



Future Investments and the Regulatory Till

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1. Introduction

- 1.1 This paper provides an update on our current thinking about the definition of the regulatory till used for the purposes of making determinations governing airport charges at Dublin airport. We previously published a consultation paper in late 2010 inviting stakeholders to comment on possible changes to the regulatory till.¹
- 1.2 We have not been persuaded to adopt a dual-till approach to price-cap regulation at Dublin airport. This follows careful consideration of the responses to the consultation paper CP4/2010.
- 1.3 At the same time, we propose to consider further whether and how the approach to regulation might address investment plans where the DAA and airlines disagree about the commercial viability of the project. In doing so, we recognise that this may have implications for the future scope of the regulatory till and require changes to the regulatory asset base (RAB).
- 1.4 Our goal in considering refinements to the current regulatory approach is to permit the DAA to undertake commercial investments and assume the risks around such investments in instances where users may not share the DAA's optimism about the project. Currently, we decide whether to allow such investments into the RAB. When we make an allowance, the DAA receives a return equal to the regulated cost of capital, while users assume the risks (in the form of higher or lower airport charges) associated with the investment's uncertain income stream. In instances where the DAA wants to proceed with a commercial investment that users oppose, we are willing to adapt the regulatory till such that the DAA can make the investment knowing that it rather than users will bear all the risks of the venture. Future determinations will have no regard to the costs or revenues associated with the investment, so it will have no implications for price-cap calculations for airport charges.
- 1.5 The following chart illustrates the circumstances in which we might decide to exclude an activity from the regulatory till. The focus is on what we have termed commercial investments in this paper. Such investments are in activities expected to generate revenues from non-aeronautical services. Should the DAA propose a commercial investment, we would want to be satisfied that it was possible to separate the costs and revenues from the rest of the Dublin airport accounts in a meaningful and straightforward manner. This is likely to mean many investments relating to retail activities, for example, remain in the regulatory till because of the arbitrary judgments that would be necessary to decide what share of the costs of terminal or pier should be allocated to the retail activity. Where a separation is practical, we would then consider whether excluding the activity from the regulatory till would be mutually beneficial to the DAA and users. This is most likely to be the case for commercial investments that the DAA wants to undertake, but for which users have reservations about whether the investment will yield positive returns.

¹ CAR. "Defining the Regulatory Till". CP4/2010. http://www.aviationreg.ie/fileupload/2010_CP4-2010%20Defining%20the%20regulatory%20till%281%29.pdf

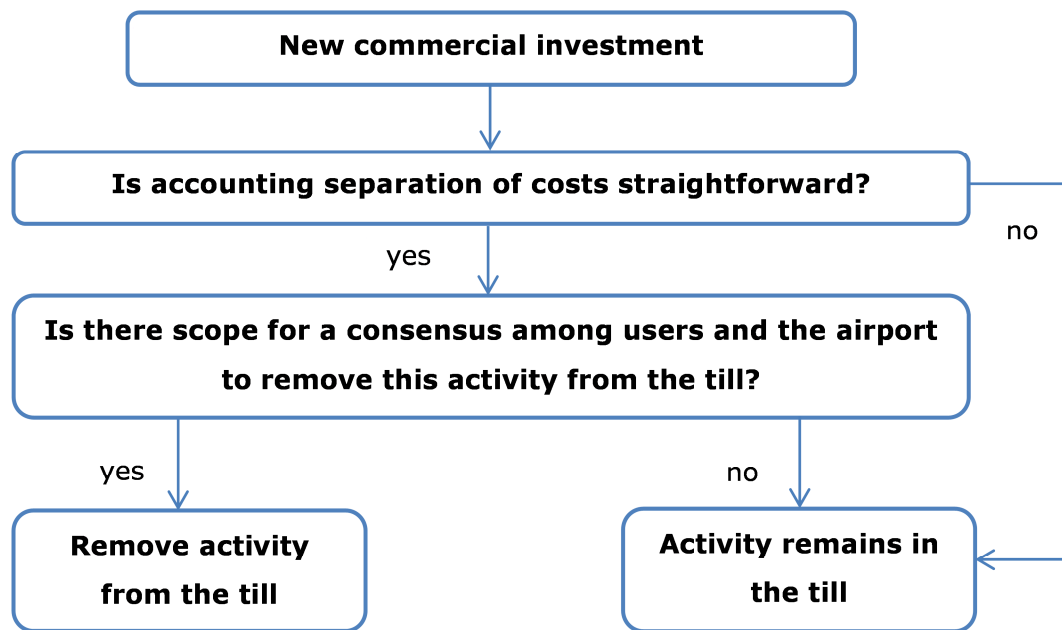


Chart 1: **Decision tree for excluding investments from the regulatory till**

- 1.6 Dublin airport city provides an example of a commercial investment that meets these criteria, and for which the Commission has previously indicated an intention to exclude its costs and revenues from the regulatory till (with the support of both the DAA and airlines). The proposals in this paper arguably do not represent a completely new regulatory philosophy. Instead, they seek to develop a more structured framework for considering future commercial investments when making determinations. We hope that this will benefit all stakeholders, by providing both the DAA and users with a better understanding of how future determinations might treat commercial investments, allowing parties to plan accordingly.
- 1.7 The proposed approach gives rise to many questions. What happens if the commercial investment relates to an activity already in the regulatory till? What adjustments, if any, should be made to the RAB if an investment is excluded from the regulatory till? Under what circumstances, if any, might an investment excluded from the regulatory till be re-introduced to the till at a later date? Is it possible to provide a regulatory environment that protects the interests of current and prospective users and permits the DAA to develop and commence commercial investment plans without waiting until the next determination to have sufficient clarity about the regulatory implications? These and other questions are identified and some preliminary thoughts offered later in this paper.
- 1.8 The next section summarises the responses to CP4/2010 and sets out our reasoning for not switching to dual-till regulation. In Section 3 we discuss why we nevertheless think that there may be merit in excluding some commercial investments from the regulatory till. We outline how we might make such decisions, the possible implications for the RAB, and some possible problems that might arise over time if some commercial investments are excluded from the regulatory till. Section 4 concludes, by setting out the next steps that we propose for this work stream and

providing details for parties wishing to respond to this consultation paper. The deadline for responses is 27 June 2012.

2. Single versus dual till

- 2.1 This section outlines why we have not been persuaded to adopt dual-till regulation and base airport charges solely on an estimate of the costs of providing aeronautical services in isolation, having no regard to possible commercial revenues.

Responses to the first consultation paper

- 2.2 We first summarise the responses to the initial consultation paper from November 2010 (CP4/2010). That paper set out the distinction between a single and dual till approach to regulation, and why it might matter when setting a price cap. The parties who submitted a response were Aer Lingus, Airports Council International Europe (ACI Europe), the DAA, and the International Air Transport Association (IATA).
- 2.3 Consistent with the traditional divide between airlines and airports on this topic, Aer Lingus and IATA favoured retaining the single-till approach to setting a price cap while ACI Europe and the DAA supported changes to the regulatory till.
- 2.4 Aer Lingus argued that single-till regulation most closely replicated how a competitive market would work. Hence, single-till regulation properly applied sent the correct pricing signals for decisions about use of the airport and investment in new facilities. Aer Lingus also thought single-till regulation was more practical, although it identified some potential problems: the need to review the till to only include commercial activities that are a by-product of the aeronautical services or have a cost base largely shared with those services; the need to provide the DAA with incentives to manage commercial activities efficiently; and the risk that airlines would be asked to underwrite commercial developments. It thought these problems were surmountable.
- 2.5 ACI Europe thought that regulation should only cover those activities for which the DAA has market power. It cited the Airport Charges Directive, claiming that this had arisen following a comprehensive consultation process and its design recognised the changing balance of market power between airports and airlines. ACI Europe suggested that the Commission should cease making the minute and detailed decisions it currently has to make under the building-blocks approach, and instead take on the role envisaged for an independent supervisory authority. It claimed that single-till regulation led to the regulator being asked to adjudicate between airports and airlines as to where rents should go, when instead the regulator's focus should be proportionate and target optimum social outcomes. Granting the airport commercial freedom would benefit all players in the long run. ACI Europe supported adopting an "economic approach", with regulation only affecting those activities for which the DAA has market power.
- 2.6 The DAA welcomed the consultation on the composition of the regulatory till. It cited international precedent demonstrating a move away from the single till, which it argued artificially reduced airport charges. It thought such a switch would also improve efficiency, since airport charges would give better

pricing signals and in the longer run there would be less risk of under-investment. The DAA suggested that a transitional move away from the single till may make more sense than a complete transfer to a dual till, since the latter option would be a substantial change in regulatory policy. It thought that the “economic approach” should be used to define the boundaries of the regulatory till, predicting that this would improve the potential for the Commission to set price caps that were economically efficient.

- 2.7 IATA reiterated its consistent support for a single-till approach to regulation. It set out the reasons for this position. It acknowledged that in practice regulators rarely apply a single till in full, and suggested a number of important considerations should a dual till be introduced, such as clearly defining what is in the regulatory till; providing full details on the cost-allocation methodologies; and a revised rate of return for airport charges’ calculations to reflect the lower risk for aeronautical activities.

Rationale for not adopting the dual till

- 2.8 The responses to CP4/2010 made appeals to the concept of economic efficiency. We have previously consulted with the industry and set out how the economic concepts of productive, allocative, and dynamic efficiency promote our statutory objectives when making a determination governing the level of airport charges the DAA can collect at Dublin airport:
- the efficient and economic development of Dublin Airport
 - the ability of the DAA to operate in a financially viable manner
 - the protection of the interests of users and potential users of the airport.
- 2.9 Respondents also referred to the benefits of competition, and how such an environment can lead to economic efficiency. There were calls for regulation to provide the same sort of incentives for the DAA as would be found in a competitive market. Parties disagreed on whether we should move from single-till regulation to dual-till regulation, yet when analysed more closely it appears to us that a primary area of concern is shared between parties: how to ensure the DAA faces the same incentives to invest in commercial activities as entities in a competitive market.
- 2.10 In thinking about how airports might compete, we tend to agree with the model of competition Aer Lingus outlined. A simple model of competing airports would predict that airports will ultimately have to pass through any cost savings that they are able to realise to their users, in the form of lower airport charges. Airlines will gravitate to the airports that offer the lowest airport charges (controlling for differences in quality of service). To attract airlines, the airports will compete to offer lower prices than their rivals. Airports will face competitive pressure to match the prices of those airports with the lowest cost bases. Hence, an airport which finds a way to cut its costs compared to other existing airports will only be required to pass through this saving if a rival airport operates at a lower cost. It can retain its profit though if it is currently the most cost-efficient airport and offers marginally lower charges to undercut the next most efficient airport.
- 2.11 The model does not need to specify exactly how the cost saving is realised. Perhaps the airport finds a way to undertake a particular process with fewer staff. Maybe the airport is able to persuade a retailer to undertake some of

the activities, such as cleaning, that the airport was previously doing in exchange for the right to run a food and beverage operation at the airport. If, instead of doing the cleaning, the retailer agrees to pay the airport a sum equal to the costs the airport incurred cleaning, we do not believe that there is any reason why the implication for airport charges should differ. For this reason, we think that if airports were competing, it is costs **net** of revenues from commercial activities that would be important. Airport charges in a competitive setting will align more closely conceptually with the costs as measured using a single-till calculation.

- 2.12 For certain commercial activities at an airport, there will be a relationship between the number of passengers and the level of profits from these activities. In other words, there exist demand complementarities. The profits will depend on passenger numbers. Passengers processing through one airport generate for that airport revenues that another airport foregoes. An airport subject to competition will be prepared to cut airport charges if the aeronautical revenues foregone are at least offset by the incremental levels of net commercial revenues from the extra passengers.

3. Future treatment of new commercial investments

- 3.1 Our continuing preference for a single-till approach reflects a belief that it is likely to yield airport charges more in line with those that might arise in a competitive environment. Nevertheless, we recognise that single-till regulation does not always present the DAA with the same incentives it would face if it were subject to competitive pressures. In particular, in a competitive setting, a commercial investment that an airport might consider undertaking would either leave the airport suffering losses if the investment proved unsuccessful, or receiving the profits for a number of years until competitors replicated the investment. The current regulatory approach does not provide such incentives. Instead it implicitly requires users to underwrite any project the regulator decides to permit into the RAB: airport charges rather than the regulated company's profits vary depending on whether the investment proves to be a commercial success or not. This is arguably most problematic for projects where there are differences of opinion about whether a commercial investment really will prove to be profitable.

Determining the scope of the regulatory till

- 3.2 We have previously had to consider investments for which at least some users did not necessarily share the DAA's optimism about the commercial prospects for the project. The following table lists some examples. It also describes how we chose to treat the project for the purposes of making a determination, illustrating that to date we have adopted a flexible approach and not always stuck with a "pure" single-till approach. For example, the current determination did not consider possible costs or revenues associated with Dublin airport city, while the capital costs for T1X are only included in the price-cap calculations to the extent that we believe the project generates incremental commercial revenues. More generally, by excluding investments that we do not think have a sufficient nexus to the airport (e.g. investments by DAA Group at other airports), we have implicitly adopted an approach to defining the regulatory till that is more pragmatic than the most dogmatic approach to single-till regulation might require. We noted in

CP4/2010, that the distinction between the single and dual tills is, in practice, not as stark as often portrayed.

T1X. In 2007, the DAA outlined plans to build a terminal one extension (T1X). Users expressed reservations about the project, with at least one airline stating it had no willingness to pay for the project. The DAA claimed that the project would pay for itself in terms of extra commercial revenues. We chose to permit the cost of the project into the RAB, but with a treatment of forecast commercial revenues after that date sufficient to offset the costs, such that the cap on airport charges would not have to be increased to permit the DAA to recover the costs.

Retail refurbishments. Users and the DAA disagreed about the need to invest in retail refurbishments at Dublin airport in the years 2010 to 2014. Having considered the arguments, we chose to include an allowance into the RAB of over €10m (less than the DAA sought but a positive amount notwithstanding user opposition).

Dublin airport city. Plans for Dublin airport city were announced in April 2008. There was no request from the DAA at the time of the 2009 determination to include a capex allowance for the project, and both the DAA and users have indicated support for excluding the project from the till. The calculations in the 2009 determination made no reference to possible costs and revenues associated with such a project; we did indicate that should the project proceed we intended to exclude the costs and revenues from the regulatory till in future determinations but to revise the RAB according to RAB roll-forward principles published at the same time.

Hangar maintenance. The DAA's plans relating to hangar maintenance evolved during 2009 in terms of scope, costs and expected revenues, with the costs of the project rising from €4.2m to over €10m. Users opposed this spend, expressing doubt that there was demand for such facilities despite the DAA's claims that the investment would generate annual rental income. We chose to not to make an allowance for this capex, but also revised down the forecast commercial revenues to exclude forecast rental income from renting the hangars. There was no adjustment to the existing RAB.

Car park. In 2009 the DAA argued for a €40m capex allowance to permit it to build a multi-storey car park. It argued that the project would generate excellent returns, but during capex consultation meetings users expressed doubts. Ultimately we did not adjudicate on the project's business merits since there was already an allowance for a T2 car park from the 2007 interim review. We accepted the DAA's contention that a car park would enhance the customer experience at the airport.

Table 1: **Regulatory treatment of some past commercial investments**

Source: CAR.

- 3.3 In terms of allocating the risks associated with the project, the approaches described in the preceding table have varied from the example of Dublin airport city, where it is proposed that the DAA should assume all the risks, to capital expenditure on retail refurbishment where (implicitly) airlines bear the risks. This approach has, on occasion, allowed the Commission to avoid adjudicating on the merits of a particular investment, but arguably some of the regulatory solutions are overly complex and the whole process may benefit from a more transparent and consistent approach.

- 3.4 A first step is reviewing whether the current regulatory till includes the right set of activities. In what activities should the Commission scrutinise investments by the DAA and decide whether to make an allowance for the costs and revenues in its price-cap calculations? The following table lists the categories of commercial revenues for which we currently have regard when making a determination; it also gives the Commission's forecast level of commercial revenues for 2012 for each category at the time of the last determination. For an alternative list of services that an airport might provide, the Civil Aviation Authority (CAA) in the UK listed the services provided at Heathrow airport in its recent review of market power at that airport.²

Category	2012 Forecast Revenues (€)
Direct retail revenues Concession retail revenues	58m
Car parking <ul style="list-style-type: none"> • short term • long term • taxi • coaches 	27m
Property concessions <ul style="list-style-type: none"> • banking • hotels • car hire 	16m
Property rental <ul style="list-style-type: none"> • office space • hangars • warehouses • check-in desks • airport-specific facilities (e.g. fuel depot) 	14m
Property advertising	4m
Other commercial operations <ul style="list-style-type: none"> • executive lounges and VIP services • taxi permit income • US customs border protection income • income from water-disposal services, utility handling charges, communications and cabling charges and identity badge income 	5m

Table 2: **Sources of commercial revenues currently in the regulatory till**

Source: CAR.

² CAA. "Airport market power assessments- Annex" February 2012.
<http://www.caa.co.uk/docs/5/MarketPowerAnnex.pdf>

- 3.5 To determine the activities that are included in the regulatory till, to date we have relied on the idea of “a sufficient nexus to the airport”. It is questionable whether this always provides enough guidance to parties about what precisely will be included or excluded.
- 3.6 One option would be to revisit the list of activities currently included in the regulatory till, and determine whether the list either (a) includes some activities that users do not consider a desirable complement to aeronautical services or (b) excludes some activities that they would expect an airport to offer. Such an exercise would yield a potentially revised list of activities included in the regulatory till, but would provide no guidance on how an activity not conceived of might be treated – a list of activities provided at an airport drawn up in the early 1990s may not have listed internet access and wi-fi services but many airport users may today consider such activities essential. Nor does it identify the mechanism by which a final decision would be made should parties differ on what activities are integral to an airport.
- 3.7 Instead, we propose considering afresh whether an activity should remain in the regulatory till (or be added to it) whenever there is a commercial investment that the DAA would like to make. We define a commercial investment as an investment that seeks to generate revenues from non-aeronautical services.
- 3.8 For such investments we will first consider whether the associated activities give rise to costs and revenues that can readily be identified separately from the costs and revenues associated with providing aeronautical services. A necessary condition for us to consider excluding an activity from the regulatory till will be that we are satisfied that the activity does not give rise to a large proportion of shared costs with other activities in the regulatory till. Where shared costs are significant, excluding the activity from the till would require us to rule on arguments about what share of costs to allocate to the till at the time of each determination. The allocation of risks and returns from such an investment may depend critically on subsequent, potentially arbitrary, regulatory decisions about how to allocate these costs, rather than the actual merits of the investment. Future determinations could be dominated by parties arguing about the appropriate cost-allocation rules to use rather than about what scope there is for the DAA to operate the airport more efficiently to meet the needs of current and prospective users.
- 3.9 Where accounting separation appears to be relatively straightforward and non-contentious, we will consider whether removing the activity from the regulatory till might have the support of both users and the DAA. This condition is most likely to be satisfied in instances where the DAA proposes an investment for which users have reservations. In such circumstances, the goal would be to assign the risks (positive and negative) of the proposed investment to the DAA while ensuring that users are not asked to pay higher airport charges than they would have had to pay had the activity remained in the regulatory till and the investment not been undertaken.
- 3.10 Dublin airport city is an example of an investment proposal that appears to meet both these criteria. Separate identification of most of the costs and revenues associated with the project appears to be possible; and representations made in 2009 to the Commission revealed support from both the DAA and users for excluding the investment from the regulatory till.
- 3.11 We suspect that in many instances, support from all parties to exclude an activity from the regulatory is most likely when the proposed investment is in an activity where the DAA has limited or no market power and for which the existing regulatory till includes relatively few costs and revenues. In

such cases, the only significant disagreement between the parties is likely to relate to the willingness to assume the risks associated with the project, a disagreement that can be addressed by excluding the activity from the regulatory till. The next section, discussing possible implications for the RAB, sketches why potential market power or existing costs and revenues in the regulatory till may make it harder for parties to agree to exclude something from the regulatory till.

- 3.12 When making a determination, we would advise on any activities that we were minded to exclude from the regulatory till. In most circumstances, where the DAA and users agree that an activity should be excluded from the regulatory till, we would expect to concur with that agreement and make a determination on the basis that the parties had agreed. But where parties disagree about whether or how the activity might be removed from the regulatory till, uncertainty about the regulatory treatment would only be resolved at the time of the next determination, notwithstanding the danger that this may hinder some investment planning.

Implications for the RAB

- 3.13 A primary concern to all parties will be how any change to the scope of the regulatory till might affect future price-cap calculations. The subsequent regulatory treatment is likely to influence whether the DAA and users want an investment to proceed with the activity excluded from the regulatory till. This section discusses some of the practical issues likely to arise. We start with the implications for the regulatory asset base (the RAB).
- 3.14 The proposed adjustments to the regulatory till seek to permit the DAA to invest in cases where the DAA and users have different attitudes to the risk of a commercial venture; they are not intended to change the level of airport charges. A change in the regulatory till should be net present value neutral, in terms of the stream of expected revenues from future airport charges, compared to a situation where the DAA did not proceed with the investment. We intend to achieve this neutrality goal by adjusting the RAB accordingly.
- 3.15 In the 2009 determination, we set out the general principles that we would follow in rolling forward the RAB between determinations.³ These principles include a scenario 7 which describes how we would envisage adjusting the RAB if the DAA sells an asset to a third party. We think that this approach would apply to assets required by the DAA to undertake an activity that will henceforth be outside the regulatory till. Hence, should an activity be excluded from the regulatory till, the RAB would be revised down by an amount corresponding to the *current* value of those assets (including land) required to provide the activity.
- 3.16 Since the asset will not have been sold to a third party, there will not be a sale price that might be used as a market valuation. Instead, in these scenarios the current value of the asset will have to be inferred. There are a variety of approaches that might be used and the preferred approach may depend on the asset in question.

³ See Annex 3, CAR "Determination on the Maximum Level of Airport Charges at Dublin Airport". CP4/2009. http://www.aviationreg.ie/fileupload/2009_CP4_Final%20Determination_4DEC.pdf

- 3.17 For a new activity, such as Dublin airport city, it may be that the only implication for the RAB is an adjustment to reflect the value of land removed from the regulatory till to facilitate the development. In this instance, reference could be made to recent prices paid for land in the vicinity of the airport and/or advice from real estate experts sought.
- 3.18 For investments where it is relevant, we will also have regard to the future stream of income (and costs) that would have been included in price-cap calculations had the associated activity stayed in the regulatory till. One approach would be to estimate the discounted future (net) income stream from the activity. For example, if the activity in question was car parking, what is the net present value of the DAA's existing car parks? This value might be estimated by building up a model of the likely future costs and revenues associated with the car parks. Alternatively, it may be possible to arrive at a value based on evidence from prices paid for car parking businesses elsewhere.
- 3.19 Decisions about the current value of an asset for the purposes of adjusting the RAB clearly have the potential for parties to express very divergent views. For the purposes of future price-cap calculations, users would prefer that assets being removed from the till be assigned a high value, while the airport would favour the reverse. Where the DAA is expected to have market power or there are already related activities included in the regulatory till, users and the DAA may differ markedly in how large an adjustment to the RAB is necessary if the activity is to be removed from the regulatory till.
- 3.20 The scope for divergent views may be constrained partially by the fact that the discussion will arise in the context of trying to facilitate the opportunity for the DAA to undertake a commercial investment for which users have reservations. It remains possible that we will ultimately decide not to remove the activity from the regulatory till, and instead decide whether to make an allowance for the proposed new investment. In those circumstances, arguments by users that the activity is very valuable may support the DAA's contention that its investment should be permitted, while arguments by the DAA that the activity has little value may undermine its case for additional investment being allowed into the RAB.
- 3.21 In theory, it would be possible to think about some form of profit-sharing arrangement which re-allocates only some of the risks of an investment away from users and on to the DAA. Including the costs of building a new hotel in the regulatory till means airport users bear the risks, in terms of higher or lower airport charges, should the hotel's profits not accord with what was expected; excluding the hotel from the regulatory till implies a total re-allocation of that risk onto the airport. We could instead consider only a partial re-allocation of the risk, such that future airport charges would reflect some of the profits from the hotel should it prove successful. Any such arrangement would have to be specified clearly in advance, so that all parties understood the allocation of risks, and the adjustment to the RAB would be smaller than if the activity was completely removed from the regulatory till. One attraction of such an arrangement is that it may reduce incentives for parties to disagree about the scale of the RAB adjustment. However, it comes at the risk of adding regulatory complexity and losing transparency, things that we would be keen to avoid. The onus would be on parties advocating a profit-sharing scheme to outline how these problems might be overcome and why it would be better than having the activity either entirely inside or entirely outside the regulatory till.
- 3.22 We would decide how to adjust the RAB when making a determination. We acknowledge that this may leave regulatory uncertainty between

determinations. This does not mean that commercial investments plans could not be advanced between determinations. For investments users want excluded from the RAB, the DAA and users may be able to agree a joint position that the activity should be removed from the till and the amount by which the RAB should change. We would normally expect to concur with such agreements and make subsequent determinations accordingly. Even where the DAA and users are unable to agree on the precise amount by which the RAB should change, agreeing a range may suffice for the purposes of the DAA deciding whether to pursue the investment outside the regulatory till in advance of the next determination actually being made.

- 3.23 Where the proposed investment is large relative to the possible adjustments to the RAB that might be sought, it is probably in the interests of both the DAA and users either to agree to the investment proceeding with the costs included in the RAB, or to agree to exclude the activity's costs and revenues from the regulatory till. In contrast, for investments that are small relative to the possible implications for the RAB, a decision by the Commission about what capital allowance, if any, to make may be preferable to parties to a decision by the Commission about what adjustment to make to the RAB so as to exclude the whole activity from the regulatory till. So parties may agree to exclude Dublin airport city from the regulatory till, but prefer that the Commission decide whether to include an allowance for a proposed €5m car-parking project rather than have car parking removed from the regulatory till and the Commission make a one-off adjustment to the RAB.
- 3.24 Once a decision to remove an activity from the regulatory till has been made, and the RAB adjusted accordingly, we would not ordinarily envisage revisiting the decision. We are keen to create an environment in which there is a degree of certainty about the regulatory treatment should the DAA proceed with an investment. Constantly revisiting the decision of whether to include the activity in the regulatory till may undermine such incentives. Where an activity is excluded from the regulatory till, the DAA would be constrained by competition law from abusing any dominant position it was subsequently able to obtain, but should not normally expect to have the costs and revenues included in future price cap calculations. The only exception we can see is if the commercial investment in question related to an activity that had evolved from an unusual marginal offering at an airport into something that all airports now offered. In these circumstances, the interests of prospective users might better be served if we capped the number of years for which the DAA was able to retain monopoly rents from the activity, in the same way that patents only protect investors for a limited number of years before competition is permitted and users realise the full benefits from the innovation in the form of lower prices.
- 3.25 This bias against revisiting decisions to exclude an activity from the regulatory till means that there would not be recurring, protracted regulatory arguments about the current value of the same assets at every determination. It also means that the DAA will assume the risk (upside and downside) of subsequent changes in the value of such assets, e.g. if land prices move sharply in later years. Should future developments relating to aeronautical services require some of these assets being brought back into the till, e.g. land needed to permit a terminal redevelopment, we would envisage considering afresh the current value of those assets at that date. This implies that the resulting RAB from having first removed an asset and then reinstated it may be higher or lower than it would have been had the asset never been taken out of the RAB.
- 3.26 At future determinations, we would continue to expect the DAA to consult on its investment plans for activities included in the regulatory till. For activities

excluded from the regulatory till, such an expectation would no longer exist provided the plans do not have implications for aeronautical services.

Policing the boundary of the regulatory till

- 3.27 The implications for future operating cost and commercial revenue allowances, as well as any one-off adjustment to the RAB, will also be important. For the purposes of developing investment plans in advance of a determination, parties will know that if an activity is removed from the regulatory till, future price-cap calculations will not include any allowances for either operating costs or commercial revenues related to the activity.
- 3.28 We propose retaining within the regulatory till activities for which a lot of the costs are shared with providing aeronautical services. Consequently, the magnitude of any disputes about what level of future operating costs to disallow if an activity is removed from the regulatory till should be relatively small. Nevertheless, such questions may arise when thinking about an appropriate allowance in the regulatory till for head-office costs, for example.
- 3.29 One concern is that there will be “competition” between what is inside the regulatory till and outside the regulatory till, a competition where both “businesses” are managed by the same entity. The DAA’s incentives will be for profits to accrue to activities outside the regulatory till; users will face higher airport charges if this leads to lower commercial revenue forecasts at subsequent determinations. It is for this reason that throughout this paper we have talked about removing an activity from the regulatory till, rather than excluding a particular investment. We want to avoid providing distorted incentives so it is unlikely that, for example, we would support having some DAA-owned short-term car parks in the regulatory till and some outside. We would normally expect to either include or exclude the whole activity from the regulatory till.
- 3.30 This only provides a partial solution. Businesses evolve. An airport city may, over time, start offering activities that the DAA was already offering elsewhere within the airport campus. The effect may be to reduce the commercial revenues from activities remaining within the regulatory till. A balance needs to be struck between limiting the incentives for this potential regulatory gaming and not restricting unnecessarily the DAA’s ability to respond to the evolving business environment when managing commercial ventures around the airport that have been excluded from the regulatory till.
- 3.31 Moving to a regulatory environment where some activities generating commercial revenues are within the regulatory till and others outside may create some perverse incentives. It may distort future investment incentives. For example, if car parks are outside the regulatory till the DAA’s incentives to invest in other transport modes may be reduced if such investments might reduce demand for its car parks.
- 3.32 Further work addressing these concerns is necessary. This is true in the case of Dublin airport city, where we have previously indicated an intention to exclude the project from the regulatory till with the support of both airlines and the DAA. It will also be true for any other future investments which we are minded to exclude from the regulatory till. We would need to identify what activities the investment will provide and whether there are existing activities at the airport that are similar and warrant being removed from the regulatory till. We would also need to identify what, if any, restrictions the

DAA would be expected to agree to in terms of future developments for an investment excluded from the regulatory till.

4. Summary and next steps

- 4.1 This paper has sought to set out our current thinking, rather than detail a final regulatory position. At this stage, we do not envisage switching to a dual-till regime in 2014, but we are willing to consider changes to the regulatory till where that might facilitate investments in commercial activities by the DAA that users of aeronautical services do not support. We are keen to provide a regulatory environment which encourages the DAA to behave commercially. While we are comfortable applying regulatory oversight to investment proposals relating to aeronautical activities, we are keen to explore if there are alternatives to the Commission having to second-guess proposed commercial investments.
- 4.2 We have developed criteria we intend to use when deciding whether to exclude an activity from the regulatory till. The table below may help readers thinking about what investments might be affected should the proposals in this paper be adopted. It lists investments in the DAA's 2009 CIP that might have generated commercial revenues, and identifies those that would have been the strongest candidates for removal from the regulatory till had we adopted the approach outlined in this paper at the time of the 2009 determination. The table is indicative and merely intended to provide guidance.


Capex Grouping or Project	Accounting separation straight-forward?	Scope for users and airport to support removal from till?	Value in CIP
Step in the decision tree	1. 	2.	
Airport Operations			
CIP2.017 Hangar Maintenance	Yes	Yes: airlines did not support the investment	€4.2m
Landside Infrastructure			
CIP3.012 New taxi holding area	Yes	Yes: airlines did not support the investment	€4.0m
CIP1.016 Refurbishment of existing MSCP Blocks A, B & C	Yes	No: airlines did not support the investment BUT potentially significant implications for the RAB to remain "airport charges neutral" given car-parking revenues accounted for over 20% of forecast commercial revenues.	
Utilities			
CIP9.024 Fuel farm redevelopment	Yes	No: airlines indicated some support for investing in fuel-farm facilities at the airport.	
Retail			
CIP5.013 Retail Refurbishments	No		
Revenue			
CIP1.006 MSCP	Yes	No: airlines did not support the investment BUT potentially significant implications for the RAB to remain "airport charges neutral" given car-parking revenues accounted for over 20% of forecast commercial revenues.	
CIP2.018 Cargo distribution centre	Yes	Yes: airlines did not support the investment	€14.3m
CIP2.016 DAA tenant accommodation	No		
CIP2.014 Retail logistics centre	No		
Stands and Airfield			
CIP6.009 Engine testing facility	Yes	No: airlines indicated some support for investing in such a facility if demand for aeronautical services grew.	

Table 3: **Identifying what commercial investments in CIP2009 might have been candidates to exclude from the regulatory till**

- 4.3 There is no intention to review all activities currently included in the regulatory till. Instead, we envisage conducting such a thought experiment on a case-by-case basis should the DAA propose a future commercial investment for which there were indications that users did not support the investment. Between now and the 2014 determination, there may be merit in considering in more detail specific candidate investments that might warrant a change to the regulatory till. This will allow all parties to see how the changes might work in practice and identify if there are problems that to date we have not foreseen. In the process, we hope to provide more details on how exactly we might consider changes to the regulatory till.
- 4.4 Looking beyond 2014, we continue to aspire to a situation where capex plans can evolve as the business environment dictates, and not be constrained by the need for regulatory reviews every four-plus years by the regulator. We have previously indicated our proposed regulatory approach in instances where users and the airport agree to revised investment plans between determinations.⁴ For commercial investments, to the extent possible we would like to move to an environment where the DAA and users can agree to disagree about the business case for a commercial investment and know how the investment is likely to be treated should the DAA decide to proceed in advance of the next determination. Unfortunately, we are pessimistic that we will be able to outline an approach that provides such information for all possible future commercial investments.
- 4.5 Parties are invited to comment on the thoughts expressed in this paper and how future work on this topic might proceed. We do not envisage revisiting the specific question of single-till versus dual-till regulation, but we are keen to hear representations about how best to treat investments in non-aeronautical services where users and DAA disagree. Such responses may comment on
- the merits of the approach we have outlined,
 - whether there are important considerations that we have not addressed, and
 - how best the work might proceed.
- 4.6 Our goal is to have consulted fully with users on all the practical issues that might be associated with any change to the regulatory till in time for the 2014 determination. Clearly, between now and then the DAA will need to develop its investment plans and consult with users to establish if there are commercial investments which might best proceed outside the regulatory till following an adjustment to the RAB. We will be happy to use such candidate commercial investments to provide more detailed guidance on how the proposed refinements to setting future determinations might work in practice.
- 4.7 Responses to this consultation paper should be titled "Future Investments and the Regulatory Till" and should be received no later than Wednesday 27 June 2012 at 5pm, and should be sent to

⁴ See Annex 3, CAR "Determination on the Maximum Level of Airport Charges at Dublin Airport". CP4/2009. http://www.aviationreg.ie/fileupload/2009_CP4_Final%20Determination_4DEC.pdf

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- 4.8 Respondents should be aware that the Commission is subject to the provisions of the Freedom of Information legislation. It is the usual practice to place all submissions received on our website. If submissions contain confidential material, it should be clearly marked as confidential, and a version of the submission should be provided which can be used for publication.
- 4.9 The Commission may also include the information contained in responses in reports and elsewhere as required. Ordinarily, the Commission does not edit this material. Any party submitting information to the Commission shall have sole responsibility for the contents of such information and shall indemnify the Commission in relation to any loss or damage of whatsoever nature and howsoever arising suffered by the Commission as a result of publication or dissemination of such information either on its website, in its reports or elsewhere.
- 4.10 While the Commission uses best endeavors to ensure that information on its website is up to date and accurate, the Commission accepts no responsibility in relation to and expressly excludes any warranty or representations as to the accuracy or completeness of the contents of its website.