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26th April 2002

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Ms. Anne Moloney
Deputy Head of Economic Affairs
Commission for Aviation Regulation
36 Upper Mount Street
Dublin 2

RE: Consultation Paper on the Implementation of the Levy pursuant to Section 23 of the Aviation Regulation Act, 2001 (CP4/2002)

Dear Ms. Moloney,

Aer Lingus supports the general principle as set out in CP4/2002 that the levy provided for in Section 23 of the 2001 Act be collected from each sector of the aviation industry on the basis of the proportion of the Commission's costs incurred in respect of its responsibilities relating to that sector. As set out in more detail below, the manner in which the levy is collected and apportioned will depend on the nature of the costs and the cost centre concerned. We do not agree with the imposition on all undertakings within the aviation industry of a levy to cover the Commission's entire costs on the basis of a percentage turnover of each undertaking in the aviation industry, or indeed on any other basis, without reference being made to the use made by that undertaking of the Commission's work. This, in our view, would be totally inequitable.

We agree with the basic principle of the Commission's suggested method of cost allocation of its administrative costs, i.e. that where a cost relates to a specific cost centre then it should be allocated to that cost centre and where costs are general in nature they should be allocated in accordance with the percentage of Commission time spent working on each cost centre. However, this basic principle must be qualified insofar as it relates to professional fees. This issue is discussed in more detail below in relation to the regulation of airport charges.

1. Regulation of Airport Charges

We agree with the Commission's assertion that airport users should not bear the entirety of the regulatory costs and expenses under this heading as the airport benefits from regulation. In addition to the factors set out by the Commission in CP4/2002 which would justify a

proportion of the Commission's overall costs and expenses being payable directly by Aer Rianta and not recoverable, we believe that sectoral regulators are beneficial for regulated companies for the following reasons:

- the sectoral regulator is familiar with the realities of the sector concerned;
- the regulator is more predictable than constraints imposed on monopolies resulting from legal actions which are by their nature unpredictable;
- the regulator can have regard to general government policy.

A reasonable proportion of the overall costs and expenses incurred by the Commission in the determination process should not therefore be recoverable by Aer Rianta. We consider that the Commission is best placed to determine what constitutes a reasonable proportion of costs and expenses (excluding professional/litigation fees) in this case. However, for the reasons outlined below we believe that professional/litigation fees should be considered separately.

(i) Professional Expenses

Significant portions of the professional fees incurred by the Commission arise from the reports produced by IMG relating to Benchmarking, the Recoverable CAPEX Programme and Capacity Analysis. The three reports produced by the Commission should reduce the need for Aer Rianta to carry out similar reports during the determination period. If provision has already been made by the Commission for the cost of similar studies in Aer Rianta's opex for the determination period, then in order to prevent any double recovery by Aer Rianta, the quantum of any opex allowed in the determination for similar reports should be set off against the cost of the three reports produced by the Commission.

Moreover, the professional services provided during the course of the determination process have been of particular value to Aer Rianta. The Benchmarking Report clearly showed that there is an efficiency gap between Aer Rianta and other airports. This had been consistently denied by Aer Rianta who had spent considerable sums of money on studies supporting their position. If the Benchmarking Report had confirmed Aer Rianta's position and found that no efficiency gap existed between Aer Rianta and the selected comparators, we would agree that the costs relating to this report should be recoverable by Aer Rianta. However, as this independent study established a clear efficiency gap which Aer Rianta had previously been unaware of, it is of considerable strategic value to Aer Rianta.

Similarly, the reports relating to the Recoverable CAPEX Programme and Capacity Analysis have highlighted that if Aer Rianta acted as if it were in a competitive market, it could and should be more cost efficient. This will have financial benefits to Aer Rianta in the future. There have been many instances in the recent past where Aer Rianta has incurred additional costs correcting mistakes that could have been avoided if consultation had taken place with the airport users. The practice of Aer Rianta of goldplating and/or investing in overcapacity should also now cease.

For these reasons, we believe that Aer Rianta has benefited from the findings of these three reports to such an extent that the related professional costs should not be recoverable under the maximum average revenue per passenger allowed by the Commission.

(ii) Litigation Costs

It is clear that significant professional fees will be incurred by the Commission as a result of the judicial review proceedings initiated by Aer Rianta (over 50% of budgeted recoverable costs for 2002). However, as is pointed out in CP4/2002, the extent to which these costs will be borne by the Commission is largely dependent on the outcome of the proceedings. A number of scenarios must therefore be considered.

If Aer Rianta is unsuccessful in its action and is ordered to pay the Commission's costs in addition to its own costs in these proceedings, these costs should be borne in full by Aer Rianta and not recoverable from airport users. If this was not the case, a ludicrous situation would arise whereby Aer Rianta could initiate legal proceedings against the Commission, no matter how vexatious, in the knowledge that it could recover its costs in full from users regardless of the outcome of the proceedings. This would be totally unacceptable.

On the other hand, if Aer Rianta succeeds in its action and the Commission is ordered to pay costs, this would indicate that the Commission has erred in some way in reaching its determination. We believe that it would be unreasonable to expect airport users to pay for the mistakes of the Commission in this case and that these costs should be borne directly by central government which appointed the Commission. Section 23 of the 2001 Act provides for the recovery of operating costs and expenses through the imposition of a levy on undertakings but does not preclude other methods of meeting its costs and expenses. If, however, it is considered that this is not permissible under Section 23, the government as the shareholder of Aer Rianta should fund these costs indirectly through the imposition of a levy on Aer Rianta which is not recoverable from the airport users under the regulated charges. This rationale should also apply in any case where the Commission is ordered to pay costs. For instance, if a user was to bring a successful action against the Commission and an order for costs were made against the Commission, it would be absurd if the Commission could recover these costs from all users (including the successful litigant).

We totally reject any suggestion that the mere participation of an airport user in proceedings involving the Commission could result in that user paying a greater share of the Commission's costs unless the court orders the user to pay the Commission's costs. Aer Lingus along with Ryanair is currently participating as a notice party in the judicial review proceedings being brought by Aer Rianta against the Commission. It would be totally unreasonable if this participation alone resulted in Aer Lingus and Ryanair having to pay a greater portion of the Commission's costs. Indeed, if this were to be the case, Aer Lingus would need to reconsider its participation in the proceedings.

In conclusion therefore, the funding of the Commission's litigation costs will depend on the outcome of the litigation and the order of the court. As set out above, we do not believe that users should be responsible for such litigation costs. However, if the Commission should take the view (with which we disagree) that litigation costs regarding airport charges should in certain instances be recovered from users, we believe that this should be done by billing Aer Rianta directly and allowing Aer Rianta to recover these costs through airport charges.

2. Regulation of Aviation Terminal Services Charges

We agree with the Commission's assertion that airport users should not bear the entirety of the regulatory costs and expenses under this heading as the IAA benefits from regulation. We again consider that the Commission is best placed to determine what constitutes a reasonable proportion of costs and expenses in this case. We also agree that the portion of the costs allocated to users should be levied directly by the Commission from the IAA and that the IAA should then recover these costs from aviation terminal services users through aviation terminal service charges. These costs should be allocated among users in the same way as aviation terminal services charges generally are allocated among users.

3. Slot Allocation and Co-ordination

Up until the recent appointment of a co-ordinator (ACL Ltd.), Aer Lingus performed the function of slot coordinator at Dublin Airport. This function was performed on a voluntary basis and in a non-biased way to the satisfaction of all users at Dublin Airport. The performance of this function consumed in total one man-year's effort. This cost was borne by Aer Lingus.

Aer Lingus was willing to continue this function and, to our knowledge, all the other users were happy for Aer Lingus to do so. However, it would appear from CP3/2001, that Aer Rianta contacted the Minister in September 1999 to request that Dublin Airport be fully coordinated. This request was made without any prior consultation with the airport users. At this time, Dublin Airport was undergoing significant refurbishment and problems of overcrowding existed in the terminal. As has been indicated in previous submissions to the Commission, we are of the view that this situation arose as a result of poor project management and a lack of consultation with the airport users on the part of Aer Rianta. Aer Rianta attempted to deflect criticism from their failures by suggesting that the problems at Dublin Airport were due to the absence of full coordination. Aer Lingus and other users publicly stated at this time that full coordination was not necessary.

Following an independent study carried out by SH&E at the Commission's request, the Commission concluded that full coordination was not required. However, as a result of this process, a function which had previously been carried at no cost by Aer Lingus, was transformed into a much more expensive activity. Had Aer Rianta engaged in proper consultation with airport users and supported the effective operation of the previous schedule facilitation system, we believe that the perceived capacity deficiencies at Dublin Airport could have been addressed without the imposition of any additional costs on the airline community. For this reason, we believe that the cost of the SH&E study, which showed that full coordination was not in fact required, should be met by Aer Rianta and not be recoverable from the airport users. In addition, the majority of the annual running costs, which could have been avoided, should be treated in a similar fashion.

In conclusion, Aer Rianta's mismanagement of the terminal refurbishment, their incorrect analysis of the capacity and demand position at Dublin Airport and their failure to consult with airport users have resulted in unnecessary costs. These costs should therefore be borne entirely by Aer Rianta and should not be recoverable from users through airport charges.

4. Ground Handling

We agree that these costs should be recovered through an annual administration charge levied on approved groundhandlers. This charge should be applied equally on all approved groundhandlers as the costs incurred by the Commission in this cost centre are generated equally by the handlers.

5. Air Carrier Licensing

We agree that a fee payable by licensed carriers should cover the costs incurred in this cost centre. The same fee should apply to all licensed airlines as the costs involved in processing each application are the same.

6. Travel Trade Licensing

We agree with the Commission's proposal that the licence fees charged to tour operators and travel agents should cover the costs and expenses of this cost centre. The licence fee should not differentiate between applicants as the costs involved in processing each application are the same.

Yours sincerely,

Laurence Gourley
Group Legal Office