BARA Board of Airline Representatives of Australia Inc

Airline Views

March 2019

1 Productivity Commission Draft Report: Airport regulation

BARA's response to the Draft Report dispels the misconception that international airlines are biased, regulatory gamers.

The Productivity Commission chose to largely ignore the genuine and legitimate concerns international airlines have about the provision and pricing of airport services. The problems in airport services, however, are not going away under the Draft Report's findings.

BARA estimates there are some $270m in potential operating efficiencies for international flights over the next 5 years through improved airport services.

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2 International on time departures performance

Improved airport services could lift on time departures performance at Sydney and Melbourne airports by about six percentage points.

At Sydney and Melbourne airports, on time departures performance for international flights is about 77−78%. This is only average performance when measured against comparable overseas airports and well below achievable outcomes.

With the airport operators assuming a position of limited influence, however, it's not surprising they're not actively managing those issues that would support improved on time performance of international airlines.

3 Sydney Airport's FOD problem

International airlines have raised problems with foreign object debris (FOD) in submissions and the airport monitoring report.

The highly unacceptable FOD issues at Sydney Airport are to the detriment of efficient international airline operations. Damage to aircraft and aviation equipment is imposing additional costs on the airlines.

BARA considers that Sydney Airport's FOD problems are a breach of the Aeronautical Pricing Principles by the airport operator.

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4 Sydney Airport's fuel throughput levy

BARA estimates Sydney Airport extracts $16−17m a year in economic rent through its unjustified fuel throughput levy.

BARA's understanding is that, at privatisation, Sydney Airport did not purchase the automatic right to impose a fuel throughput levy. Instead, Sydney Airport chose to exercise its market power and impose the levy in subsequent lease renewals over the land occupied by the aircraft refueling facilities at the airport.

The economic rent is estimated to generate an excess annual rate of return of about 400% on the land it leases for aircraft refueling facilities.

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Productivity Commission Draft Report

BARA was surprised to learn the Productivity Commission questions the motivation of international airlines in raising concerns about the quality of airport services. There is no basis to assert that international airlines have sought to 'game' the regulatory system by giving low ratings. In response, BARA has responded with more evidence that covers international on time performance, baggage and some highly unacceptable airfield services outcomes at Sydney Airport.

Airlines pay the operators of the major international airports over $800 million annually in airport services for international flights, and BARA estimates they incur over $250 million in additional operating costs due to aviation infrastructure inefficiencies. Large and sustained productivity gains could be achieved by improving the provision and management of airport services. Member airlines are disappointed the Commission did not seek to investigate these matters in greater detail.

International airlines are biased, regulatory gamers? Seriously?

The commentary in the Draft Report conveys to the international airlines and interested parties that the Productivity Commission has taken an explicit position to disregard the performance assessments of airport services provided by the international airlines, as the Commission believes their evidence is biased.

In particular, the Commission's comment in Box 5.1 of its Draft Report, when referring to the Australian Competition and Consumer Commission's (ACCC) airline survey in the airport monitoring report and BARA's member survey, states that:

> or airlines might be motivated to 'game' the regulatory system by giving low ratings.

BARA rejects this position. The international airlines have not sought to game the Commission's inquiry through the information they have provided. Rather, they have provided an informed assessment of airport services, both positive and areas of concern, with an emphasis on the ability of airport services to support their efficient operations at the airport.

The member survey provided in BARA's initial submission to the Commission's Inquiry is consistent with the ongoing information and feedback BARA has been providing to the airport operators over many years.

The Commission's Draft Report also draws attention to the fact that international passengers have generally rated airport services higher than international airlines, which BARA considers is largely irrelevant.

It is important to understand that international airlines are rating services that international passengers are not asked about, which means the two groups of services being surveyed are different. The fact that international passengers may be well satisfied with their shopping experience does not mean international airlines have been biased in reporting that highly unacceptable levels of foreign object debris around Sydney Airport International Terminal are reducing the efficiency of their operations and causing damage to their aircraft.

If it is asserted that international airlines have sought to manipulate their evidence, which is a serious allegation, then BARA would have expected the Commission to have requested further evidence that justified the service ratings given by international airlines.

Some extra monitoring data won't fix matters

The Commission thinks that there may be a need for airports to demonstrate to airlines (and more broadly) how the airport operators are meeting expectations of value for money. As such, they have called upon the ACCC to revamp the annual airport monitoring report with new data.

Airlines already have a deep understanding of service quality and value for money in airport services, based on the fact they are using the services daily and paying monthly invoices from the airport operators. Most airport services key performance indictor (KPI) regimes, however, are still at a basic level. The industry is a long way from being able to accurately measure and understand its performance given the quality of airport services provided.

BARA is challenged to see how a revamped monitoring regime will address the problems international airlines have with the provision and management of airport services at Australia's major international airports.

Without change to the underlying commercial accountabilities, BARA does not expect the industry to realise the attainable efficiency improvements in airport services. The non-binding Aeronautical Pricing Principles are not assisting international airlines, which do not have the countervailing market power to achieve acceptable commercial outcomes.

Ultimately, international airlines will operate to Australia's airports to the best of their ability given the quality of services on offer. Whether the benefits of superior performance in airport services are delivered for the Australian economy and people will depend on the willingness to achieve them rather than simply accept current standards or only look for sustained poor outcomes.

Sydney Airport's FOD problem

The Productivity Commission's Draft Report paints a very positive picture of the outcomes achieved by the operators of the major international airports. Unfortunately, international airlines can face a quite different reality.

A prominent example is airfield services around Sydney Airport International Terminal. Member airlines consider the standard of airfield services, especially the active management and removal of foreign object debris (FOD) from around the terminal, remains highly unacceptable.

FOD is generated by infrastructure and equipment operations at terminal gates, cargo aprons, taxiways and runways. It describes a wide range of items, including broken equipment and loose hardware such as bolts and metal fragments, pavement rubble, catering supplies and luggage parts. FOD is recognised worldwide as an issue that must be actively managed at all airports. This should occur daily to systematically maintain a safe, clean area for aircraft operations.

Inspections by BARA confirm the ongoing concerns raised by international airlines. BARA has observed extensive FOD, including metal parts, general litter and rubbish on the aircraft aprons around the international terminal gates.

The lack of active management of FOD around Sydney Airport International Terminal is both making aircraft operations less efficient and causing damage to international aircraft.

BARA considers the FOD problem represents a breach by Sydney Airport of the Aeronautical Pricing Principles, namely 'that service-level outcomes for aeronautical services provided by the airport operators should be consistent with users' reasonable expectations' (Principle E).

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Sydney Airport's fuel throughput levy

BARA regards Sydney Airport's fuel throughput levy (FTL) as nothing more than an unjustified extraction of economic rent, estimated to generate an excess annual rate of return of 400% on the land it leases for aircraft refueling facilities. Sydney Airport did not obtain the automatic right for this revenue stream at the time of privatisation. It represents a sustained exercise of market power by Sydney Airport in aircraft refueling services.

No right to impose

BARA's understanding is that, at privatisation, the lease between Sydney Airport and the owners of the aircraft refueling facilities at the airport (Sydney JUHI) did not give Sydney Airport the automatic right to impose an FTL. Sydney Airport chose to exercise its market power and impose an FTL in subsequent lease renewals with Sydney JUHI. As explained by the Shell Company of Australia in its submission to the Commission's 2007 Inquiry *Price regulation of airport services*:

> The Sydney airport owner has the right to introduce a throughput fee when it can reasonably assert that the payment of throughput fees is common around Australia, which to date has not been able to be made out. However, the Sydney airport JUHI lease is coming up for renewal. On current indications any imposed throughput fee is likely to result in a very significant cost increase that is many times greater than the current commercially based lease charge. No additional benefit is being offered.

The Commission should require Sydney Airport to provide the initial JUHI Agreement to confirm the commonly understood position.

400% annual excess return

BARA estimates Sydney Airport likely earns between $16–17 million per year through the FTL, thereby generating an excess annual rate of return of about 400% on the value of the land occupied by the Sydney JUHI (see table below). BARA's estimate could be refined through data sourced directly from Sydney Airport and Sydney JUHI.

Unless there is some manifest mistake in the analysis, which BARA has based on the best available data it can gather and which is consistent with the evidence put forward by the Shell Company of Australia, it is clear Sydney Airport is exercising its market power in the lease arrangements over the land occupied by the Sydney JUHI. These inflated costs are then passed onto airlines through higher fuel bills.

It will take some inventive economics for Sydney Airport to come up with a reasonable justification for its FTL. BARA would expect that, with over $16 million each year in free money, it will fund plenty of effort in seeking to do just that. BARA, however, considers that this money and effort could be much more usefully put to dealing with service issues at the airport, such as the highly unacceptable FOD around Sydney Airport International Terminal.

Analysis of Sydney Airport's FTL

	Units	Value
JUHI land area	m^2	27,000
Land valuation	$/m^2$	$148
Total land value	$ millions	$4.0
Fuel throughput levy	cents per litre	0.5
Annual fuel sales	Billions	3.3
Annual FTL revenues	$ millions	16.5m
Excess return	% per year	**413%**