

British Airways' Response to the Commission for Aviation Regulation Report CP6/2001 - Draft Determination of Proposed Maximum Levels of Airport Charges

British Airways welcomes the opportunity to respond to the Draft Determination of Airport Charges and the Regulatory Framework to be established by the Irish Commission for Aviation Regulation.

Our response is set out as chronological comments to the points raised in the Commissions Report.

3. Proposed Degree of Reliance on Statutory Factors

We welcome the detail and specificity of the 10 factors contained in Section 33 of the Aviation Regulation Act, 2001. Such detail serves to minimise misunderstanding in the interpretation of the objectives of the Commission in carrying out its functions.

We would urge the Commission to ensure that the economic welfare of all the users of the airports be given an equal priority as the economic welfare of the airports in any decisions reached by the Commission. Airlines, which operate in a competitive business environment, are the best proxies for the interests of passengers. Therefore, by recognising the importance of the economic welfare of airlines the Commission would be pursuing policies which further the public interest of passenger's; the passenger's benefiting from the pricing levels and quality of services presented to the market by airlines healthily and actively competing for their custom.

Statutory Factors

1. "the level of investment in airport facilities at an airport to which the determination relates, in line with safety requirements and commercial operations in order to meet current and prospective needs of those on whom the airport charges may be levied"

It is of vital importance that the Capex needs of users be considered in determining the investment programme at the airports which will be recoverable from airport charges. The Commission should ensure that the users have played a full and transparent part in any consultation process to determine the capex needs and that the investment planned by the airport is such that it will meet the current and prospective needs of the users who pay the charges. The Commission should also ensure that the airports are measured against providing the level and type of investment agreed at the time of setting the price cap with a reduction in airport charges if the capex is not being provided as planned. The fairest way of funding the development of infrastructure from a monopolist supplier, and the manner which most closely replicates the construction industry, would be for users to only pay for a facility once users are able to occupy it and engage in the operational activities for which it was intended.

4. *“the contribution of the airport to the region in which it is located”*

British Airways considers that each airport within any group of airports should fund investments from revenues specific to that airport. Users at airport A should not be burdened with costs intended to provide for investment at airport B. The Commission should ensure that the capex plans of each airport within the group provide the clarity needed by users to identify and track investments at each airport.

5. *“the level of income of the airport authority from airport charges at the airport and other revenue earned by the authority at the regulated airports or elsewhere.”*

British Airways welcomes the recognition by the Commission that users should benefit from generating economic activity at an airport through aeronautical and commercial income streams being included in the regulatory tills of the airports.

However, we see increased complexity, the potential of gaming on the part of the airports and the need for regulatory intervention under the proposal of the Commission to exclude new commercial activity from the regulatory till at Dublin airport. That is to say a forward looking dual till. What would be deemed to be new commercial activity, on what criteria, and by whom will such decisions be made? Aeronautical charges will only be reduced under a single till regime if the airport makes a determined effort to increase commercial activity and from growth in the number of passengers. Devoting more terminal space to commercial activities will actually reduce the operational efficiency of the airport to process the increasing numbers of passengers. Incentivising the airport to increase commercial activity to the detriment of operational functionality in the face of increasing passenger numbers sends the wrong signal to the airport company. It also allows the monopoly airport company to reap supernormal profits directly from the extra expense incurred by airlines, already operating with low margins in a competitive business environment, who are facilitating the demand for air transport being generated by the economic activity of the city of Dublin not Dublin airport.

An important advantage of the Single Till is that it actually gives the airport an added incentive to develop and grow in order to develop retail opportunities in the new or redeveloped facilities. At the same time the Single Till also ensures that the economic surplus generated from commercial revenue is not kept solely by the monopoly airport company but is used to benefit the whole air transport community ; that is to say Airports, Airlines and Passengers. It is a virtuous spiral.

Airports over simplify the issue when they state that any commercial profits are simply passed on to airlines by forcing down charges. In the UK model of airport regulation used to regulate BAA’s London airports and Manchester Airport the application of the Single Till is such that the airports have the incentive to maximise commercial revenue in the 5 years of a regulatory period. The benefit to the airport is that if the out turn commercial revenue is more than was forecast when the Single Till was set at the beginning of a regulatory period the airport keeps the commercial revenue surplus which it can use to increase shareholder value. Each regulatory period repeats this cycle with airports benefiting from increases in commercial revenue. The regulatory framework ensures that these extra revenues are not kept exclusively by the airport but are used to distribute this benefit to all the parties which contributed to its generation when the Single Till is set at the next review taking into account : capex plans, passenger numbers, non-aeronautical revenue.

Whilst there are other issues with the UK system of regulation, the model of the application of the Single Till in the UK does provide a half way house allowing airports to benefit from additional commercial revenue in the short term while enabling airlines and therefore passengers to share in the benefits from commercial revenue in the long term through the application of the Single Till.

An increasing number of airports are making the assertion that the commercial revenue earned in a dual till framework could be used to finance infrastructure investments. However, it should be noted that in the UK model of the Single Till the cost of financing any additional capacity or facilities which have been agreed between the airport and airline community is already a cost element within the Single Till. This means that commercial revenue already contributes to infrastructure development costs through the Single Till and is not immediately used to reduce aeronautical charges. In the application of a dual till, would Dublin airport be prepared to use the increased commercial revenue kept by them to finance capital expenditure in a way which reduces the need for airlines to pay for infrastructure through airport charges on a pound for pound basis? This would be the fairest way to fund infrastructure under the forward looking dual till system being considered by the Commission and is what the Single Till already achieves in a less complex manner.

It is very important that the forecasts of passenger numbers and revenue requirements used in setting the price cap through the Single Till be as accurate as possible as it is recognised that airports have the incentive to under-forecast passenger numbers and game the system in a price cap based revenue yield framework.

A problem which could occur through the application of a dual till is that it would skew airport development to retail facilities and away from operational requirements. This would not be in the interests of airlines but it would also not be in the interests of passengers either. The danger is that important aspects of customer service and operations become compromised by an excessive emphasis on retail development at the expense of operational efficiency.

Passengers have indicated that the scope and number of retail facilities, whilst being of interest to them, are not fundamental to their airport experience. Evidence has shown that passenger's priorities are; the ability to move quickly and efficiently through an airport, with the best level of customer service, minimum check-in times and short connection times between terminals. These are operational criteria which airlines, in the interests of passengers, seek to have provided as optimally as possible. Therefore British Airways does not support a move to a forward looking dual till system at Dublin airport as it would then have the incentive to develop increased amounts of commercial facilities which could compromise operational efficiency and therefore would not be in the public interest.

7. *“the level and quality of services offered at the airport by the airport authority and the reasonable interests of users of those services.”*

We welcome the implicit recognition by the Commission of the incentives to the regulated airports to allow quality of service levels to drop in a price cap regulatory environment as a means of saving costs and maximising returns.

We believe the existence of robust measures of quality with effective implementation policies are fundamental both to furthering the reasonable interests of users, both providers of air transport services and passengers. The object of implementing binding regulated service standards should be to achieve alignment of the provision of airport service, with airline needs, and the expectations of passengers.

The Commission should concentrate on core provisions including timely provision of capacity, and operational effectiveness, particularly as measured by punctuality.

The overriding target when a service quality regime is being implemented should be punctuality and the factors which materially contribute to it. Therefore, the Commission should establish binding service standards for the provision of core services such as jetty availability, people movers, security queuing, planning standards, ramp services, baggage systems and stand availability. The measures of quality used should be as simple as practicable, measurable, and incorporate specific trigger points requiring corrective action when service standards fall below agreed minima. The Commission should ensure that granting of rights to the airports to levy aeronautical charges should be conditional on the existence of agreed binding service standards which in the event of these not being achieved results in some form of rebate or compensation payment to users. These standards should be incorporated in the Conditions of Use publications of the airports in order for users to have an assurance of receiving certain levels of service in exchange for the charges paid.

The majority of passengers have scant interest in the ownership or provision of facilities at the airport - they hold their chosen airline responsible for their passage through the airport - whether it is queues at check-in, security, walks to the departure gate, bussing or non-delivery of baggage. Airlines are the de facto guardians of passengers' interests in airport infrastructure and services and as such have a primary interest in meeting consumer needs. It is essential that the operations of airlines are not hampered by the provision of poor levels of service from the regulated airports. Airlines operate in conditions of high competition; this fact ensures that they strive to keep their services aligned as precisely as possible with the needs and expectations of their passengers.

A combination of the airport specific and internationally accepted planning standards could be used in setting a generic level of service which all airlines and passengers could expect from a given airport under all circumstances.

Airlines should then be able to request service levels above the generic standard, for which a premium may be paid. However, the generic service standard should not be set so low as to make it necessary for most airlines to put in place bilateral agreements in order to reach a standard level of service that is acceptable to users. In addition bilateral agreements must only address the achieving of higher standards than the generic. No bilateral agreement should be permitted that arranges for service levels that are below the generic standard at a lower price than standard airport charges. This would place a disproportionate burden of cost on the majority of airlines who wish to operate to the generic standard.

5. Explanatory Memorandum

iii/A) “The Commission proposes applying a price cap to an airport’s average revenue per Work Load Unit (WLU).”

The revenue yield approach remains the preferred form of price cap regulation although we would agree that when it is designed to allow a revenue yield per passenger, it can incentivise the airport companies to focus on passenger volumes at the expense of other outputs. By selecting a composite denominator such as a hybrid between passenger numbers and air transport movements airports should be focused on a greater number of outputs, and incentivised to provide those facilities/services which maximise those outputs.

It is very important that a framework of consultation fora be set up between the airports, users and the Commission with good transparency for all aspects of charges and rents. This would allow users to have a meaningful role in charges and rents negotiations and an understanding of the value obtained in exchange for the charges paid.

iii/B) “The Commission wishes to investigate the feasibility of a tariff basket of revenues.”

Before taking a view on the feasibility of a tariff basket users should be shown detailed tariff basket price modelling using the same forecasts as used in setting the revenue yield price cap as currently suggested by the Commission. This would allow users to take a more informed view on the benefits or not of a tariff basket approach.

Therefore unless and until the Commission demonstrates tangible benefits from a tariff basket the revenue yield price cap would still be British Airways’ preferred approach.

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