HYDERABAD RAJIV GANDHI INTERNATIONAL AIRPORT

GMR Hyderabad International Airport Limited

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Letter No. GHIAL/2017-18/SPG/1364
Dated: 5th July 2018

To,

The Secretary,
Airports Economic Regulatory Authority of India
AERA Building, Administrative Complex,
Safdarjung Airport,
New Delhi – 110 003

Reference: Consultation Paper no. 05/2018-19 in the matter of Determination of tariffs for Aeronautical Services in respect of Kempegowda International Airport, Bengaluru, for the Second Control Period (01.04.2016 to 31.03.2021)

Dear Ma'am,

We write with respect to the captioned consultation paper with respect to Kempegowda International Airport. In this regard we have following submission on the abovementioned consultation paper:

1. **Pre-control period eligibility:**

While calculating eligibility towards pre control period, Authority has considered pre control period starting from 1st Sept'2009 to 31st March'2011. Bengaluru Airport commissioned Terminal operation in May'2008 however authority considered tariff determination period starting from 1st Sept'2009 basis the date on which Authority's power came into force in chapter III and VI of the AERA Act.

Since airports are regulated and tariff is determined under regulated framework, the commencement of determination shall be from the date of commissioning of the Terminal. As per the concession agreement, BIAL prior to the appointment of Independent Regulatory Authority (IRA) should seek approval of MoCA for applicable Airport Charges based on final audited project cost. Initially MoCA in case of BIAL had approved adhoc tariff based on the information and as part of normal tariff determination process followed by authority the tariff is always subject to true up based on actual financial numbers. Accordingly BIAL had submitted true up calculations for pre control period along with first control period tariff filing to AERA who was in place by that time. Since the MoCA has relinquished its rights and obligation regarding tariff determination to AERA. It is AERA's responsibility to act on behalf of MoCA and determine tariff accordingly.

Also, the appellate tribunal TDSAT in a recent case of Delhi International Airport Ltd (DIAL) had dealt with the similar issue and ordered following:

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"Once AERA was legally constituted from September 2009, the unfinished exercise could have been finished only by AERA. Clearly, the Central Government had the authority to consult independent expert body for the period between 01.04.2009 and 01.09.2009 when AERA came into existence. The exercise by AERA for that period has been within the knowledge of Central Government which has issued communications relating to tariff formulation. In absence of any objection from any quarters including Central Government, it would be futile to direct the Central Government to go through the formality of fixing tariffs for the 5 months between April 2009 and August 2009 when Central Government cannot complete that exercise in a meaningful and proper manner so as to avoid retrospectively and delay."

Above order clearly states that AERA has stepped into MoCA role as far as tariff determination is concerned and any unfinished work of MoCA has to be completed by AERA. Accordingly we request AERA to take cognizance of above order of TDSAT and consider pre control period starting from 1st April'2009 instead of 1st Sept'2009.

2. Revenue from Non-airport activities (land development) considered as non-aeronautical revenue:

Authority in its consultation paper no 5/2018-19 has considered revenue from Non-airport activities as part of non-aeronautical.

As per Schedule 3, Part 2 of the Concession Agreement, activities pertaining to CPD land are non-airport activity accordingly is out of AERA purview. Also, it is outside the aeronautical service as defined in the AERA Act.

The Purpose of the land given for Non-airport activities is for development of and to serve the larger objective of industrial development, general economic and social development. Airport project in India generally unable to generate fair rate of return on investment only by airport operations and real estate is the one of the source of funds to recoup the short fall. Land in excess of the airport requirement was leased out to make the 'Project' feasible.

AERA by cross subsidizing aeronautical charges by non-airport activity is not honoring the terms of the concession and consequently the AERA Act which made a mention that existing concession should be honored. Accordingly we submit that AERA should not consider the revenues from non-airport activities for the purpose of cross subsidy.

3. Revenue from Cargo, Ground Handling and Fuel

Authority in its determination of tariff has considered Cargo, Ground Handling and Fuel services as regulated (Aeronautical) in nature. The consideration of the Authority as such is in contradiction to the AERA act and the concession agreement which is amply clear from the following :

i. **AERA Act 2008**: The section 13 of the Act defines the functions of the Authority which is binding in nature for all parties. The Section 13, sub section (a) (vi) under the functions of the Authority states as follows:

"..the concession offered by the Central Government in any agreement or memorandum of understanding or otherwise.."

It is amply clear from the above provision that the concession agreement are preserved under the act for all purposes. Further the Section 13(1)(a) of the AERA act states that :

"different tariff structures may be determined for different airports having regard to all or any of the considerations specified at sub-clauses (i) to (vii)"

The above exemplifies the intent of the statute that different tariff structures can be followed by the Authority based on the provision which include the concession agreement.

ii. **Concession Agreement:**

The Concession agreement at the Chapter 10 deals with the Charges to be levied at the Airport. The Section 10.2.1 relates to the regulated charges to be levied which states as below:

"..10.2.1 The Airport Charges specified in Schedule 6 ("Regulated Charges")....."

Further reliance is also placed on the definition of Regulatory Charges which in terms of the concession is as follows:

*"**Regulated Charges**" shall be defined in article 10.2.1*

The above section clearly defines the Airport Charges under Schedule 6 of the Concession Agreement as Regulatory Charges. According to Schedule 6 of the Concession Agreement following are the Regulated Charges:

a. Landing, Housing and Parking Charges (domestic and international)
b. Passenger Service Fee (domestic and international)
c. User Development Fee (UDF) (domestic and international)

Since above charges are regulated these are classified as Aeronautical Charges.

It is further substantiated by section 10.3 of the Concession agreement that the Authority has no jurisdiction to regulate the charges other than specified in schedule 6 stated above. The section 10.3 states as follows

> *".. BIAL and/or Service Provider Right holders **shall be free without any restriction** to determine the charges to be imposed in respect of the facilities and services provided at the Airport or on the Site, **other than the facilities and services in respect of which Regulated Charges are levied**.."* **(Emphasis added)**

In a recent judgment dated 23rd April 2018 in the case of DIAL, the TDSAT has stressed on honoring the concession agreement. Accordingly as per Concession Agreement, the revenue streams apart from Aeronautical Charges will be termed as Non-Aeronautical which will include retails, space rental, advertisement, duty free and also include Cargo, Ground Handling and Fuel.

iii. **ICAO Policies:** Clause 10.2.1 of the Concession Agreement clearly stated that the Regulated Charges shall be in accordance with the ICAO Policies. In this regard, ICAO Document No. 9562 clarified that the revenues from ground handling and fuel services shall be non-aeronautical revenues. The ICAO Document No. 9562 stated as follows:

> ***"Revenues from ground-handling charges***
>
> *This refers to charges and fees collected from aircraft operators for the use of facilities and services provided by the airport for the handling of aircraft. It should be noted that at the majority of airports ground handling is largely carried out by one or more airlines or*

special ground-handling enterprises. In the latter case, the airport will impose concession and/or rental fees which should be recorded as revenues from non-aeronautical activities.

Revenues from non-aeronautical activities

> ***Aviation fuel and oil concessions (including throughput charges). All concession fees, including any throughput charges, payable by oil companies or any other entities for the right to sell or distribute aviation fuel and lubricants at the airport.*** *Revenues from an automobile service station concession, including the sale of automobile fuel and lubricants, should be entered in the revenue accounts covering "Other concessions and commercial activities operated by the airport"." **(Emphasis Supplied)***

AERA while considering the cargo, ground handling and fuel services (**"CGF"**) services as aeronautical services failed to consider that in terms of Schedule 6 of the Concession Agreement, the CGF facilities do not fall under Regulated Charges. Furthermore, Section 13 (1) (vi) of the Act requires the AERA to consider the Concession Agreement. Thus on a conjoint reading of the Concession Agreement and the Act, AERA is not mandated to regulate any 'Other Charges' in respect of the facilities and services provided at the airport and CGF should be outside the regulations.

AERA while relying solely on the definition of 'aeronautical services' under Section 2 (a) of the AERA Act to include the CGF within the ambit of aeronautical revenue AERA has completely disregarded the mandate of Section 13 (1) (vi) to give effect to the Concession Agreement.

In the case of the BIAL, since one of the concession granted by the Central Government is that save for the 'Regulated Charges', the BIAL shall be free without any restriction to determine all Other Charges. Thus, on a reading of Section 13(1)(a)(vi) of the AERA Act read with Article 10.2 and 10.3 of the Concession Agreement stated above, AERA cannot regulate any Other Charges in respect of the facilities and services provided at the Airport including the other Aeronautical Services as defined in Section 2(a) of the AERA Act.

Accordingly AERA ought to consider the categorization of the services as provided under the definition of the Act. However, when a specific categorization has been provided by way of a concession granted by the Central Government, due regard has to be placed on such a special circumstance and the Concession Agreement ought to prevail over the categorization provided in the Act.

Accordingly the decision of the AERA to include CGF revenues within aeronautical revenues is not only against the Concession Agreement but also against the principles laid down by the ICAO which it is mandated to considered by virtue of Section 13 (1) (vi) of the Act.

4. Notional income on non-aero deposits:

With respect to the deposit received by the Airport Operator from non-aero concessionaires, AERA in its order has considered notional revenue. Same has been considered as aero/non-aero in line with the nature of service provided. Authority while considering notional revenue has stated following view:

> *The Security Deposits could mean a reduction in the rentals/ charges collected from the respective users. The Authority accordingly proposes to consider a notional revenue on the Security Deposits collected from Non-Aeronautical service providers.*

The consideration of airport operator from Non aeronautical contract is mainly revenue linked and rental being charged at the standard prevailing rates. Security deposit has been taken by the Airport Operator considering security and performance aspect which is of utmost importance in case of Airport. By taking security deposit airport operator ensures that there is adequate stake involved and in case of any default the security deposit gets forfeited. This obligation lead the responsible operations by the concessionaires.

Also, as per AERA guidelines for the airport operators, AERA has to consider only 30% of non-aeronautical revenue. This does not include any notional revenue over deposits. Deposits are capital receipt and taken by the airport operator for specific reason of securing the cashflow. It does not reduce rentals or any other related non aeronautical revenue. The artificial revenue considered by AERA from these deposit is beyond its jurisdiction.

This is clearly biased approach of AERA in treating notional income over deposits from non-aero. One side the deposit paid by the Airport Operators as part of acquiring airport rights has not been considered in tariff determination and other side AERA considering notional income from the deposit received by the Airport Operator from the non-aero concessionaires. This will adversely affect airport operator to recoup its investment from the project. Rather these deposit in case used in airport project should be eligible for adequate return.

Further, it is pertinent to note that the working capital requirement of the airport operator has been reduced to the extent of the amount of deposits, benefit of which has been reflected in the calculations of the Authority.

Accordingly, we request AERA to not consider any notional return on non-aero deposits.

5. Interest income being considered for cross subsidy purpose

AERA in case of BIAL considered notional interest income on surplus cash available with the Company. Interest income relate to investment of interim surplus funds and the retention of the share-holders' funds in the business till the same are paid out as dividends. Such incomes do not form part of either aeronautical or non-aeronautical revenues. Accordingly this is outside regulatory purview.

Temporary surplus is primarily retained in the business for redeployment at an opportune time. This is kept in the business by depriving the shareholders (without paying dividend) to meet future capital requirements. Hence taking away 30% of income from investment is penalizing the company on cash management.

It is in the part of the Airport operator cash management process. This revenue is neither generated from non-aeronautical service nor aeronautical services. It is only because of the efficiency brought in by the airport operator in managing working capital. It is very unlawful that the airport operator is being penalized for efficient operation.

6. Revenue earned by BIAL from concessionaire

The Authority proposes to consider any revenue earned by BIAL from Concessionaires providing Aeronautical services as Aeronautical revenues (For ex. space to AAI etc.).

AERA in its previous consultation paper and order have considered rentals as non-aeronautical in nature owing to it being commercial transaction. Departure from the principles already established are not called for. Considering the illustration given by the Authority we understand that the Authority intent to consider the lease rental earned by BIAL from the space let out to AAI etc. In this regard we would like to submit that the providing space is not an aeronautical service as far as airport operator is concerned. Letting out space is non aeronautical in nature and it should be treated accordingly. Authority's approach of considering this as an aeronautical revenue is against the terms of the concession agreement. Further in this context we would like to give reference of ICAO 9082 document which states as follows:

> *"Revenues from non-aeronautical sources- Any revenues received by an airport in consideration for the various commercial arrangements it makes in relation to the granting of concessions,* ***the rental or leasing of premises and land, and "free-zone" operations, even though such arrangements may in fact apply to activities that may themselves be considered to be of an aeronautical character (for example, concessions granted to oil companies to supply aviation fuel and lubricants and the rental of terminal building space or premises to aircraft operators).*** *Also intended to be included are the gross revenues, less any sales tax or other taxes, earned by shops or services operated by the airport itself." (Emphasis added)*

Based on the above all rentals to be considered non-aero irrespective of the service as it is a commercial consideration.

7. Corporate Social Responsibility

We would like to submit that the CSR as stipulated by the central government is in the nature of tax which reduces the overall profitability of the company including the aeronautical profitability as decided under regulatory framework thereby reducing the return to equity shareholders. Hence the CSR spent by the company shall be treated akin to tax computation under regulatory mechanism. We request the Authority to consider aeronautical portion of CSR as derived from aeronautical P&L should form part of eligible expenses. Moreover, the return assured on equity under the regulatory regime is reduced in case this is not considered as an expense. This being a regulated asset, the Authority should ensure that the return to the shareholders after making statutory deduction (in the form of tax or similar deduction like CSR) is protected under all circumstances.

\Yours faithfully,

For **GMR Hyderabad International Airport Limited**

Authorized Signatory

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