



**Maximum Levels of Airport Charges  
at Dublin Airport**

**Commission Paper CP6/2006**

**PUBLIC CONSULTATION ON THE CARRYING OUT OF AN  
INTERIM REVIEW OF THE SEPTEMBER 2005 DETERMINATION  
ON THE MAXIMUM LEVELS OF AIRPORT CHARGES AT DUBLIN  
AIRPORT**

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Commission for Aviation Regulation  
3<sup>rd</sup> Floor, Alexandra House  
Earlsfort Terrace  
Dublin 2  
Ireland

Tel: +353 1 6611700  
Fax: +353 1 6611269

**E-mail [info@aviationreg.ie](mailto:info@aviationreg.ie)**

## TABLE OF CONTENTS

<b>1. EXECUTIVE SUMMARY .....</b>	<b>3</b>
<b>2. CONSULTATION QUESTIONS .....</b>	<b>6</b>
<b>3. BACKGROUND: THE 2005 DETERMINATION AND THE 2006 CIP .....</b>	<b>7</b>
<b>4. LEGISLATIVE BASIS FOR A REVIEW OF A DETERMINATION ....</b>	<b>8</b>
<b>5. INTERPRETATION OF 'SUBSTANTIAL GROUNDS' .....</b>	<b>9</b>
5.1 PRECEDENTS .....	9
5.2 FUTURE APPLICATION .....	12
<b>6. DO CURRENT CIRCUMSTANCES PROVIDE SUBSTANTIAL GROUNDS? .....</b>	<b>15</b>
<b>7. SCOPE OF A REVIEW.....</b>	<b>19</b>
<b>8. TIMETABLE FOR A REVIEW .....</b>	<b>22</b>
<b>9. ADMINISTRATIVE MATTERS .....</b>	<b>24</b>
9.1 PURPOSE OF CONSULTATION PAPER .....	24
9.2 CALL FOR SUBMISSIONS .....	25
9.3 PUBLICATION OF SUBMISSIONS .....	26
<b>LEGAL NOTICE .....</b>	<b>26</b>
<b>INDEMNITY .....</b>	<b>26</b>

## **1. EXECUTIVE SUMMARY**

1. The Commission for Aviation Regulation (the "Commission") is responsible for periodically determining the maximum levels of airport charges that may be levied by the Dublin Airport Authority (the "DAA") at Dublin Airport. The Commission's most recent determination (the "2005 Determination") was published on 29 September 2005 after an extensive period of analysis and consultation.
2. The Commission indicated in September 2005, that it might be appropriate to review the 2005 Determination once the Commission and other interested parties would have had time to consider the final Capital Investment Plan (CIP) to be proposed by the DAA.
3. It is a statutory obligation of the Commission to decide whether substantial grounds exist to review a Determination. On the previous occasion on which the Commission considered undertaking an interim review, it reached the conclusion that 'substantial grounds' for a review should be interpreted in a manner consistent with the Commission's statutory objectives in making a determination. The Commission continues to believe that the 'substantial grounds' criterion should be interpreted in a manner consistent with the Commission's statutory objectives in making a determination. The Commission's interpretation of those objectives (set out in CP9/2004) is that the essence of its statutory mandate is to promote economic efficiency.
4. The Commission considers that the primary mechanism by which its determinations of maximum airport charges promote efficiency is the incentive effect of additional profits that would arise if the regulated company performs more efficiently than the Commission reasonably estimated at the time of a determination.

5. An expectation that interim reviews could interrupt the period of a determination, for other than truly exceptional circumstances, would reduce the power of incentives to promote efficiency as required by the Commission's statutory objectives. A propensity for interim reviews would also have other detrimental effects on efficiency. It is considered that these detriments would escalate were there to be a multiplicity of interim reviews in a single price control period.
6. There should be a presumption against holding reviews other than in exceptional circumstances, that are outside the control of the DAA, and where the financial or other effects of those circumstances are liable to be large enough to compromise the achievement of the Commission's statutory objectives unless the original decision were reviewed. Only in such a situation might a review – after taking account both of the certain detriments and the possible benefits – have a positive net effect on incentives.
7. The Commission has considered the circumstances in which the DAA was unable to provide a finalised CIP to the Commission, prior to the statutory deadline for the 2005 Determination, and has concluded that the particular combination of circumstances appears to meet the criterion of substantial grounds and thus warrant the holding of a statutory review. It should be noted that a decision to hold a review is entirely separate from a decision about whether to revise a price cap consequent on a review.
8. An option for a review, which is currently viewed sympathetically by the Commission, would be, as far as possible, to consider the data and arguments before the Commission as they were in September 2005 *except that* the 2006 DAA investment plan (and associated materials) would be substituted for the May 2005 DAA investment plan. It may also be necessary to recognise other material consequences for other model inputs if they arise directly from the revised plans for the capital programme. However, at present, the Commission does not envisage that any such consequences will be material to the review and it will need to be furnished with good evidence to be persuaded otherwise, especially as the second terminal is, at present, due to open in late 2009, only some months from the end of the present regulation period (2006-2009). In particular, matters that were comprehensively rehearsed during the work for the

September 2005 Determination do not appear to the Commission at this stage to meet the Commission's threshold for substantial grounds for a review.

9. The Commission anticipates that any review would examine the 2006 CIP and the justifications provided for it by the DAA to inform the Commission's conclusion about the extent to which it should adopt the 2006 CIP in the calculation of any adjustment to the 2005 Determination.

10. The Commission now wishes:

(I) to advise that it has decided in accordance with section 32 (14) (a) of the 2001 Act that there **appear to be** 'substantial grounds' to conduct a statutory review (the "Review") of the 2005 Determination; such grounds for a review include, but are not limited to the following:

(a) a requirement to analyse the forthcoming 2006 CIP for Dublin Airport arising from the circumstances surrounding the unavailability of a finalised CIP at the time of the 2005 Determination;

(II) to advise that it has decided in accordance with Section 32 (14)(a) of the 2001 Act that there **may be** 'substantial grounds' to conduct a review of the 2005 Determination; such grounds for a review including but are not limited to the following:

(b) the degree to which airline users of Dublin Airport have revised their anticipated requirements for airport facilities such that the DAA has developed a substantially larger capital programme.

and

(III) to invite comments generally and in respect of the consultation questions raised in this document.

**11.** The Commission requests interested parties to submit responses to the questions raised in this consultation paper no later than **12 noon on Thursday 28 September 2006.**

## **2. CONSULTATION QUESTIONS<sup>1</sup>**

1. *Do you agree with the Commission's conclusion on the types of circumstances necessary to justify holding an interim review? Please provide reasons and, where appropriate, evidence.*
2. *Do you consider the degree to which airline users of Dublin Airport have revised their anticipated requirements for airport facilities (such that the DAA has developed a substantially larger capital programme) to provide the basis for exceptional circumstances?*
3. *Do you consider the degree to which airline users of Dublin Airport have revised their anticipated requirements for airport facilities to be liable to give rise to financial or other effects that are large enough to compromise the Commission's statutory objectives unless the September 2005 decision is reviewed?*
4. *Do you consider the circumstances surrounding the unavailability of a finalised CIP at the time of the 2005 Determination to have been exceptional? If you consider the circumstances exceptional, is this for any of the reasons suggested as possibilities in this paper or for some other reason?*
5. *Do you consider the circumstances to have been outside the control of the DAA?*
6. *What do you consider should be the scope of any review? Do you consider that the scope of any review should be limited as far as possible to the matters directly affected by the circumstances justifying the review?*

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<sup>1</sup> For ease of reference, the specific questions to which the Commission is inviting responses are collected together in this section of the paper; they also appear in the body of the document following the discussion of the material to which they relate.

### **3. BACKGROUND: THE 2005 DETERMINATION AND THE 2006 CIP**

The Commission is responsible for periodically determining the maximum levels of airport charges that may be levied by the DAA at Dublin Airport. The Commission's most recent determination, covering the period January 2006 to December 2009, (the "2005 Determination") was published on 29 September 2005 (as CP3/2005) after an extensive period of analysis and consultation. The Commission was required by the State Airports Act, 2004 (the "2004 Act") to publish its decision before 1 October 2005.

The Foreword to that Decision noted that a key driver of the 2005 Determination was the implementation by the DAA of the Government's Aviation Action Plan (released in May 2005) and the delivery of cost-effective capacity at Dublin Airport in a timely manner. Although the DAA had furnished the Commission with a proposed capital investment programme (CIP) on 9 May 2005, that plan predated the Aviation Action Plan. The DAA undertook to review its CIP in the light of the Aviation Action Plan and further to consult with stakeholders at the airport. However, the DAA was unable to deliver a final revised CIP to the Commission within the timeframe prescribed for the publication of the Determination. Furthermore, the Government had not at that stage initiated its independent verification of the costs of a second terminal, this being one pillar of the Government's triple safeguard set out in the Action Plan to ensure maximum efficiency and cost effectiveness.

In the absence of a final CIP, the Commission made an independent assessment of the company's May 2005 CIP and provided an allowance in the price cap for an indicative capex programme based on the analysis by its consultants. The consultants who prepared that assessment made it clear that their "top down analysis is not sufficient by itself to provide a safe basis for a firm capital expenditure needs assessment covering a control period of four or five years. It may provide the basis for a provisional assessment provided there is an expectation it will be supplemented with a more considered bottom-up assessment after this review".<sup>2</sup>

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<sup>2</sup> 'Review of the Capital Programme', IMR/WHA, Annex 8 to CP3/2005, p.7

The Commission accordingly indicated, in CP3/2005, that it might be appropriate to review the 2005 Determination once the Commission and other interested parties (including the Government's own verification experts) had time to consider the final CIP to be proposed by the DAA.

In recent months, the DAA has made a number of presentations to the Commission outlining its work towards finalising its 2006 CIP. It is evident that DAA has carried out a wide-ranging review of its investment requirements over the remaining part of the current price control period, and beyond, and it has indicated that it will shortly deliver to the Commission a new 2006 CIP. The DAA has also indicated that the 2006 CIP will propose a substantially larger (and more front-loaded) investment programme than the Commission allowed for in its 2005 Determination.

#### **4. LEGISLATIVE BASIS FOR A REVIEW OF A DETERMINATION**

Subsection 32(14)(a) of the Aviation Regulation Act, 2001 (the "2001 Act"), as amended by the 2004 Act, states:

"The Commission may after the making of a determination—

- (i) at its own initiative, or
- (ii) at the request of an airport authority or user concerned in respect of the determination,

if it considers that there are substantial grounds for so doing, review the determination and, if it sees fit, amend the determination."

It is, therefore, a statutory obligation of the Commission to decide whether substantial grounds exist to review the 2005 Determination.



## **5. INTERPRETATION OF 'SUBSTANTIAL GROUNDS'**

### **5.1 Precedents**

Under the legislation, the Commission is required to consider whether or not there are substantial grounds for a review of a determination. On the previous occasion that the Commission considered undertaking a mid-term review, it reached the conclusion that 'substantial grounds' for a review should be interpreted in a manner consistent with the Commission's statutory objectives in making a determination. In 2003, this was done with reference to the Commission's (then) single statutory objective:

"to facilitate the development and operation of cost-effective airports which meet the requirements of users."

In that context, the Commission considered how a review would affect the incentives for a regulated firm to develop and operate an airport efficiently. The Commission's thinking in terms of 'substantial grounds' was set out in Commission Paper CP3/2003<sup>3</sup> in the form of the following two principles:

- (i) One of the key indicators of the effectiveness of incentive regulation is the extent to which the financial consequences of decisions by the regulated firm are borne by the firm rather than being passed on to the consumers. This requires sufficient time between determinations to reflect developments in actual conditions, some of which will be outside the management's control. This period of time should be sufficiently long as to provide strong incentives for efficient operations.
- (ii) In general, the scope of a review at an interim stage should be limited in the main, to matters of an exceptional nature, which are generally outside the control of the regulated firm.

In CP3/2003 the Commission also argued that as "it is a very desirable characteristic of economic regulation that it offer maximum price certainty, it follows that there should be a presumption against holding a mid-term review

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<sup>3</sup> All of the Commission's papers are available on its website [www.aviationreg.ie](http://www.aviationreg.ie)

unless events have occurred which significantly affect the objectives of the original decision. This is consistent with the approach of the Act, which is to provide intermittent quinquennial determinations, with interim reviews if there are substantial grounds for them, so as to ensure stability and predictability in the meantime.” (CP3/2003 p7-8)

Prior to 2003, the Commission in its first airport determination<sup>4</sup> also briefly considered some possible circumstances for an interim review. It argued that a failure to deliver an additional Pier (since named Pier D) at Dublin Airport for which adequate funding had been included in the computation of the price cap, could constitute substantial grounds for a review.<sup>5</sup>

The current statutory objectives of the Commission are set out in Section 33 of the 2001 Act (as amended by the 2004 Act). These are:

- (i) to facilitate the efficient and economic development and operation of Dublin Airport which meet the requirements of current and prospective users of Dublin Airport,
- (ii) to protect the reasonable interests of current and prospective users of Dublin Airport in relation to Dublin Airport, and
- (iii) to enable Dublin Airport Authority to operate and develop Dublin Airport in a sustainable and financially viable manner.

Following the passage of the 2004 Act, the Commission considered the impact of the amendments made by that Act to the 2001 Act. It concluded:

“the new explicit reference to the efficient and economic operation and development of Dublin Airport strengthened the basis for [the Commission’s] view that the essence of its statutory mandate is to promote economic efficiency. In addition to strengthening the basis for its approach of promoting economic efficiency, objective (a) can also be seen as a replacement of the previous Section 33(b) of the 2001 Act, which required the Commission to have due regard to the regulated company

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<sup>4</sup> Published as CP7/2001, CP8/2001 and CP9/2001.

<sup>5</sup> See CP9/2001, part VI, para 422, p.157. Also, a failure by the airport to meet specified measures of service quality was given as a possible ground for a review (CP9/2001, part VI, para 184, p.76).

earning a reasonable rate of return on capital employed. Providing for a reasonable rate of return encourages the entity providing the regulated services to make efficient decisions regarding the amount of capital to invest in the regulated activities.

Providing for the regulated firm to earn a reasonable rate of return on capital employed in the investment, thereby allowing the sustainable and financially viable operation of the airport is in the interest of users. This approach, which facilitates dynamic efficiency, best meets the newly framed statutory objective, having regard to the level of investments in line with safety requirements and commercial operations in order to meet current and particularly prospective needs of users. In this regard statutory objectives (a) and (b) are closely linked.

The Commission is of the view that it should attain its objective of enabling DAA to operate and develop Dublin Airport in a sustainable and financially viable manner while also providing incentives for DAA to operate and develop in an efficient manner and protecting the reasonable interests of users. The Commission is of the view that objective (c) requires the testing of the financial robustness of its regulatory proposals in the context of measuring the financial risks likely to face a regulated firm operating in a reasonably efficient manner.

The Commission is of the view that equal weight must be given to all three objectives and that one does not have precedence over the others. " (CP9/2004, p.44-45).

The Commission continues to believe that the 'substantial grounds' criterion for a review should be interpreted in a manner consistent with the Commission's statutory objectives in making a determination. The Commission's interpretation of those objectives, as set out above, is that the essence of its statutory mandate is to promote economic efficiency.

## **5.2 Future application**

The Commission considers that the primary mechanism by which its determinations of maximum airport charges promote efficiency is the incentive effect of additional profits that would arise if the company performs more efficiently than the Commission reasonably estimated at the time of a determination. This incentive effect is dependent on there being a passage of time between making estimates (and basing a determination thereon) and the corresponding outturns. It is during this period that the regulated company is free to take actions that would enhance its profitability. Thus the incentive effect is directly governed by the period of time that elapses between reviews.

The incentive mechanism is relevant to all decisions with an economic effect that must be made in respect of the regulated business, including decisions following unanticipated exogenous events. The regulated business is not assumed to be risk-free and the management of risk is a central responsibility of any business management. A simple pass through of new or exogenous costs to the customers of the regulated firm would leave the regulated firm with no incentive to minimise the detrimental cost or service impacts (or maximise the advantageous impacts) of those events.

An expectation that interim reviews could interrupt the period of a determination, for anything other than truly exceptional circumstances, would thus be liable to reduce the power of incentives to promote efficiency as required by the Commission's statutory objectives.

The implication of these considerations accordingly means that in so far as the Commission is concerned, any review undertaken in 2006, would be the only interim review that it would be minded to initiate under Section 32 (14) during the period 2006-2009.

A propensity for interim reviews would also have other detrimental effects on efficiency:

- (i) confidence would be reduced in the stability and predictability of the economic regime, and uncertainty for the DAA, for providers of finance and for airport users could increase;

- (ii) incentives on the DAA to provide the Commission with timely and properly justified information for price reviews could be weakened, possibly seriously;<sup>6</sup> and
- (iii) additional staffing and consultancy costs would be incurred by the Commission, the DAA and by other participants in consultation.

It is considered that these detriments would escalate were there to be a multiplicity of interim reviews in a single price control period.

The Commission therefore considers that the grounds for an interim review need to be sufficiently strong to outweigh those incentive and other detriments that would arise from uncertainty about review or from an expectation of a low threshold for review. There should be a presumption against holding interim reviews other than in exceptional circumstances, that are outside the control of the DAA, and where the financial or other effects of those circumstances are liable to be large enough to compromise the achievement of the Commission's statutory objectives unless the original decision were reviewed. Only in such a situation might a review – after taking account both of the certain detriments and the possible benefits – have a positive net effect on incentives. Expressed alternatively: substantial grounds for a review would be held to exist only if *not* holding a review would be more harmful to efficiency<sup>7</sup> (which in the Commission's view is the essence of its statutory objectives) than holding a review, even allowing for the known detriments to efficiency of the latter.

For the incidence of review to be exceptional, the threshold for substantial grounds would need to be high enough for the occurrence of an interim review within a determination period to be rare. The Commission considers that its regulatory regime – taking into account financial headroom implicit in profit allowances, the in-period price control formulae and the arrangements for adjustments affecting airport charges in subsequent periods – already accommodates normal levels of uncertainty.

Such a threshold might be satisfied: where the financial or other effects are outside a reasonable range of expectations at the time of a determination; or where (exceptional) uncertainties around significant elements of the forecasts

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<sup>6</sup> This important matter is taken up again at the end of section 5 below.

<sup>7</sup> Including productive, dynamic and allocative efficiency, see p. 44 of CP9/2004.

required for the determination were so great that the Commission considered its objectives may not be robust to a reasonable range of expectations at the time of a determination without explicitly relying on the possibility of an interim review.

Finally, in making its decision regarding any interim review, the Commission is mindful of the desirability of regulatory consistency. Thus, the statements in the Commission's September 2005 Determination that an interim review might be appropriate<sup>8</sup>, would make the Commission, all other things being equal, more open to holding an interim review than otherwise.

The Commission considers that such an approach is consistent with the objectives of the Act.

*Consultation question*

1. *Do you agree with the Commission's conclusion on the types of circumstances necessary to justify holding an interim review? Please provide reasons and, where appropriate, evidence.*

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<sup>8</sup> The independent assessment of capex, on which the Commission relied in 2005, also described its work as a provisional assessment in need of a subsequent and more considered evaluation. See 'Review of the Capital Programme', IMR/WHA, Annex 8 to CP3/2005, p.7.

## **6. DO CURRENT CIRCUMSTANCES PROVIDE SUBSTANTIAL GROUNDS?**

The previous section identifies a three-stage test for substantial grounds:

- (i) Are the circumstances exceptional?
- (ii) Are the circumstances generally outside the control of the regulated company?
- (iii) Are the effects of those circumstances liable to be significant enough to compromise the objectives of the original decision without a review (taking into account the incentive and any other detriments that would in general also arise from a review)?

The current circumstances that provide grounds for an interim review, outlined in section 1 above, relate to DAA's 2006 CIP.

Are those circumstances exceptional? The Commission is awaiting a 2006 CIP from the DAA, and in particular the justifications concerning the main drivers for change that require the DAA to propose a substantially larger investment programme than set out in May 2005 CIP. At present, the Commission is open to the following possibilities:

- (i) that the Aviation Action Plan has required the DAA to change the basis on which it makes decisions on its capital programme;
- (ii) that users have, since May 2005, indicated a change in their anticipated requirements for airport facilities in the short or medium term, whether on account of a changed outlook for passenger volumes or of changes in airline business plans;
- (iii) that the DAA's wide-ranging review of its investment requirements has identified a capital programme that, although it involves higher levels of investment in the shorter term, will enable a more efficient and economical airport in the longer term than would have been possible had the May 2005 CIP been implemented.

The Commission is not necessarily persuaded that any of these reasons, by themselves, are sufficient to make current circumstances exceptional and outside the control of the DAA.

But in the circumstances of 2006, for example, it is possible, that without an interim review to consider the DAA's 2006 CIP, the dynamic efficiency of Dublin airport would be below the optimum. Specifically<sup>9</sup>, if, in the absence of an interim review, airport capacity were to be provided too late relative to demand growth, then airport users could be exposed to congestion costs, in the form of time costs (delays) as well as crowding and other discomfort, that could be inconsistent with the efficient and economic development of Dublin airport and also with the interest of current and prospective users.<sup>10</sup>

#### *Consultation questions*

2. *Do you consider the degree to which airline users of Dublin Airport have revised their anticipated requirements for airport facilities (such that the DAA has developed a substantially larger capital programme) to provide the basis for exceptional circumstances?*
  
3. *Do you consider the degree to which airline users of Dublin Airport have revised their anticipated requirements for airport facilities to be liable to give rise to financial or other effects that are large enough to compromise the Commission's statutory objectives unless the September 2005 decision is reviewed?*

The Commission believes that the circumstances surrounding the provision of a CIP at the time of the 2005 Determination appear to be exceptional. First, the 2004 Act required a new price determination to be concluded in 2005 i.e. within one year from the appointed day of the newly incorporated airport company. This brought forward by almost a year the designated time for a new determination.

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<sup>9</sup> See the Commission's position with regard to Pier D in its response to the report of 2006 Aviation Appeal Panel, CP5/2006, p13.

<sup>10</sup> On the other hand, it should be noted that an expectation of frequent or low-threshold review could increase perceived regulatory uncertainty and thus risk, and hence could raise financing costs of future capex programmes.



Second, the 2004 Act created a new and separate Board for Dublin Airport which took office in October 2004 and this led in turn to the appointment of a new DAA Chief Executive who took up his position in April 2005. The new DAA Board undertook a robust analysis of Dublin Airport's future capital requirements.

In addition, on 18 May 2005, the Government published its Aviation Action Plan. That Plan announced a revised policy approach, in relation to airport capacity. Specifically, the Government mandated the DAA:

- (i) To build a new Pier for aircraft parking stands at Dublin Airport, available from 2007; and
- (ii) To build a Dublin Airport Authority owned new Terminal (Terminal Two) at Dublin Airport to open in 2009.

Thus, the passage of the 2004 Act had two linked impacts on investment at Dublin Airport. The 2004 Act led (via the appointment of a new DAA Board) to a fundamental re-examination by the DAA of Dublin airport's investment plan, which, in conjunction with the Government's Aviation Action Plan, led to a very substantial increase in the time required by the DAA to produce a new CIP. At the same time, the 2004 Act reduced the time available for a price review by bringing forward the following review from 2006 to 2005. The combination of these impacts was to render the company unable to submit a final CIP to the Commission in time for it to be properly considered for the 2005 Determination.

Against this background, the Commission considers that the DAA might reasonably have required a longer period of time to conclude in a proper and thorough manner, a review of an investment programme as critical as the one now contemplated and that these circumstances can be regarded as exceptional.<sup>11</sup>

The Commission further considers that these circumstances may have been outside the control of the DAA's management. While these circumstances might

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<sup>11</sup> In the UK, where regulatory timetables are both much longer and give more discretion to regulators, it has been customary to extend deadlines for receipt of information following a major change in circumstances, such as ownership. (This occurred recently in UK aviation, following the change of ownership of the BAA.) Whereas a UK regulator has possessed the flexibility reasonably to extend deadlines, in the situation in which the Commission found itself in 2005, this was impossible, and thus the need for a review arises.

not be regarded as necessarily outside the control of DAA's shareholder, the Government, there is no evidence or suggestion that the Government had been acting other than in its capacity as legislator and policy maker for the transport sector rather than as the shareholder.

The final part of the three-part test relates to the scale of the effects. DAA has indicated to the Commission that the revised CIP will propose a substantially larger investment programme than the Commission allowed for in its 2005 Determination. The Commission accepts that the scale of the revised programme may be large enough for its viable implementation to be in doubt without a review of the 2005 Determination. In particular, the 2005 Determination was designed with a capex programme in mind that was not as substantial as the one that the Commission understands is now being contemplated by the DAA and therefore, may not be appropriate for the investment programme in the 2006 CIP.

#### *Consultation questions*

4. *Do you consider that the circumstances surrounding the provision of a revised CIP at the time of the 2005 Determination to have been exceptional? If you consider the circumstances exceptional, is this for any of the reasons suggested as possibilities in this paper or for some other reason?*
  
5. *Do you consider the circumstances to have been outside the control of the DAA?*

## 7. SCOPE OF A REVIEW

The 2001 Act provides that the provisions in the Act relating to the process leading to a determination<sup>12</sup> shall apply to any amendment made on foot of a review in the same way as to the making of the original determination. In other words, the process of an interim review is the same as the process for a determination. However, the scope of an interim review can be significantly more restricted.

It follows from the analysis set out in section 5 relating to the incentive detriment arising from a review, that the scope of an interim review should be no wider than necessary to address the grounds for that review. It should, in particular, not revisit assumptions made at the time of the determination that are not materially compromised by the circumstances relevant to the review.

Thus an option for a review, which is currently viewed sympathetically by the Commission, is that any review would, as far as possible, consider the data and arguments before the Commission as they were in September 2005 *except that* the 2006 DAA investment plan (and associated materials) would be substituted for the May 2005 DAA investment plan.

The Commission has been advised that the DAA's 2006 CIP will be structured to address a revised outlook for user requirements, including updated forecasts of passenger volumes. It may therefore be necessary, in order to maintain the internal consistency of the review assumptions, to adopt revised traffic forecasts for the review and to recognise the consequential impacts on operating costs and retail revenues.<sup>13</sup>

It may also be necessary to recognise other material consequences for operating costs, commercial revenues or other model inputs if they arise directly from the revised plans for the capital programme. However, at present, the Commission

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<sup>12</sup> For example, the issue of a Notice to interested parties, the provision of a consultation period, and the receipt of representations and the making and publication of a report.

<sup>13</sup> The financial model used by the Commission to compute future DAA airport charges in part relates operating costs and commercial revenues (according to various formulaic relationships) to forecast traffic; what is envisaged here therefore is the possibility of the application of an unchanged methodology for projected costs and certain classes of revenues to a new traffic forecast.

does not envisage that any such consequences will be material to the review and it will need to be furnished with good evidence to be persuaded otherwise, especially as the second terminal is, at present, due to open in late 2009, only some months from the end of the present regulatory period (2006-2009).

In particular, matters that were comprehensively rehearsed during the work for the September 2005 Determination – for example, the methodology used to project operating costs and commercial revenues, the treatment of the pension deficit, the impact on the company’s balance sheet of activities not directly related to Dublin Airport (GSH, Cork Airport, Shannon Airport), and the cost of capital – do not appear to the Commission at this stage to meet the Commission’s threshold for substantial grounds for a review. In addition, even if these matters were for some reason to be reviewed, as far as the Commission is aware, nothing has happened since September 2005 to warrant the Commission, in the light of its statutory objectives in making a determination, to change its stance on these matters.

The Commission envisages therefore that the focus of any review should be the implications of the 2006 CIP for airport charges at Dublin Airport. The Commission considers that an assessment of DAA’s capital programme and its efficiency is a central element of the economic regulation of Dublin Airport. Consequently, it is necessary that DAA’s investment plans be carefully scrutinised as to their timing and efficiency. This conclusion is supported by O’Sullivan J in his judgement,<sup>14</sup> which also considered the scope of a review of capital expenditure:

“In my view there is a specific duty on the [Commission] to review a subject airport’s capex.” . . . The Commissioner, “in carrying out his duty of regulating airport charges, has a positive duty to aim to facilitate the development of cost effective airports and while so doing must have due regard to the level of investment in the subject airport and is specifically equipped with a power to reject any proposals in relation, *inter alia*, to capex that may be submitted to him by the operators of the airport.” . . . “in carrying out this item by item review [, the Commission] is clearly doing what the Oireachtas intended [it] to do under the characterisation of

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<sup>14</sup> Aer Rianta cpt -v- Commission for Aviation Regulation, 2001 No. 707 JR per O’Sullivan, J

determining maximum airport charges and not under the characterisation of managing and developing an airport”

There can therefore be no presumption that the Commission will accept the 2006 CIP in its entirety, before reaching a conclusion for an interim review. It should be noted that a decision to hold a review is entirely separate from a decision about whether to revise a price cap consequent on a review.

The Commission has initiated preparations for a possible review. It has engaged consultants to assist it in an ongoing analysis of certain issues and these consultants will be further requested to examine matters arising under a review.

The Commission anticipates that any review would examine the 2006 CIP and the justifications provided by DAA to inform the Commission’s conclusion about the extent to which it should adopt the 2006 CIP in the calculation of any adjustment to the 2005 Determination.

In the event of a review, the Commission will also consult with the users of Dublin Airport.

The Commission, in the event of a review, will avail of such an opportunity to seek to strengthen the incentive framework of the prevailing price cap, especially in regard to the efficient procurement and financing of capital investment by the DAA, and for the development and continued evolution of the CIP after any review.

In order to address the issue of delayed delivery of important data and the circumstances in which this scenario could be used to undermine future price reviews, the Commission will give further consideration to the information requirements and review processes in advance of the next determination. Specifically, the Commission will consider the appropriate timetable and information ‘milestones’ necessary for the conduct of a price review for the period after 2009 that would be compatible with the maintenance of good efficiency incentives in order to seek to avoid a repetition of the apparent need for a review only shortly following a price decision. The time for the airport and airport users to debate and, if possible, agree the appropriate level of capital expenditure is at the time of a periodic determination. It is not the Commission’s intention, with regard to the holding of any interim review, to leave the impression that it is

willing to allow parties to come back with more information at a later date for whatever reason.

*Consultation question*

6. *What do you consider should be the scope of any review? Do you consider that the scope of any review should be limited as far as possible to the matters directly affected by the circumstances justifying the review?*

## **8. TIMETABLE FOR A REVIEW**

At this stage, it is very difficult for the Commission to comment with any precision on the time required for the conduct of a review. As of end-August 2006, the Commission has had a series of high-level briefings from the DAA and its advisors over recent months. These meetings were instigated at the Commission's request. They have tracked a very fluid investment plan with as yet no final list of projects, no precise timetables and no definite costs.

Thus the Commission is still awaiting finalisation of the key classes of information that would form the basis of a review of the price cap, and that would allow the Commission to decide whether a new price cap would meet the Commission's statutory objectives.

The Commission understands the present position to be that the DAA has itself not finalised<sup>15</sup> its 2006 CIP.

In any case, the Commission has as yet seen no investment plan, nor has it been provided with the critical supporting justifications for a proposed set of investments at a particular set of costs over a given horizon.

Therefore, without information even as to the scale of materials that it may have to consider, the Commission's best estimate of the time needed for the proper conduct of a review can only be indicative.

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<sup>15</sup> By 'finalised' CIP is meant in particular the budget that the DAA wishes to present to the Commission for the purposes of a possible price review, notwithstanding that fact that an investment plan necessarily continues to evolve over time for many different reasons.

In these circumstances, the Commission estimates that it would need a period of 6 months prior to publishing a Draft Determination. This period would be devoted to careful scrutiny of the company's investment plan. It would also allow for a round of consultation, if necessary, with interested parties on key substantive policy issues associated with the investment plan. A statutory consultation period of one month would follow. The Commission would then require at least one further month to carefully consider the statutory representations and to make a final Determination.

All told, this means that a review would be expected to take a period of some 8 months from the date of receipt of the 2006 CIP. This estimate assumes that no out of the ordinary issues would arise from consideration of the 2006 CIP.

However, given that the assets that will be built at Dublin Airport as part of the CIP will be in operation for many decades – perhaps even for most of the remainder of the 21<sup>st</sup> century – the most critical issue for a regulated firm is the average return it earns from those assets over their full useful lives. In that context, the price that prevails over the very attenuated horizon of 2007-2009 will be only a very modest part of the overall return. Any decision on the part of a regulated firm on the merits of proceeding with a multi-decade investment plan should rationally therefore, have a broader base than the actual returns arising from the 2007-2009 price control period. From a business planning perspective, the case for a CIP would be assessed in terms of the long-term commercial benefits compared to the long-term costs.

## 9. ADMINISTRATIVE MATTERS

### 9.1 Purpose Of Consultation Paper

In the interests of transparency and in accordance with the established practice of providing a consultative forum for interested parties' views on the Commission's role and responsibilities in terms of economic regulation, the Commission now wishes:

(I) to advise that it has decided in accordance with section 32 (14) (a) of the 2001 Act that there **appear to be** 'substantial grounds' to conduct a statutory review (the "Review") of the 2005 Determination; possible grounds for a review include, but are not limited to the following:

(a) a requirement to analyse the forthcoming 2006 CIP for Dublin Airport arising from the circumstances surrounding the unavailability of a finalised CIP at the time of the 2005 Determination;

(II) to advise that it has decided in accordance with Section 32 (14)(a) of the 2001 Act that there **may be** 'substantial grounds' to conduct a review of the 2005 Determination; such grounds for a review including but are not limited to the following:

(b) the degree to which airline users of Dublin Airport have revised their anticipated requirements for airport facilities such that the DAA has developed a substantially larger capital programme.

It is important to note that a decision to hold a review is entirely separate from a decision about whether to revise a price cap consequent on a review.

and

(III) to invite comments generally and in respect of the consultation questions raised in this document and as to:

(a) whether there are substantial grounds for a review of the 2005 Determination; and



- (b) whether any substantial grounds would include the possibilities suggested above or that other matters ought be considered as part of the Review on the basis of substantial grounds.

The Commission would like to emphasise that any submissions made in this regard should set out clearly and comprehensively the issues which should be considered and a reasoned explanation as to their being of a substantial nature.

## **9.2 Call for Submissions**

The Commission requests interested parties to submit responses to the questions raised in this consultation paper no later than **12 noon on Thursday 28 September 2006**. Submissions should be addressed to:

Ms. Anne Moloney  
Commission for Aviation Regulation  
Floor 3  
Alexandra House  
Earlsfort Terrace  
Dublin 2.

Submissions may be made;

- (i) in electronic form either on floppy disk or by e-mail to [info@aviationreg.ie](mailto:info@aviationreg.ie) and should be either in Microsoft Word (".doc") or portable document format ("pdf")
- (ii) by fax to 00-353-1-6611269
- (iii) by post to the Commission's offices at the above address.

The Commission requests that all written submissions be typed.

### **9.3 Publication of Submissions**

It is the Commission's intention to place any submissions received on its website. Ordinarily, the Commission does not edit this material. As a result, the content of any submission is solely a matter for the submitting party, and in that regard, interested parties are referred to the declarations below dealing with legal notice and indemnity concerning use of the Commission's website.

It should be noted that the Commission is subject to the provisions of the Freedom of Information legislation.

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#### **INDEMNITY**

Any party submitting information to the Commission in response to a document inviting submissions acknowledges that the Commission intends to publish that information on the website of the Commission, in reports of the Commission and elsewhere as required or appropriate. Parties submitting such information to the Commission consent to such publication. 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.