operation and use of airports	2.6, 3
1 (1)	The Commission is to report on the appropriate economic regulation … in … promoting the economically efficient and timely investment in airports	2.8, 4.5-4.6
1 (2)	The Commission is to report on the appropriate economic regulation … minimising unnecessary compliance costs	7.2, 7.5, 8.1
1 (3)	The Commission is to report on the appropriate economic regulation … facilitating commercially negotiated outcomes in airport operations	1.1, 2.7, 4, A3
1	The Commission is to report on … the effectiveness of the price and quality of service monitoring	7, A7-9
3 (1)	The Commission is to examine aeronautical services and facilities provided by the airport operators	4
3 (2)	The Commission is to examine passenger-related aeronautical services and facilities provided by major airline tenants	8.2
3 (3)	The Commission is to examine the provision and quality of land transport facilities providing access to the airports	5, 6, A4-6
4	… the Commission is to examine the economy-wide costs and benefits	3, A11
4	… the Commission is to examine distributional impacts of the regime	4.5
4	It should also seek to provide international comparisons of the performance of the airport operators	-
5 (1)	… whether the existing regime is effective in appropriately deterring potential abuses of market power	2, 4.8, A2
5 (2)	… whether the existing range of remedies is effective in dealing with potential and suspected abuses of market power	2, 4.3
5 (3)	… the effectiveness of the monitoring regime conducted by the ACCC, including the methodology used and the adequacy of the information collected	7, A7-9
5 (4)	… whether the current regime impacts on the ability of airports to price, operate and invest in airport infrastructure in an efficient and timely manner	7
5 (5)	… whether the coverage of the current regime is appropriate	N/A

Bullet	Terms of Reference text	Submission section
5 (6)	… any improvements or enhancements that could be made to the existing regime	8
5 (7)	… the appropriate future role of the regime	2, 8
5 (8)	… the adequacy and arrangements for the control of planning, operation and service quality monitoring of land transport access to major airports	5
5 (9)	… whether existing arrangements for the planning and operation of land transport linkages to the airports are effective	5, A4
6	To the extent applicable, the Commission is to have regard to the ACCC Airport Monitoring Report	7
6 (1)	To the extent applicable, the Commission is to have regard to … the matters raised by the ACCC … such as … the quality of service at major Australian airports	4.7, 7.4
6 (2)	To the extent applicable, the Commission is to have regard to … the matters raised by the ACCC … such as … landside access to airport terminals such as car parking and its alternatives, and the cost and quality of car parking facilities	6, 7.5, A5-6
6 (3)	To the extent applicable, the Commission is to have regard to … the matters raised by the ACCC … such as … the extent to which monitored airports can act strategically to raise costs of on-airport car parking by controlling the conditions of landside access to terminal facilities	6.2, A5

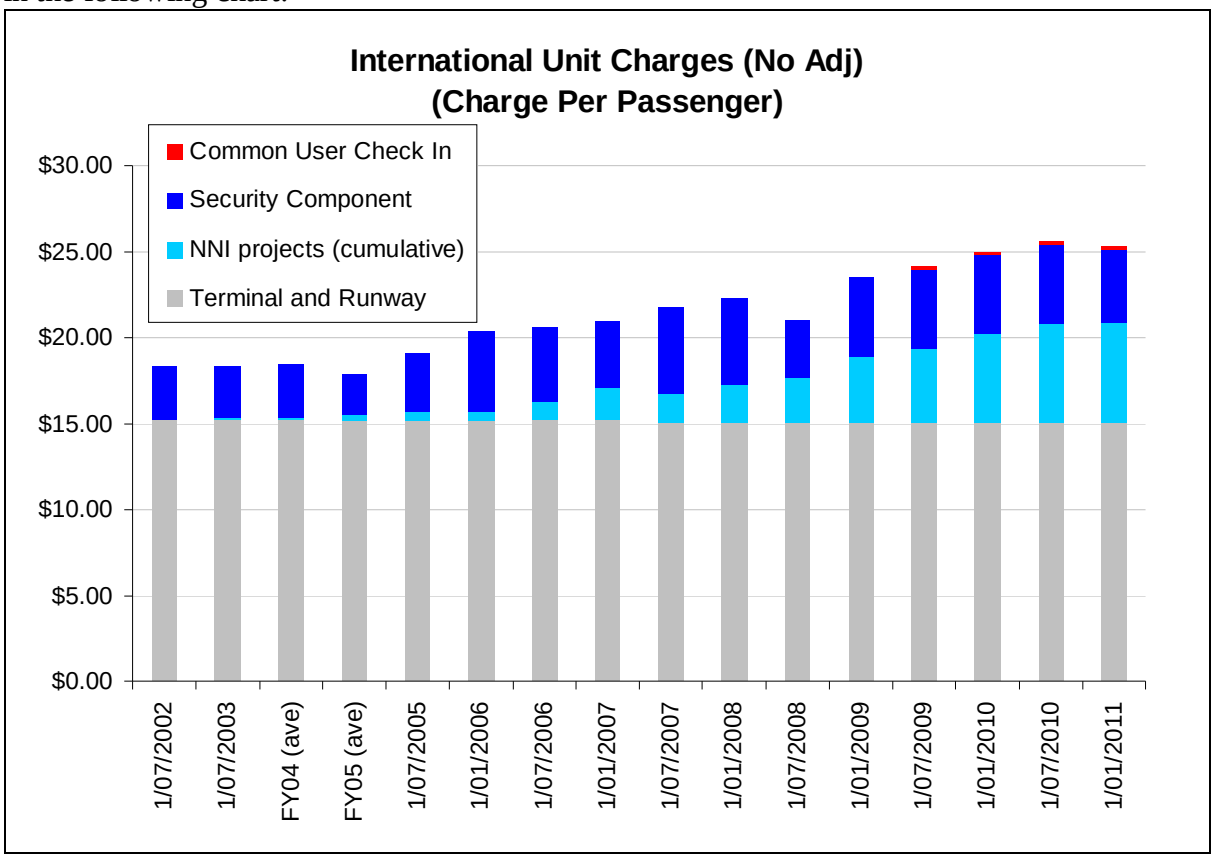
Appendix B History of Aeronautical Charges

B1 International Passenger Services

Sydney Airport's current charges levied for international services are as established by the ACCC in its May 2001 pricing decision and the subsequent August 2001 decision to convert international charges to a single passenger based charge, varied only to:

Recover the cost of new investment in aeronautical facilities as agreed with airlines in consultative processes since 1 July 2002, including government-mandated safety changes as well as both CUTE and GPPCA
Include a price reduction negotiated by airlines in June 2007; and
Recover the cost of providing security services to meet Government-mandated security obligations, with charges fluctuating over time to reconcile actual costs incurred with revenue collected.

Movements in the International Passenger Services Charge between 2002 and now are shown in the following chart.

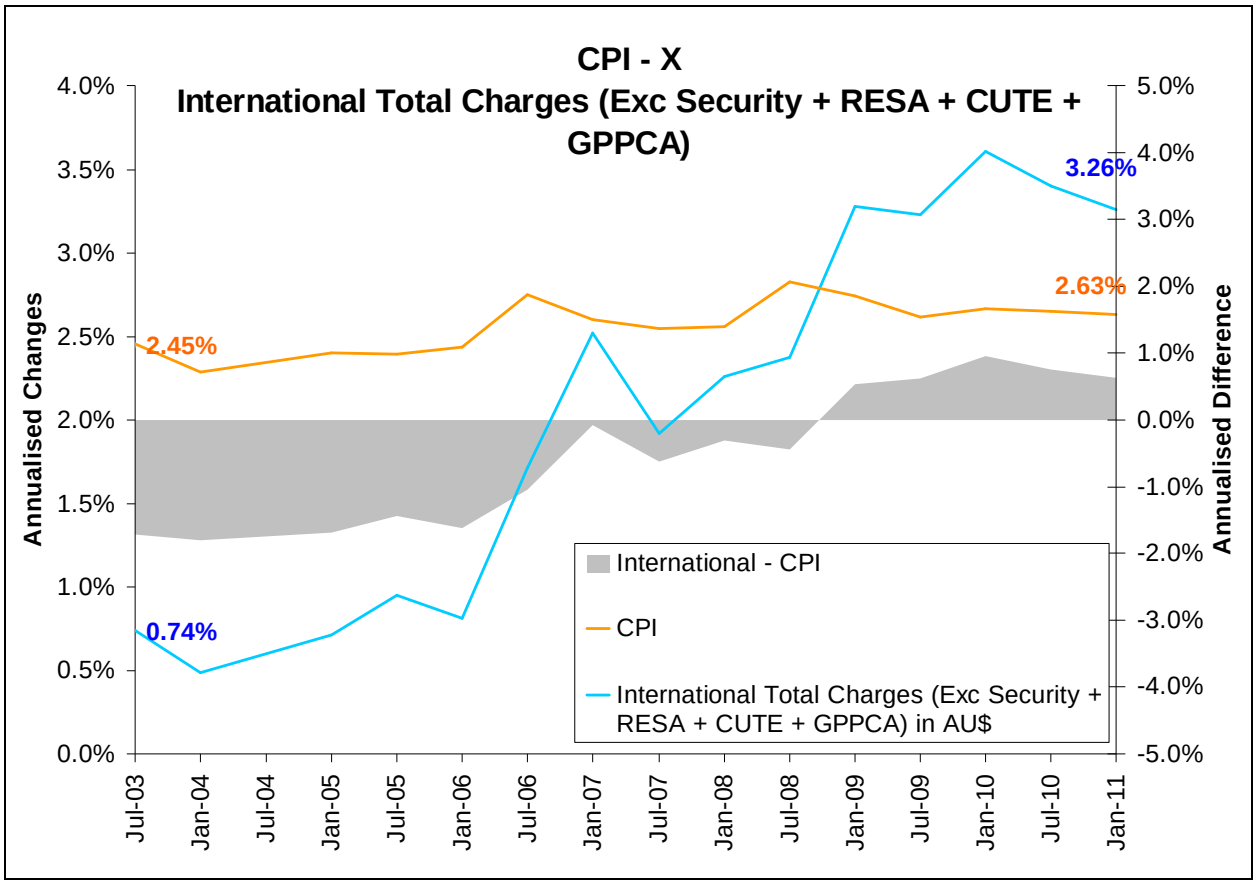


Source: Sydney Airport analysis

The following chart shows the movements in Sydney Airport's charges levied for use of international facilities since the introduction of light-handed regulation, excluding government mandated security, regulatory compliance and capital recovery charges relating to airline cost transfer[87]. As can be seen, underlying headline charges have increased by

[87] Cost transfer and regulatory compliance capital expenditure include RESA $100m $0.51 per passenger, and international only include $0.19 per passenger for CUTE (Common User Terminal Equipment) services and

CPI+0.6%. This reflects cost increases associated with inflation[88], investment and increased activity levels, largely offset by increased passenger volumes, but doesn't include any discounts incorporated within commercial agreements.



Source: ABS (Index Numbers; All Groups; Sydney), Sydney Airport Analysis

The international fees charged by Sydney Airport are small compared to the other taxes, charges and levies included in an average airfare. The current published fees mean that international airlines pay $26.02 (excluding GST) for each arriving and departing international passenger. There is currently no charge for infants, transit and international-to-international transfer passengers, although it is common for charges to apply for international-to-international transfer passengers at other airports. The charge includes $4.20 (excluding GST) for government mandated security requirements such as passenger screening and checked bag screening.

The fees are for the use of infrastructure and facilities such as:

Runways, taxiways, airfield lighting
Passenger terminals (including baggage handling and flight information systems)
Shared airline equipment at check-in counters and aircraft gates
Passenger and airfield safety and security systems
Aerobridges.

$0.37 for the recovery of $26m capital investment in Group Power and Preconditioned Air that represent a net cost reduction to airline operators.

[88] Note Sydney Airport charges are based on a real WACC applied to an indexed asset base, and as a result inflation affects both operating costs and capital costs

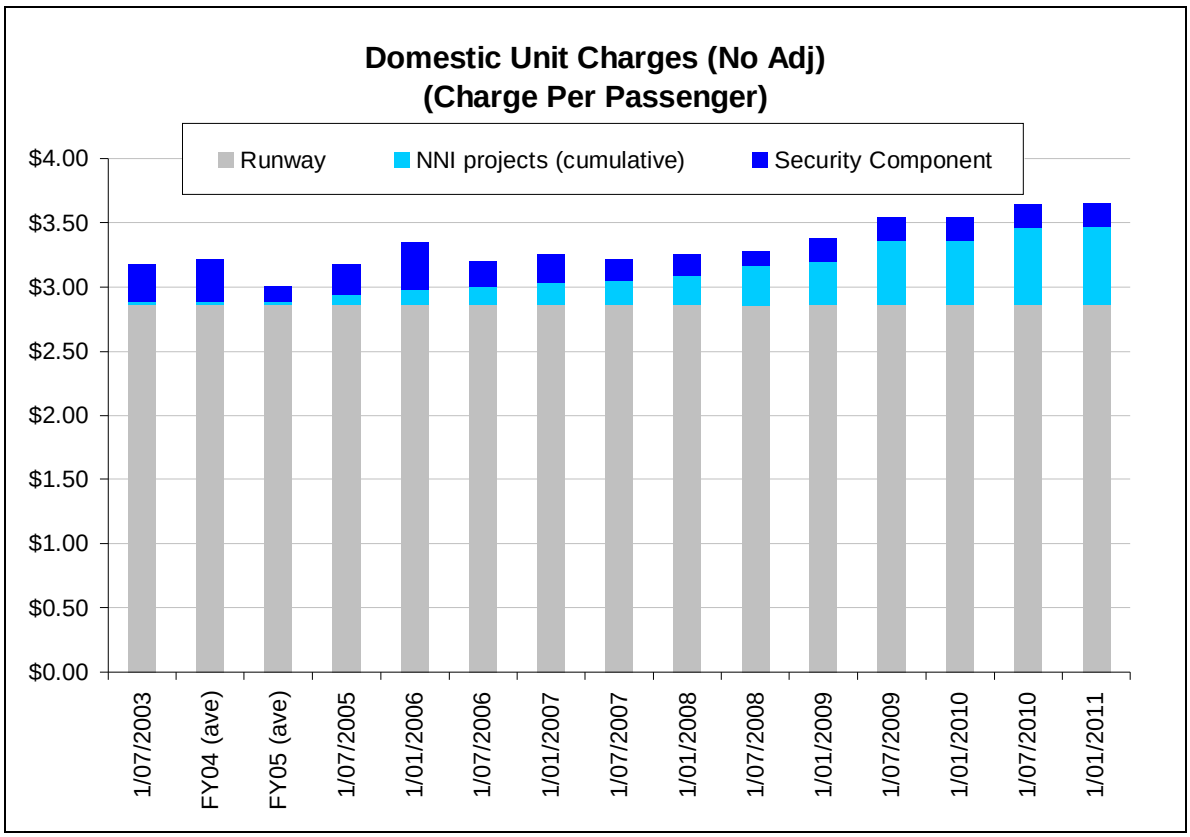
Sydney Airport's fee represents about 2% of a typical return economy airfare to London. In comparison, the Australian Government imposes a Passenger Movement Charge (PMC) of $47 for each departing international passenger and some airlines[89] impose a fuel surcharge of $190 for one-way tickets to destinations in the UK and Europe.

Domestic Airside Charges

Similarly, Sydney Airport's current charges levied for domestic services are as established by the ACCC in its May 2001 pricing decision, varied only to:

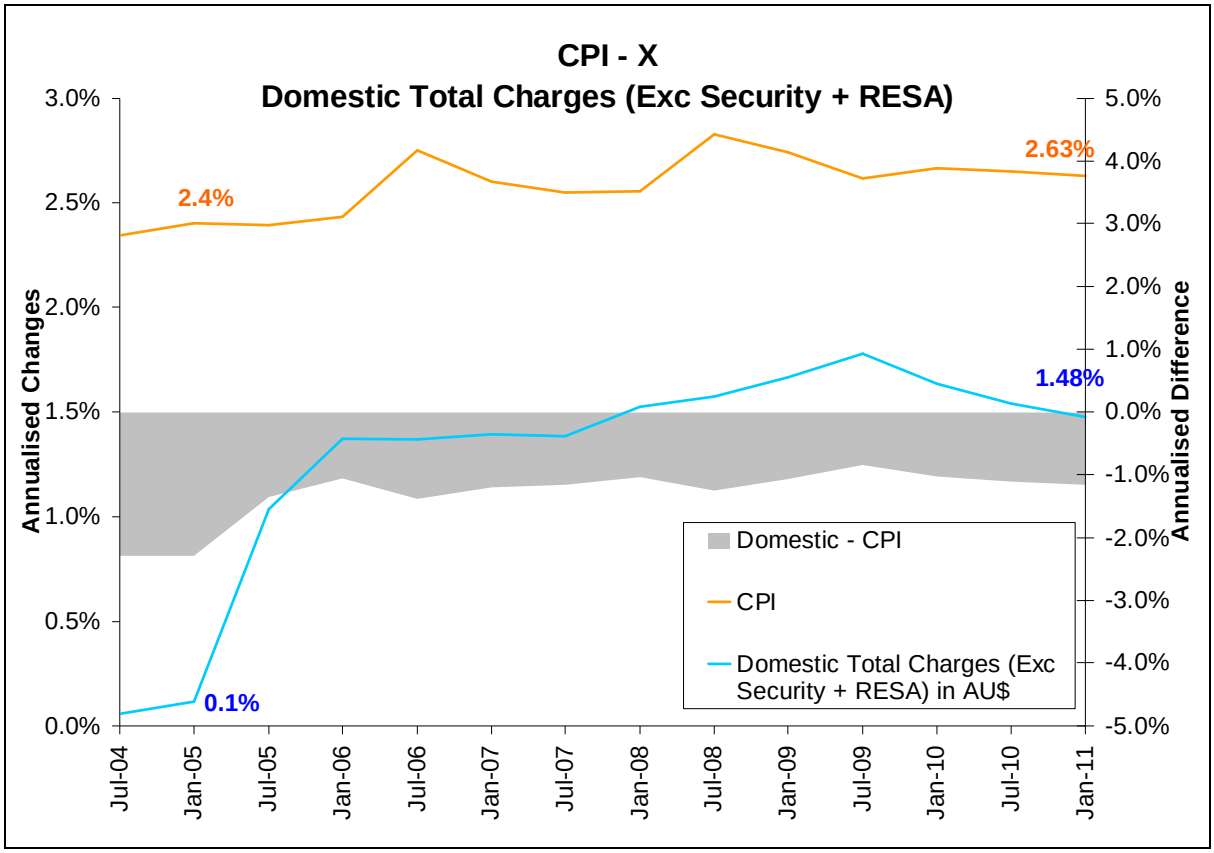
Convert MTOW charges to a passenger basis;
Recover the cost of new investment in aeronautical facilities as agreed with airlines in consultative processes since 1 July 2003
Agreement with certain domestic airlines to charge on an aircraft MTOW basis
Recover the cost of providing security services to meet Government-mandated security obligations, with charges fluctuating over time to reconcile actual costs incurred with revenue collected.

The following chart shows the movements in Sydney Airport's charges levied for use of airside facilities by domestic passenger services since the introduction of light-handed regulation. Underlying headline charges have increased by CPI-1.1%.



Source: Sydney Airport analysis

[89] Qantas Airways announcement to increase fuel surcharge, 9 March 2011



Source: ABS (Index Numbers; All Groups; Sydney), Sydney Airport Analysis

Structure of Aeronautical Charges

International and domestic runway and airfield charges were established by the ACCC on a tonnage (maximum take-off weight) basis in 2001. A move to a per passenger basis for international carriers was approved by ACCC in August of that year. Following the ending of formal price controls, domestic charges were similarly moved to a per passenger basis in July 2003.

Sydney Airport considered that passenger-based charges represented a superior basis of charging to maximum take-off weight charges. Passenger based charges better reflect the underlying driver of airport demand, provide for risk-sharing between airlines and airports as aeronautical charges are linked to passengers on board, promote better runway utilisation through removing the disincentive for airlines to use larger aircraft (as tonnage based charges disadvantage larger aircraft based on the relationship of passenger capacity to aircraft weight).

Similarly the International Air Transport Association (IATA) position paper (July 2010[90]) argues that airport charges should be levied on a per passenger basis, citing the benefits of passenger based airport charges including accountability and transparency through increasing the visibility to passengers of the charges that are paying for airport services and encouraging greater airport cost efficiency; sharing of the risks and benefits of changes in passenger demand between airlines and airports; and financial benefits to airlines by moving airport charges from their direct cost base.

[90] International Air Transport Association, July 2010. Passenger Based Airport Charges. IATA, Geneva. http://www.iata.org/whatwedo/airport-ans/charges/Documents/Passenger-based-airport-charges-Jul10.pdf

Following the declaration of airside services in December 2005, Virgin Blue referred the manner in which charges for domestic airfield services were levied to arbitration. A commercial resolution was achieved prior to the arbitration being heard. Part of this commercial agreement included the reversion to runway charges based on maximum take-off weight, but at a new commercially agreed rate (Sydney Airport, 2007[91]). A number of other domestic airlines also commercially negotiated runway charges based on maximum take-off weight.

An advantage of the light handed regime will be the constant adaptation to changing business models. With its increased mix of aircraft types[92], it is possible that Virgin Blue may opt to revert to passenger based charges.

Other international aeronautical charges include a time based check-in and service counter charge which has increased in-line with inflation, while a time based aircraft parking charge has not changed since 2001.

The Productivity Commission recommendations in 2002 and 2006 included a statement that:

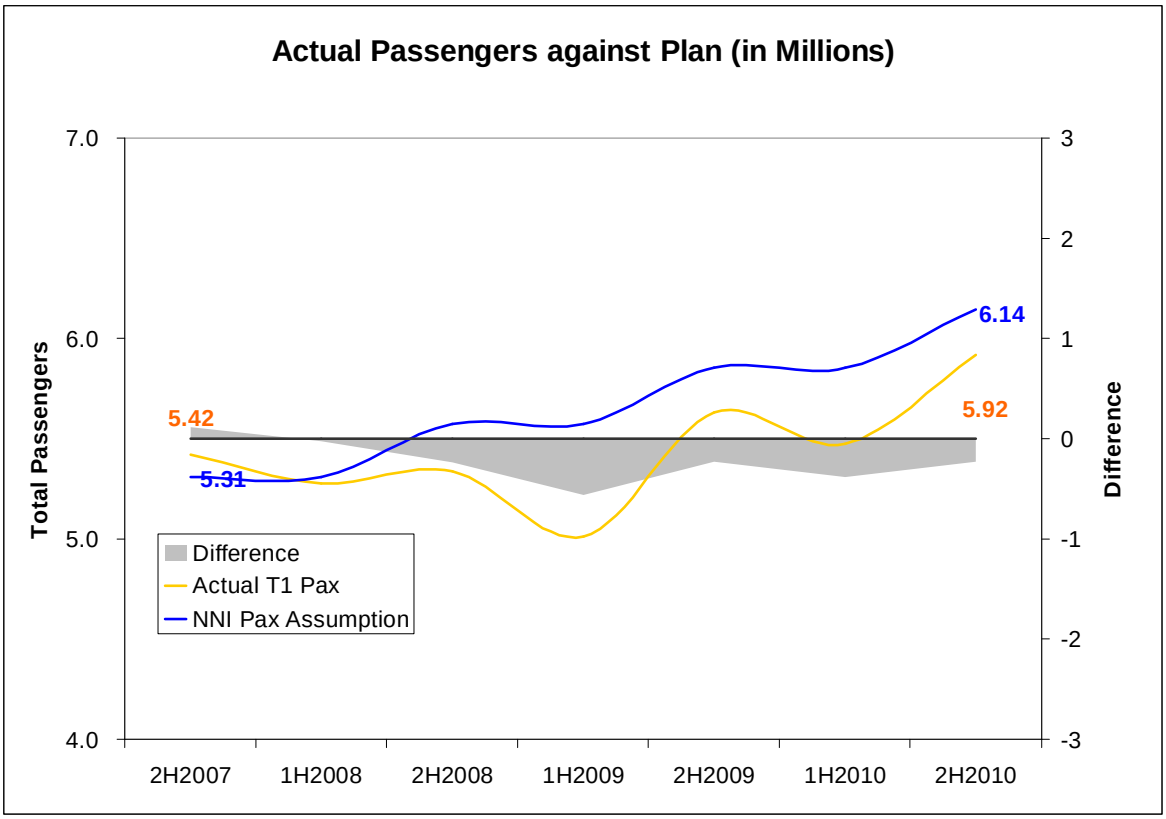
...at a significantly capacity constrained airport, efficient peak/off-peak prices may generate revenues in excess of production costs.

The principles express support for such measures provided that any additional funding thereby generated is applied to the creation of additional capacity or undertaking necessary infrastructure improvements. This principle was established in response to the potential situation where peak charges might need to be increased in order to influence demand patterns by more than could be offset by off-peak reductions. However, given the entrenched opposition of most airlines to such an approach, Sydney Airport has not introduced demand management pricing to date. Nonetheless, as part of multifaceted commercial agreements Sydney Airport has negotiated multi-part pricing arrangements with some airlines that promote more efficient use of off-peak capacity.

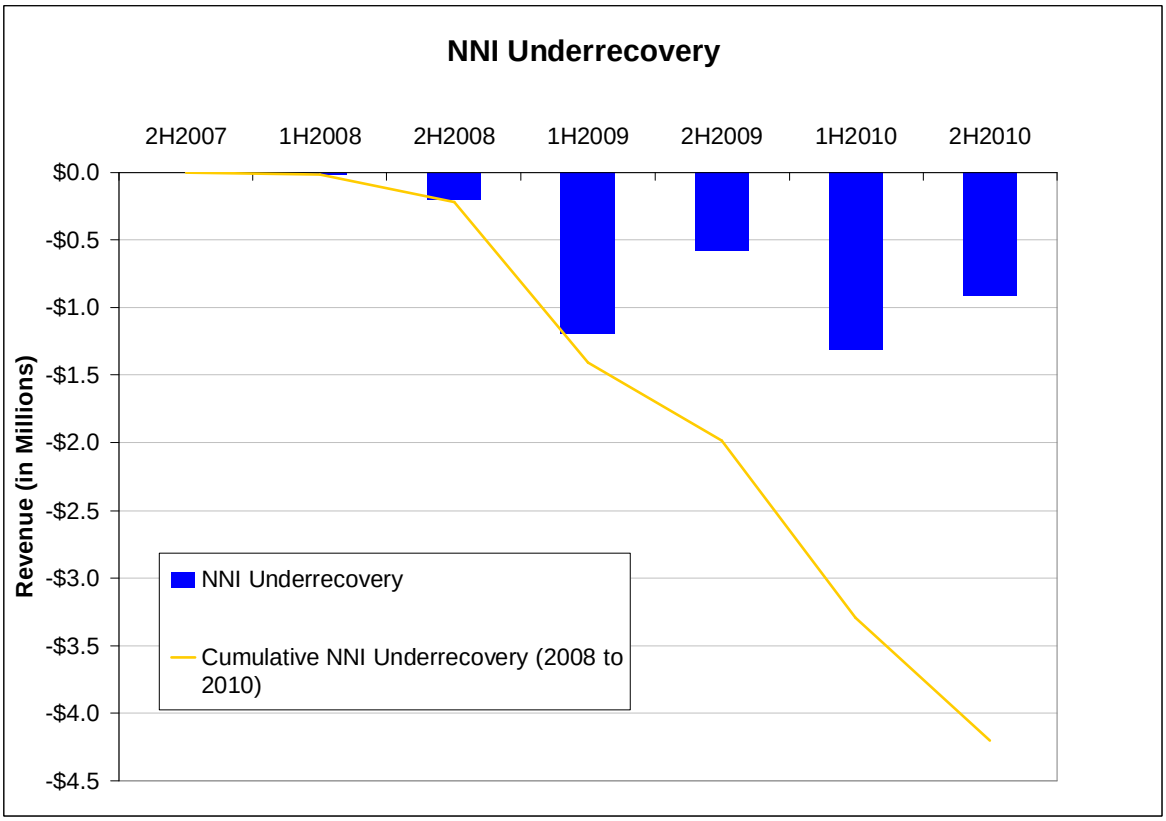
NNI passenger volume risk

Following the move to commercially agreed parameters in the 2007 pricing agreement Sydney Airport agreed a passenger volume forecast for 2008-12 which would be used for the pricing of new investments. Due to slowing economic activity the resulting passenger traffic fell short of the forecast, and Sydney Airport has structurally under recovered in this second commercial period.

[91] Sydney Airport Corporation Limited, April 2007. Media Release, Commercial Agreement Reached with Virgin Blue. Sydney Airport Corporation Ltd, Sydney.
[92] Virgin Blue ASX release – 'Advancing the Game Changing Program' 23 February 2011



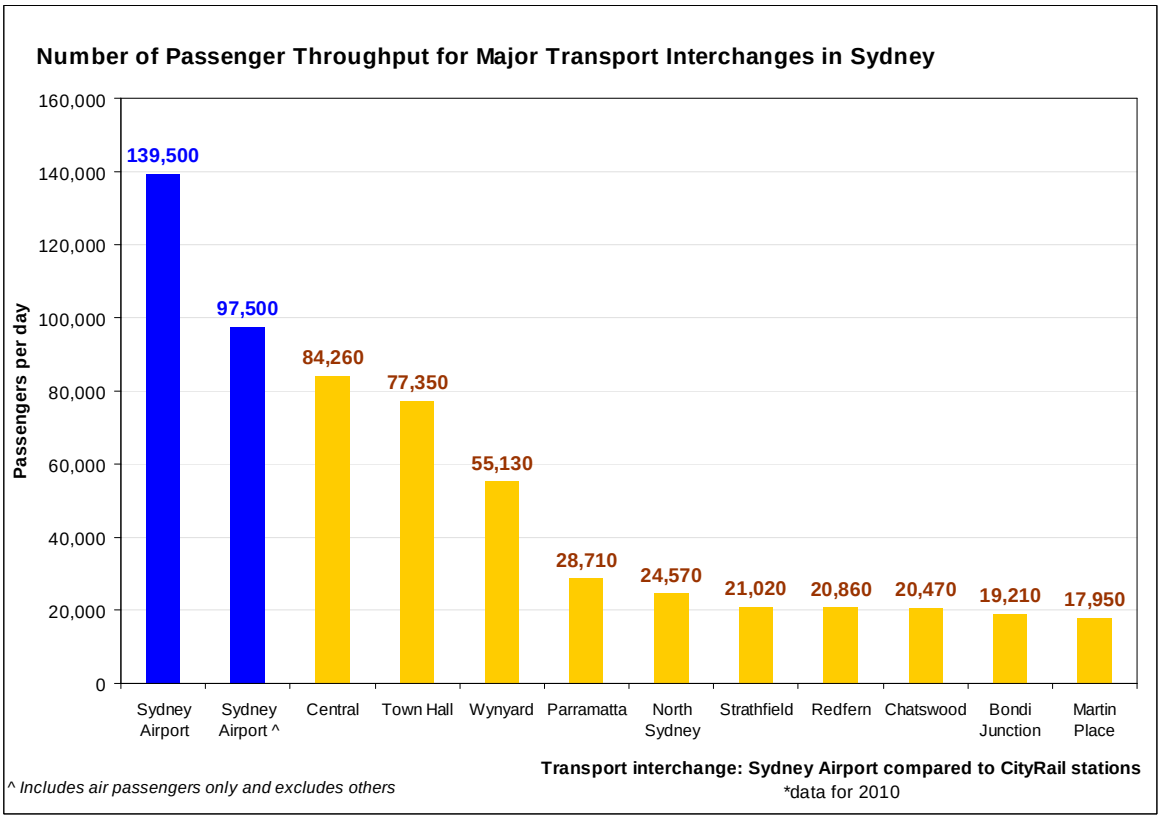
Source: Sydney Airport Analysis



Source: Sydney Airport Analysis

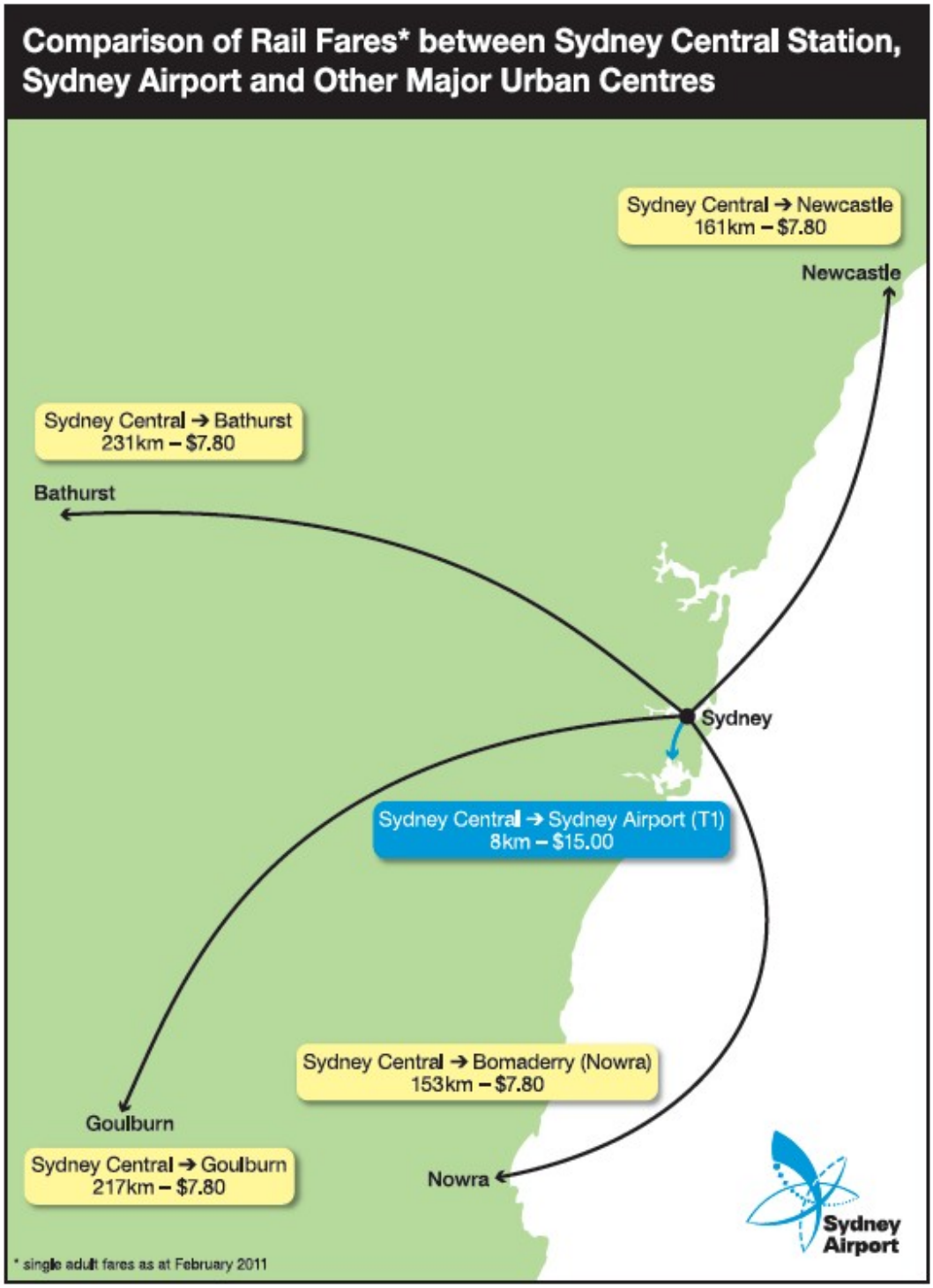
Appendix C Land transport information

3.1 Passenger Throughput for Major Transport Interchanges in Sydney

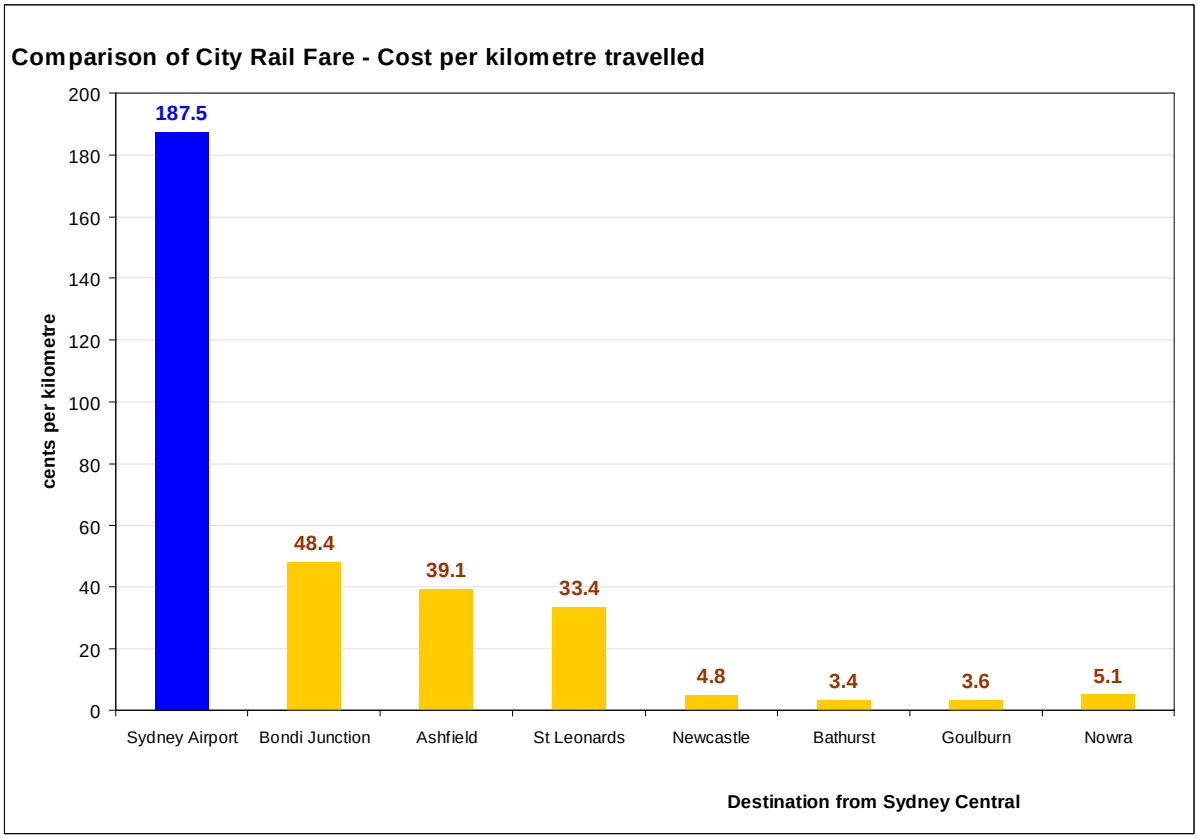


Source: Sydney Airport analysis (Sydney Airport location data 2010, other locations 2009 data)

3.2 Comparison of CityRail fares between Sydney Central Station, Sydney Airport and Other Major Urban centres



3.3 Comparison of CityRail Fares (cost per kilometre)



Source: Sydney Airport analysis

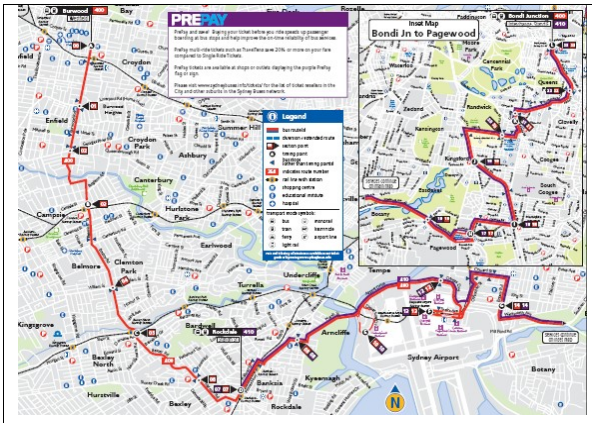
3.4 Forecast Increase in Rail Patronage

Year	Airport Train Stations		Increase in rail journeys following fare reform
	Business as Usual Patronage (millions)	Patronage following fare reform (millions)	
2010/11	4.17	5.23	+ 1.1 million per annum (3,013 per day)
2015/16	4.90	6.49	+ 1.6 million per annum (4,384 per day)
2020/21	6.01	8.15	+ 2.4 million per annum (6,575 per day)
2025/26	7.38	10.22	+ 2.8 million per annum (7,671 per day)
2029/30	9.06	12.83	+ 3.8 million per annum (10,410 per day)

3.5 Comparison of the number of bus routes serving Sydney Airport with other urban centres across Sydney

Urban Centre	Number of people employed in the urban centre	Number of bus routes
North Sydney	49,000 employees	62
Macquarie Park	32,200 employees and 33,000 Uni students	24
St Leonards	25,100 employees	28
Chatswood	23,000 employees	32
Hurstville	12,900 employees	18
Bankstown	10,200 employees	25
Bondi Junction	9,800 employees	28
Randwick	9,800 employees and 42,360 Uni students	20
Burwood	9,500 employees	22
Kogarah	9,500 employees	14
Sydney Airport	**~ 140,000 people per day (including 97,500 passengers, 30,000 meeter/greeters and 12,000 employees)**	**1**

3.6 **Comparison of the number of bus routes serving Sydney Airport with other major airports in Britain**

<table>
<tr>
<td> 
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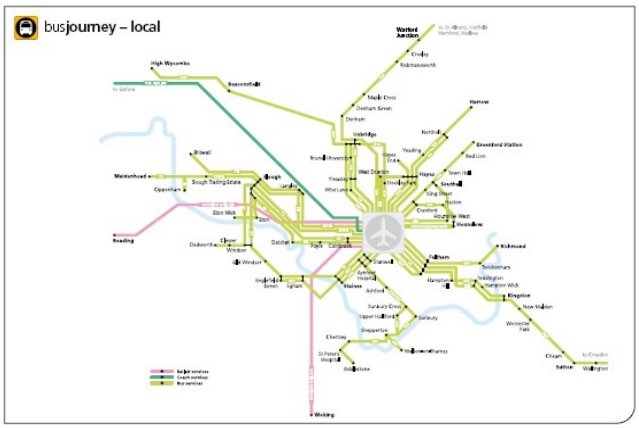
<td> 
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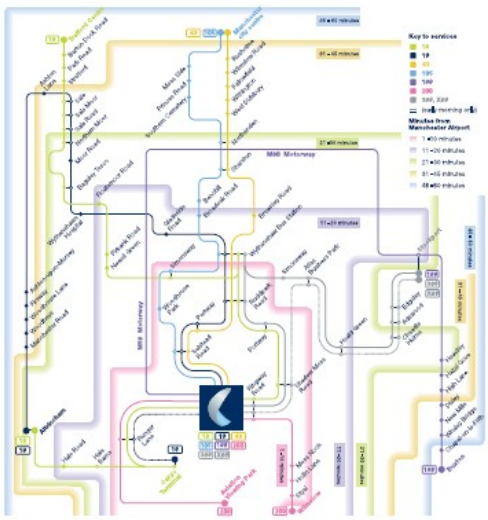
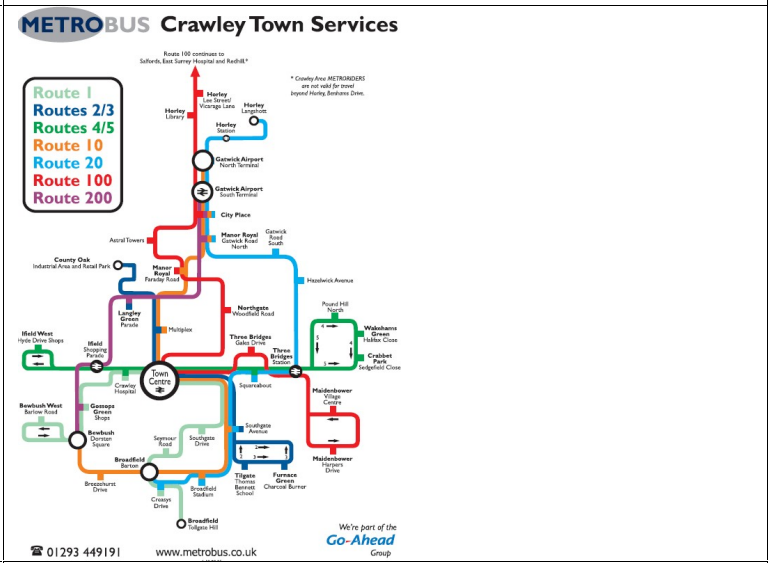
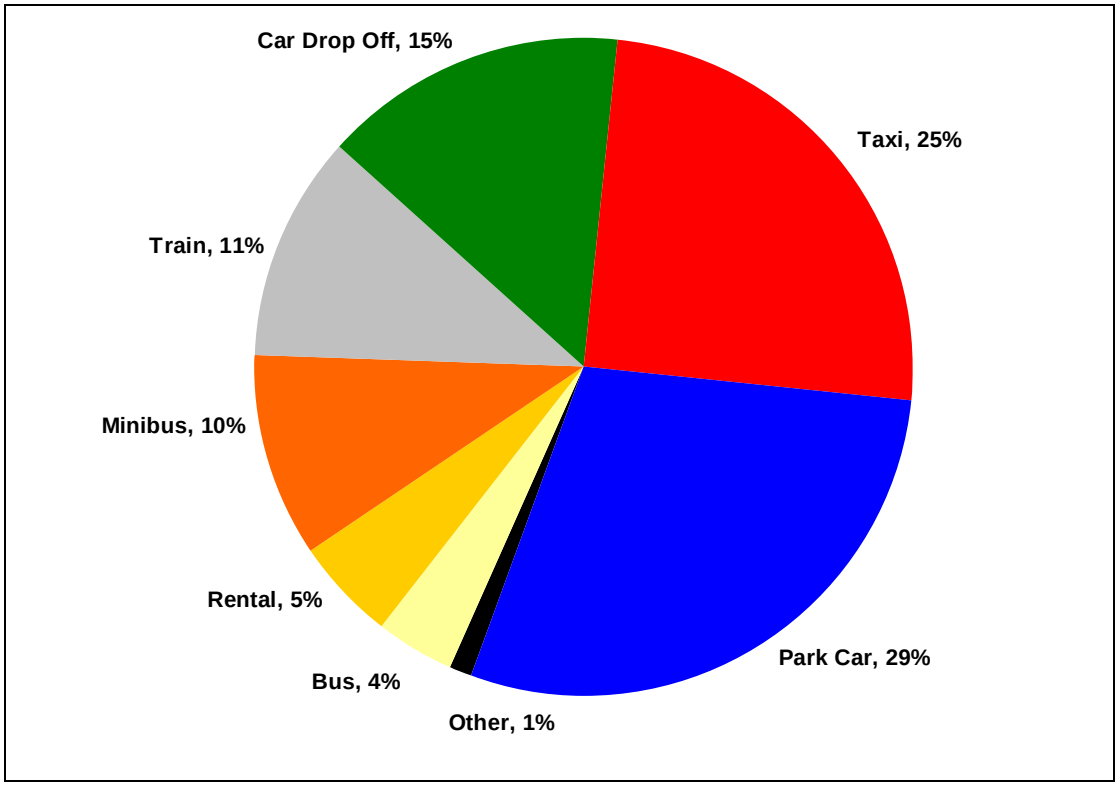
<tr>
<td>Public bus routes serving Sydney Airport
97,400 passengers per day and 12,000 on-airport workers
1 bus route services the airport passenger terminals (note the 410 service does <u>not</u> stop at Sydney Airport’s passenger terminals)</td>
<td>Public bus routes serving Heathrow Airport
183,000 passengers per day and 72,000 on-airport workers
29 bus routes service the airport passenger terminals</td>
</tr>
<tr>
<td>  </td>
<td> 
</td>
</tr>
<tr>
<td>Public bus routes serving Manchester Airport
60,000 passengers per day and 19,000 on-airport workers
8 bus routes service the airport passenger terminals</td>
<td>Public bus routes serving Gatwick Airport
90,000 passengers per day and 23,000 on-airport workers
bus routes service the airport passenger terminals</td>
</tr>
</table>

3.7 **New Metrobus services stop short of Sydney Airport**

3.8 Existing mode share proportions for accessing Sydney Airport



Source: Sydney Airport 2006, Airport Ground Travel Plan (AGTP)
Note: 'park car' includes off-airport parking and mode includes employees (airport and non-airport based), passengers and meeter/greeters

3.9 COAG's national criteria for future strategic planning of capital cities

COAG's nine national criteria for future strategic planning of capital cities aim to ensure capital cities have strong, transparent and long-term plans in place to manage population and economic growth; plans which will address climate change, improve housing affordability and tackle urban congestion. The following criteria are directly relevant to nationally significant economic infrastructure such as Australia's capital city airports and ports.

Relevant National Criteria for Future Strategic Planning of Capital Cities

Capital city strategic planning systems should:

— Be integrated across functions, including land-use and transport planning, economic and infrastructure development, environmental assessment and urban development

— Provide for a consistent hierarchy of future oriented and publicly available plans, including:
- Long term (for example, 15-30 year) integrated strategic plans,
- Medium term (for example, 5-15 year) prioritised infrastructure and land-use plans, and
- Near term prioritised infrastructure project pipeline backed by appropriately detailed project plans;

— Provide for nationally-significant economic infrastructure (both new and upgrade of existing) including:
- Transport corridors,
- International gateways,
- Intermodal connections,

— Address nationally-significant policy issues including:
- Productivity and global competitiveness,
- Efficient development and use of existing and new infrastructure and other public assets,
- Connectivity of people to jobs and businesses to markets,

— Provide effective implementation arrangements and supporting mechanisms, including clear accountabilities, timelines and appropriate performance measures.

Appendix D Operational Constraints at the largest 50 global and largest four Australian airports[93]

Additional information provided with reference to Boeing Commercial Aircraft database on airports with noise and emissions restrictions[94]

Unconstrained airports

Code	Airport	Curfew	Artificial movement cap	Preferential runway use	Ring fencing
BKK	Bangkok	-	-	-	-
DXB	Dubai	-	-	-	-
STN	London Stansted	-	-	-	-
KUL	Kuala Lumpur	-	-	-	-
BOM	Mumbai	-	-	-	-
IST	Istanbul	-	-	-	-
CGK	Jakarta	-	-	-	-

Summary – Preferential Runway use airports

Code	Airport	Curfew	Artificial movement cap	Preferential runway use	Ring fencing
ATL	Atlanta	-	-	✓	-
LAX	Los Angeles	-	-	✓	-
DFW	Dallas / Ft Worth	-	-	✓	-
DEN	Denver	-	-	✓	-
HGK	Hong Kong	-	-	✓	-
IAH	Houston	-	-	✓	-
PHX	Phoenix	-	-	✓	-
SIN	Singapore	-	-	✓	-
MCO	Orlando	-	-	✓	-
DTW	Detroit	-	-	✓	-
SFO	San Francisco	-	-	✓	-
MIA	Miami	-	-	✓	-
CLT	Charlotte	-	-	✓	-
BCN	Barcelona	-	-	✓	-
PHL	Philadelphia	-	-	✓	-
SEA	Seattle	-	-	✓	-
MEX	Mexico City	-	-	✓	-
IAD	Washington	-	-	✓	-
MEL	Melbourne	-	-	✓	-
BNE	Brisbane	-	-	✓	-
PER	Perth	-	-	✓	-
ICN	Seoul Incheon	-	-	✓	-
AKL	Auckland	-	-	✓	-

[93] L.E.K. Consulting Pty Ltd report for Sydney Airport Corporation, 28 June 2008: Artificial Constraints at the Top 50 Airports.
[94] Source: http://www.boeing.com/commercial/noise/list.html

Summary – Operational Constrained Airports

Code	Airport	Curfew	Artificial movement cap	Preferential runway use	Ring fencing
LHR	London Heathrow	✓	Noise quota	✓	-
CDG	Paris Charles de Gaulle	✓	Noise quota	✓	✓
FRA	Frankfurt	✓	Noise quota	✓	-
MAD	Madrid	✓	-	✓	-
AMS	Amsterdam	✓	✓ Noise quota	✓	-
LGW	London Gatwick	✓	Noise quota	-	-
MSP	Minneapolis St. Paul	✓	Noise quota	✓	-
MUC	Munich	✓	Noise quota	✓	-
LGA	New York La Guardia	Voluntary 2400 to 0700-	✓	✓	-
HND	Tokyo Haneda	-	-	✓	-
YYZ	Toronto	✓	✓ Noise quota	✓	-
ORD	Chicago O'Hare	-	✓	✓	-
JFK	New York JFK	-	✓	✓	-
PEK	Beijing	✓	✓	-	-
CAN	Guangzhou	-	✓	-	-
PVG	Shangai Pudong	-	✓	-	-
EWR	New York Newark	-	✓	-	-
LAS	Las Vegas	✓	-	✓	-
FCO	Rome	✓	-	✓	-
BOS	Boston	✓	-	✓	-
MXP	Milan Malpensa	✓	-	✓	

✓ = soft curfew (passenger movements allowed under certain conditions)

Summary – highly constrained airports

Code	Airport	Curfew	Artificial movement cap	Preferential runway use	Ring fencing
SYD	Sydney	✓✓	✓	✓	✓
NRT	Tokyo Narita	✓✓	-	-	-
ORY	Paris Orly	✓✓	✓	✓	✓

✓ ✓= hard curfew (no passenger movements allowed)

Appendix E ACI ASQ survey areas

International	Domestic
Overall satisfaction	
Overall satisfaction – all passengers	Overall satisfaction – all passengers
Overall satisfaction – business passengers	Overall satisfaction – business passengers
Overall satisfaction – leisure passengers	Overall satisfaction – leisure passengers
Access / navigation and connectivity	
Ground transport to/from airport	Ground transport to/from airport
Availability of parking facilities	Availability of parking facilities
Value for money of parking facilities	Value for money of parking facilities
Ease of finding your way through the airport	Ease of finding your way through the airport
Flight information screens	Flight information screens
Walking distance inside the terminal	Walking distance inside the terminal
Ease of making connections with other flights	Ease of making connections with other flights
Airport services / facilities	
Availability of baggage carts	Availability of baggage carts
Courtesy and helpfulness of airport staff	Courtesy and helpfulness of airport staff
Restaurant / eating facilities	Restaurant / eating facilities
Value for money restaurant / eating facilities	Value for money restaurant / eating facilities
Internet / IT facilities / wi-fi	Internet / IT facilities / wi-fi
Availability of washrooms	Availability of washrooms
Cleanliness of washrooms	Cleanliness of washrooms
Comfortable waiting / gate areas	Comfortable waiting / gate areas
Security and Immigration	
Courtesy and helpfulness of security staff	Courtesy and helpfulness of security staff
Thoroughness of security inspection	Thoroughness of security inspection
Waiting time at security inspection	Waiting time at security inspection
Feeling of being safe and secure	Feeling of being safe and secure
Waiting time at passport and visa inspection	
Courtesy and helpfulness of inspection staff	
Airport environment	
Cleanliness of airport terminal	Cleanliness of airport terminal
Ambience of airport	Ambience of airport
Arrivals services at this airport	
Speed of baggage delivery service	Speed of baggage delivery service
Passport and visa inspection	
Customs inspection	
Airline service	
Waiting time in check-in queue / line	Waiting time in check-in queue / line
Efficiency of check-in staff	Efficiency of check-in staff
Courtesy and helpfulness of check-in staff	Courtesy and helpfulness of check-in staff
Business / executive lounges	Business / executive lounges

Appendix F Historical comments on the ACCC's methodology

The *Airports Act 1996* requires the Australian Competition & Consumer Commission (ACCC) to monitor and evaluate the quality of various passenger and aircraft related airport services and facilities, as defined in the *Airports Regulations 1997*. The ACCC has therefore developed a quality of service monitoring program which aims "to gather and report data on criteria that facilitate assessments on changes in service quality over time as well as possible comparisons across airports."[95]

The monitoring and evaluation criteria are determined by the ACCC in consultation with the Department of Infrastructure and Transport and Treasury. The ACCC gathers data using both objective quantifiable criteria and subjective surveys of passengers, airlines and government agencies. The ACCC interprets the data and publishes Airport Monitoring Reports annually.

The Productivity Commission (PC) has twice reviewed quality of service monitoring. In 2002, the Productivity Commission identified a number of problems relating to the ACCC's conclusions, including:

- Airports do not have direct control of many of the services provided at airports, yet the poor performance of these services (for example excessive delays in clearing Customs) will affect passenger perceptions.
- The ACCC place emphasis on survey results which can be influenced by a range of factors. In its submission Melbourne Airport commented on the airline survey employed by the ACCC: "It seems to us that individual airlines use this [airline surveys] as a device to have a 'free kick' at airports and often use it as a forum for a 'pay back' against an airport for taking a particular line in a commercial negotiation."[96]
- Airports may be undertaking maintenance or building work that temporarily affects service quality.
- There are technical problems with airline and passenger surveys including the failure to weight airline survey responses and sampling biases associated with passenger surveys.
- The potential for misleading assessments of the objective indicators.

The Productivity Commission found:

The overall quality of service provision by airport operators at monitored airports does not appear to have deteriorated since monitoring commenced. This outcome reflects to a large extent the commercial incentives for airport operators not to reduce service quality."[97]

In 2006, there were more extensive concerns expressed in submissions about the reliability and inherent usefulness of the quality monitoring process. Concerns persisted about the ACCC's willingness to use problems in service delivery of services outside an airports control against an airport. There were also concerns about the ACCC's use of unsubstantiated commentary from airlines and the Australian Customs Service:

Sydney Airport has little comfort that subjective assessments of service quality by airlines provide an adequate sample, given that it is not apparent that the correct personnel are

[95] *Airport quality of service monitoring guideline*, ACCC, October 2008, page 3.
[96] Productivity Commission 2002, *Price Regulation of Airport Services*, page 270
[97] *ibid*, page 271.

surveyed, and that voluntary responses to the survey would be expected to bias responses to those with specific 'axes to grind'[98].

Sydney Airport's submission advised that it was not apparent that the ACCC was well placed to add real value to the process and suggested dispensing with ACCC reporting altogether, "replacing it with a requirement that major airports publish annually the results of a properly constructed customer satisfaction survey."[99]

The Productivity Commission considered that the value added by some aspects of the process was questionable and recommended a streamlining of the system:

In examining opportunities to improve and streamline quality monitoring, the Australian Competition and Consumer Commission should give particular attention to:

Whether it remains necessary to report survey responses from the Australian Customs Service;

How best to eliminate overlap between the airline and passenger satisfaction surveys, and between these surveys and other quantitative indicators; and
Whether greater emphasis should be placed on comparative passenger satisfaction results contained in authoritative international benchmarking exercises.[100]

Rather than follow these recommendations, the ACCC continued with surveying the Australian Customs Service and broadened the surveying to encompass other public service agencies including the Australian Quarantine and Inspection Service and the Department of Immigration and Citizenship.

In the years since 2006, Sydney Airport has become increasingly concerned about the ACCC's methodological approach to quality of service monitoring.

In 2008, following the release of that year's ACCC report, Sydney Airport wrote to the ACCC about their methodology:

As you know, Sydney Airport has previously indicated its concerns with the methodological approach used by the ACCC as it draws heavily on anonymous and subjective feedback from bureaucrats in the Australian border control agencies. In reaching an overall rating the methodology mixes this information with customer survey data and facility availability information of debatable value in measuring the overall service to our airport customers.[101]

In 2009, Sydney Airport prepared a submission to the Productivity Commission's "*Annual Review of Regulatory Burdens on Business: Social and Economic Infrastructure Services*". The submission highlighted a number of methodological inadequacies and a conflict of interest.

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[98] Sydney Airport Corporation Limited 2006, *Submission to the Productivity Commission Inquiry Into Price Regulation of Airport Services*, page 36
[99] *ibid*, page36-37
[100] Productivity Commission 2006, *Review of Price Regulation of Airport Services*, page120
[101] Correspondence from Russell Balding to Graeme Samuel, March 2008.

The conflict of interest that was of concern arises because the ACCC states that the objectives of quality of service monitoring include providing "information to users of airport facilities, including passengers *and the aviation industry*, as a basis for improved consultation and *negotiation on pricing* and investment proposals." [Emphasis added].[102]

In preparing its report the ACCC makes extensive use of airline surveys that seek to record the opinions that airlines express about the performance of airports. The details of these airline surveys are not disclosed and the anonymity of the airline sources is protected by the ACCC.

The conflict of interest that exists in asking a commercially motivated organisation (an airline) for its views on one of its commercial counterparts and suppliers (an airport operator) is obvious. Airlines have a clear commercial interest in talking down the performance of an airport as they seek to gain a commercial advantage to employ in the course of significant commercial negotiations. The ACCC recognises the "*...the potential incentive for airlines to deliberately under-report quality for the airports...*"[103], but apparently believes that the conflict is entirely negated by asking the airlines for the reason for any ratings below satisfactory.

The inherent conflict of interest involved in an airline contributing to a report that is designed to assist it in its price negotiations is compounded by the ACCC's methodological approach. The ACCC's airline survey lacks transparency and fails to disclose which airlines participate in the survey and what information each airline submits. The absence of transparency and accountability in the ACCC's approach could therefore provide an extra incentive to airlines to game the survey outcome.

In its final Report, the Productivity Commission's assessment supported the concerns put by Sydney Airport:

An airline 'talking down' the performance of an airport in a quality of monitoring survey to gain an advantage in negotiations with an airport operator is likely to be part and parcel of the commercial negotiations between these parties.[104]

Also in 2009, as part of the development of the National Aviation Policy White Paper, the Department of Infrastructure, Transport, Regional Development and Local Government issued a discussion paper: *"Improving the passenger experience: Quality of service monitoring of airports"*[105]. In its submission to the Discussion Paper, Sydney Airport detailed a number of concerns about the ACCC's work and concluded:

Overall, the current ACCC reporting system is not working and:

fails to accurately represent the complexities of airport service delivery where, more often than not, more than one party is responsible for service outcomes

[102] Australian Competition & Consumer Commission, "Airport quality of service monitoring guideline", October 2008, page 3
[103] ACCC, *Airport monitoring report 2009–10,* page 16
[104] Productivity Commission 2009, *Annual Review of Regulatory Burdens on Business: Social and Economic Infrastructure Services,* Research Report, Canberra, p 274.
[105] *Improving the passenger experience: Quality of service monitoring of airport,* DITRDLG, March 2009

is plagued by an inherent conflict of interest in using the views of airlines (and government agencies) instead of an exclusive focus on the views of passengers

has substantial methodological weaknesses and a narrow and restricted scope that together act to produce flawed and unreliable quality of service reporting.[106]

As a result of submissions like this, the Government indicated in the White Paper, released in December 2009, that the Productivity Commission would again review the ACCC's quality of service monitoring regime in 2012.

In March 2010 the ACCC released its monitoring report and stated that:

Although Sydney Airport has recently commenced significant capital works at the terminal, it seems that the timing of this investment might have been inefficiently delayed by the airport, and there has been inadequate maintenance.[107]

In fact, construction work had commenced several years earlier, in 2007, and work on the expansion and upgrade of the Departures level of the International Terminal was completed and officially opened by the Minister for Infrastructure and Transport, the Hon Anthony Albanese, three months after the ACCC's released its report, in June 2010.[108]

The Government decided to bring the Productivity Commission's review forward and, on 15 December 2010, through Terms of Reference 5, formally directed the Productivity Commission to consider and report upon the effectiveness of the existing quality of service monitoring regime conducted by the ACCC, including the methodology used and the adequacy of the information collected.[109]

After the release of the ACCC's latest report the ACCC's Chairman, Graeme Samuel, was interviewed on ABC radio, where he said:

This is not an academic research report. This is a monitoring report that the ACCC does at the request of government.[110]

It should be clarified that the expert reports commissioned by Sydney Airport were not concerned with academic publication but with the standards required of practitioners.

Sydney Airport's request for transparency on the 2009/10 report

In regard to the ACCC's 2009-10 report, Sydney Airport notes that the ACCC still has not provided essential methodological information. Sydney Airport would welcome more transparency from the ACCC and believes that it is not possible to meaningfully interpret research unless basic methodological information is disclosed.

[106] Sydney Airport submission to the Discussion Paper, 2009.
[107] ACCC, *Airport monitoring report 2008–09*, p 40.
[108] For a video of Minister Albanese's speech at the ceremony: http://www.youtube.com/watch?v=heX8n-7VDOg
[109] Australian Government, *National Aviation Policy White Paper*, December 2009, page 181 and Shorten Bill, *Terms of Reference – Productivity Commission Inquiry – Economic Regulation of Airport Services*, 2010.
[110] Transcript of an interview broadcast on ABC Radio 702, 8 February 2011

To assist in interpreting the report, Sydney Airport called on the ACCC to provide basic information about its methodology[111]:

- How many airlines participated in the airline survey at each airport? What was the response rate at each airport?
- Who in the airlines completed the surveys and how were they selected?
- How many passengers were surveyed at each airport in the study?
- If different numbers of passengers were surveyed at different airports, why?
- What is the margin of error for each passenger survey?
- Were all passenger surveys administered by AS:ISO-qualified professional research teams?
- Were some passenger surveys undertaken in-house by the airports themselves? If so, which airports did their own surveys?
- Were the exact same questions used in the surveys asked at each airport?
- How were passengers selected to participate in the surveys?
- How were the passenger surveys conducted? By internet, mail, telephone, face-to-face or other? Was the same approach used at each airport?
- How many public servants were surveyed in the government agencies survey? How were these individuals selected?
- What weightings were attached to the different elements of the research to determine the overall ratings?
- If different methodologies were used at each airport, how can the results be valid and fair?

To date, the ACCC has not disclosed any of the information sought by Sydney Airport.

[111] http://www.sydneyairport.com.au/SACL/SPContent.aspx?PageID=63&ItemID=240&count=1

Appendix G Commercial-In-Confidance

Appendix H Commercial-In-Confidance