05 July 2018 **WITHOUT PREJUDICE**

Secretary
Airports Economic Regulatory Authority (AERA) of India
AERA Building, Administrative Complex
Safdarjung Airport
New Delhi 110 003
Email: puja.jindal@nic.in

Dear Ms. Puja,

IATA'S RESPONSE TO CONSULTATION PAPER NO. 05/2018-19 DETERMINATION OF AERONAUTICAL TARIFFS OF KEMPEGOWDA INTERNATIONAL AIRPORT, BENGALURU FOR THE SECOND CONTROL PERIOD

As the global trade association representing the world's leading airlines, the International Air Transport Association (IATA) is pleased to provide a submission on AERA's consultation paper mentioned above. IATA's membership includes some 285 passenger and cargo airlines comprising 83% of total air traffic and IATA's mission is to represent, lead and serves the airline industry.

IATA appreciates the opportunity for us to comment on the consultation paper. This submission is based on the views expressed by IATA at the stakeholder consultation meeting held on 11 May and additional comments following the meeting.

We would like to specifically request AERA to consider the following:

- **Proposal No. 1: Regulatory Till and Principles of Determination of Tariff**
  IATA has objected to the unjustified application of the 40% hybrid till for the determination of the first control period tariff. Although this will be reduced to 30% by AERA to align with the National Civil Aviation Policy for the second control period, we find it important to once again emphasise our disagreement of shifting from Single to a Hybrid till basis as it unnecessarily increases costs for consumers. In this regard, it is a great disappointment that AERA has proceeded to adopt the hybrid till approach which will make aeronautical charges more expensive and goes against the fundamental requirements to boost air connectivity as envisaged by the National Civil Aviation Policy 2016 in a sustainable manner.

  IATA supports the recognition of revenues from Cargo, Ground Handling and Fuel Farm services and rentals from leasing space as aeronautical revenues.

- **Proposal No. 2: Regarding Pre-Control Period**
  While we recognise that the proposed amendment is better than what the airport proposed, we believe that such adjustment should be calculated on a Single till basis (please refer to comments on proposal 3)

- **Proposal No. 3: Truing Up of First Control Period ARR**
  For the first control period AERA used a 40% shared till, but was clear that the true up mechanism would be made on a Single till basis. However, it is now proposing to change such decision and to adopt a true up on the basis of a 40% shared till on the basis of "expansion needs". AERA should not change its decision solely on the basis of capital

expenditure needs as that would spare shareholders from the responsibility to provide adequate capital to finance investments. Moreover, it would constitute prefunding, and on top, the capex will be included in the RAB and the company would be remunerated for it.

If AERA still wished to consider a 40% share till despite our well-justified arguments, then we urge AERA to at the least avoid users paying twice for the same assets. In this regard, the difference (in funds paid by users) between the application of a true up on the basis of a single till vs using 40% shared till should be subtracted from the RAB. By doing this, users would be at least spared from double paying for the same assets (the same would apply for any calculations pre-first control period)

- **Proposal No. 4: Traffic Projections**
  No major comments on this proposal however it is advisable that any forecasts are validated by an independent entity with the required capability on a regular basis, especially given the high rates of growth, including capacity assessments to identify the demand triggers, pace and scale of investment as part of a broader master plan and phasing strategy.

- **Proposal No. 5: Capital Expenditure**
  Merely updating stakeholders on BIAL's high level investment plans is an ineffective and unreasonable approach to consultation. No project Business Cases have been shared with the airline community including information regarding costs or return on investments. Consultation on a project by project basis is required in significantly more detail than has been shared to enable the AUCC to provide informed feedback regarding investments the airlines are funding and paying for through aeronautical charges.

  IATA is perplexed at AERA's lack of willingness to enforce its own Consultation Protocol to support meaningful consultation at Bangalore, and other regulated airports in India that is surely in consumers and Users interests. With respect to AERA's comments noted on previous responses, a lack of AERA resources is not a reasonable basis avoid supporting Users consultation or addressing the concerns we consistently raise. We do not necessarily require AERA to join consultation meetings (much as that would be useful) - as a start we simply request AERA supports our request that airport's consult as they should already be doing in line with the Consultation Protocol i.e. by writing letters to airports reinforcing the need for meaningful consultation, joining conference calls, and generally taking much more of an interest in enforcement of these activities.

  While we respect the BIAL management team, the data summarised in section 5.2.2.2. and references to AUCC consultations has little meaning without the corresponding project level detail. A small handful of AUCC meetings called on an ad hoc basis between 2015-17 that includes no information on project costs and benefits is ineffective and leaves the airline community extremely frustrated regarding our ability to provide informed feedback. Until we are in a position assess project costs and benefits, and understand there is a positive return to Users we are unable to support the costs being added to the RAB.

  So AERA is aware, IATA and the BLR AOC wrote to the Managing Director of BIAL in December 2017 thanking them for information shared to date, and requesting consultation regarding further project details including costs, however we have not received a response.

  To address some specific points raised:
  - Reference section 6.2.3 BIAL states the new terminal and airfield development will also require the development of adjoining area for access to terminals and retail outlets for

passenger ease and comfort, and other elements such as Utilities, offices, and maintenance. We request consultation on project details have not been shared to date with the airline community.

Reference BIAL's comment total airport capacity is forecast to serve the passenger demand for at least 5 years from opening day of new facilities, the airport goes on to reference Phase 2 of Terminal 2 will be developed FY2025-27. Development should not be pre-determined by dates, however by demand that we recommend is supported as common industry best practice to ensure balanced capacity over time. This may be BIAL's intent however does not read as so.

- Regarding "Sustaining Capex / Special Repairs we do not agree with AERA's decision to include actual costs incurred for elements in 2016-17 and 2017-18 of 200 crores per annum until proper scrutiny of costs, on the basis the actuals incurred are almost 6 times the original costs in the first control period. We agree BIAL should consult on amounts over 50 crores.

- Reference Terminal developments we agree with BIAL assessment that a phased approach to terminal development based on demand triggers and generally accept its approach. However, a Business Case still needs to be shared and reviewed in consultation with Users.

  We request further AUCC consultation regarding terminal design concepts, passenger flows and capacity and demand analysis and a review of capital costs. We are pleased BIAL is applying IATA Level of Service parameters as a design input, however please note these are high level inputs that do not replace the need for detailed analysis and simulation that Users request to review. Consulting on detailed passenger and operational planning assumptions is very important to ensure the Users agree with them.

- Reference 6.3.12 Eastern Tunnel Works, we completely agree with AERA's assessment that feasibility requires consultation with the airline community in advance of any irreversible decisions being taken. Again, we require options, costs and benefits to be shared via a Business Case clearly demonstrating a return on investment for Users.

  London's Heathrow as one of the world's busiest hubs with around 77 million passengers and 480,000 ATM's from 2 runways, has just one public access tunnel to the central terminal area to access Terminals 2 and 3 (and the old Terminal 1). The associated risks of a single point of entry have been carefully managed over a number of years with high levels of resilience, and so a second tunnel at BIAL may or may not be required, that should be subject to scrutiny and detailed consultation.

- Reference 6.3.2 and 6.3.3 we agree with AERA's decision to map costs in BIAL's Business Plans, taking into account a review of normative cost benchmarks, and through AERA's consultant an assessment on project requirements considering capacity and demand factors.

  Regarding AERA's assessments, we agree no additional allowances should be made for GST. Reference proposal number 5, we recognise the efforts AERA has made to try and determine a capitally efficient cost for the 2nd control period and efforts to reduce costs. We would comment however that while a cap is a reasonable approach allowing an additional 10% of capex true-up provides little incentive for BIAL to be efficient, and is in effect a bonus for the airport. We recommend the cap is applied on AERA's INR10,471 assessment of costs for the period.

- **Proposal No. 6: Allocation of Assets (Aeronautical and Non-Aeronautical)**
  We note that AERA is proposing to adopt an 85% allocation of terminal assets to the aeronautical area as opposed to 91% put forward by BIAL. While we agree that adjustment goes in the right direction, we still believe that the percentage allocated to aviation is too high. As mentioned in previous submissions, there needs to be a review on the methodology for allocating common assets at airports. Hence IATA supports the review proposed by AERA once Terminal 2-Phase 1 is operational.

- **Proposal No. 7: Depreciation**
  IATA commends AERA for enforcing a more reasonable approach to depreciation than what has been proposed by BIAL. We would appreciate for AERA's confirmation that the allocation adjustments (as mentioned by AERA in proposal 6) have also been taken into account when determining the aeronautical portion of depreciation. We would also appreciate further elaboration on the "additional depreciation as per BIAL – Aero" on table 32 (in particular, on the need for a "one time" adjustment of Rs.186.12 crore for 2018-19)

- **Proposal No. 8: RAB for the Second Control Period**
  On the basis of the comments stated on proposal 6, we believe the aeronautical RAB to be overestimated, and request AERA to review its cost allocation methodology.

- **Proposal No. 9: Operating Expenditure**
  IATA commends AERA for correctly identifying items such as CSR cost which should not be part of the operating expenditure in the first place. There ought to be stricter distinction by BIAL of such costs which are not for the provision of aeronautical services. On the aspect of the increase of consultancy costs, the business cases and expected benefits should be made transparent with the aim of delivering increased efficiency to drive unit cost down. This should form the reasonableness assessment by AERA and further validated by the airport users through the AUCC framework, which AERA must enforce more diligently. A review of the aeronautical and non-aeronautical split should also dictate the personnel allocation which at present can be considered high (90%) for an airport like BIAL, and more so given that this determination is made under a hybrid till approach.

- **Proposal No. 10: Non-Aeronautical Revenues**
  We agree with AERA's amendments. However, AERA may need to consider adding an inflation adjustment to the percentage increases (i.e. 12.5% + CPI) since it would be reasonable to assume that the revenue growth would be driven by passenger growth as well as inflation.

- **Proposal No. 11: Cost of Equity, Cost of Debt and FROR**
  We note AERA's proposed cost of capital being for the second control period. While we agree that this could be used provisionally, we believe necessary for AERA to outsource a study on cost of capital items (not just cost of equity, but also gearing, asset beta, etc) and make the necessary amendments in the next control period.

  Separately, we see the cost of debt assumed by AERA of 10.25%, and that it will true up this cost with actual cost of debt. We suggest that a ceiling it also implemented by AERA, as otherwise, the airport may not be incentivised to look for the most efficient cost of debt (as it would know that whatever rate it achieves it will be trued up).

- **Proposal No. 12: Taxation**
  No major comments.

- **Proposal No. 13: Working Capital Interest**
  IATA commends AERA for recognizing the need to adjust the WC Interest from the current 12% to 9.5% from 2018-19 onwards.

- **Proposal No. 14: Wholesale Price Index (WPI)**
  No major comments on this section.

- **Proposal No. 15: Quality of Service**

  IATA's best practice approach to quality of service is summarised in our "Airport Service Level Agreement – Best Practice" paper, and recommends quantitative, objective measures rather than qualitative, perception based measures referenced in the Concession Agreement.

  This ensures the actual performance of the airport is measured, and the quality of service agreement or Airport SLA provides the Airport with a clear understanding of the levels of service and outcomes required in order to meet Users (typically the Airline Community) expectations, in return for the airport charges they pay.

  Levels of Service should be jointly agreed between Users and Airports, while the establishment of a best practice SLA between an Airport and its Users should be based on an approach of openness, transparency and collaboration, to promote a culture of continuous improvement.

  Unfortunately these best practice elements have not been included, and a total lack of transparency regarding objective measurement is a major concern. These issues need to be resolved to ensure the airport is held to account and users need delivered.

- **Proposal No. 16: Aggregated Revenue Requirement (ARR)**
  While the adjustment proposed goes in the right direction, we also request AERA to take into account the comments raised in prior proposals relevant to this proposal.

  In terms of the rate card, we would also like to propose the removal of any unjustified (and discriminatory) tariff differentials like those existing on landing charges between domestic and international flights. We would also like to propose that any reductions in charges are also applied to the fuel throughput charge (as previously mentioned, such charge is not cost related and should be eliminated or at least brought down).

We request that our views expressed above be taken into consideration by your respected agency leading to an objective and rational decision.

Yours sincerely,

Cesar RAFFO
Head – Airport Charges
+41 22 770 2778
raffoc@iata.org

IATA
33 Route de l’aeroport
Geneva 1215
SwitzerlandSwitzerland