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Pricing Consultation  
PO Box 367  
Canberra ACT 2600

Dear Sir/Madam

### **Draft Price Proposal 2012 to 2016**

Thank you for the opportunity to comment on Airservices Australia's (AsA) Draft Price Proposal for en-route, terminal navigation (TN) and aviation rescue and fire fighting services (ARFF). The Board of Airlines Representatives Australia (BARA) has actively participated in the development of long term pricing agreements with AsA since 2004. BARA is, therefore, in a position to offer a considered view on the quality of the process and outcomes of the Draft Proposal.

I have written to AsA previously to express the concerns of international airlines over the development of prices to date. While AsA has spent considerable time considering how to allocate costs between airlines, less than adequate time and resources has been devoted to justifying underlying costs. BARA does not consider that AsA has implemented the key recommendations made by the Australian Competition and Consumer Commission (ACCC) in its 2004 Final Decision. AsA has not justified basin city pricing, improved the transparency over its capital program or examined ways of introducing formal operating efficiencies over its operating costs.

As a consequence, this pricing proposal does not build upon the basis established in the 2005 Agreement as envisaged by the ACCC. It is disappointing that such a large amount of available time and resources was effectively wasted in once again examining the question of whether domestic airlines should be required to pay for the costs incurred in providing services to them at regional airports.

The deficiencies in the process are reflected in the Draft Proposal. It is far less transparent in its assumptions, revenue and cost outcomes compared to the price notification AsA lodged with the ACCC in 2004. The Draft Proposal is almost totally devoted to the matter of how total costs are to be shared between users. While numerous claims are made in the Draft Proposal about the efficiency of the proposed prices, little of the rhetoric is substantiated by evidence.

Given that AsA is now close to lodging its Pricing Notification with the ACCC, there is little value in BARA re-stating its underlying concerns. Instead, in this response, BARA focuses on where key assumptions over the pricing of services are unclear. A request is also made for some improvement in the transparency of the information provided.

## **Aviation rescue and fire fighting services**

Under the Draft Proposal, weighted average ARFF prices are proposed to increase by over 40 per cent in the 5 years to 30 June 2016. A large proportion of this increase is attributable to the ARFF Category 6 price, which increases by over 35 per cent.

As BARA has made clear on many occasions, BARA opposes the networking of Category 6 ARFF costs across Australia. While AsA has successfully exploited the deficiencies in the current Prices Notification process to date, the fact remains that poor pricing decisions encourage an inefficient domestic aviation industry less able to cope with changing market circumstances.

What is not made clear in the Draft Proposal is the approach to pricing for the new ARFF stations at Ballina and Coffs Harbour. While the Draft Proposal describes how AsA intends to price for new TN services at regional airports, it is silent on the pricing of new ARFF stations.

BARA requests that AsA states the proposed method of pricing for the new fire stations, together with information on their forecast costs, expected revenues and the impact of any shortfall on Category 6 prices. AsA also should justify any difference in the approach to pricing new ARFF stations compared to new towers at regional airports.

## **Terminal navigation**

Under the Draft Proposal, price increases for TN services at regional locations are largely limited to around 3.5 per cent per year. At major city towers, prices move in line with activity levels and costs, including the cost of some general aviation (GA) towers.

In the Draft Proposal, AsA claims that the proposed price structure ‘improves the linkages between prices and costs’.<sup>1</sup> At the same time, AsA notes that ‘Costs have also been included for proposed ATC tower service upgrades at 11 regional ports’.<sup>2</sup>

BARA is skeptical that AsA is able to provide enhanced TN services at regional airports without exacerbating the level of cross subsidy from other services with price increases of less than four per cent per year. From the information provided to BARA, it appears that at many regional towers the increase in costs across the 5 years to 2016 is not matched by an equal increase in revenues.

This underlying problem is also reflected in AsA’s contradictory pricing principles for TN services. On the one hand, AsA notes that each location should recover at least its location specific costs. On the other hand, prices at regional airports are subject to arbitrary caps, with the statement that ‘the shortfall from price capping these services will be recovered through en-route services where the distortionary impact is likely to be low.’<sup>3</sup>

The Draft Proposal also states that ‘any new services that arise which have not been included in this proposal will have a three month grace period, from the services commencement date before charging begins.’<sup>4</sup> BARA does not support AsA providing ‘grace’ periods for new services except to the extent the present value of costs are fully recovered over time. Providing grace periods on prices to domestic airlines when international airlines continue to be heavily overcharged is unjustified.

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<sup>1</sup> Draft Price Proposal, p. 5.

<sup>2</sup> Draft Price Proposal, p. 13.

<sup>3</sup> Draft Price Proposal, p. 9.

<sup>4</sup> Draft Price Proposal, p. 13.

BARA also notes that AsA has again made no effort to provide any evidence to justify basin city pricing. Only unsubstantiated rhetoric is again restated. Given that the ACCC noted AsA's commitment to properly examine the issue in 2004, AsA seems to be signaling that it now views the ACCC review as a 'rubber stamping' exercise where few, if any, of its claims will be rigorously tested. BARA will be providing its evidence and analysis on basin city pricing as part of the ACCC's review.

### **Risk sharing arrangements**

BARA notes that AsA intends to maintain the same risk sharing arrangements agreed as part of the 2005 Agreement.

Under the arrangements, AsA may decide to increase prices in response to an unplanned downturn. However, BARA does note that AsA did not increase prices from the downturn in activity associated with the global financial crisis.

From an international airline perspective, even in depressed conditions, international airlines are still likely to be paying AsA more than cost of providing the services they use. This is because international airlines are substantially overcharged to fund unrelated infrastructure at regional airports.

Any revenue shortfall during an unplanned downturn is, therefore, really about AsA's ability to fund its domestic industry protection arrangements through cross subsidises from international airlines. BARA, therefore, does not accept that there should be any price increases on international airlines during an unplanned downturn.

### **Inflation forecast**

In the Draft Proposal AsA states that 'over the next five years proposed prices will provide real price reductions of more than six per cent against general inflationary pressures of costs rising at about three to four per cent per annum.'<sup>5</sup> BARA notes that such a high inflation forecast exceeds that usually adopted by economic regulators, such as the Australian Energy Regulator.

BARA, therefore, assumes that AsA has adopted unrealistically high inflation forecasts simply for propaganda purposes so it can claim real price reductions over the next five years. However, if AsA does consider that inflation will be above the Reserve Bank of Australia's target range over the medium term, it should provide the evidence that justifies this position...

It is also important for AsA to detail and justify the inflation forecast it has used in developing its forecasts of capital and operating expenditure. BARA would expect that any general inflation indexes used by AsA to escalate future operating and capital costs are consistent with inflation forecasts currently used by economic regulators in Australia.

Yours sincerely,



Warren Bennett  
**Executive Director**

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<sup>5</sup> Draft Price Proposal, p. 5.