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28th September 2017

Ms Puja Jindal
Secretary
Airports Economic Regulatory Authority of India
AERA Building, Administrative Complex, Safdarjung Airport,
New Delhi- 110003
Email: puja.jindal@nic.in

Dear Madam,

IATA response to AERA consultation documents in the matter of determination of aeronautical tariffs in respect of both:

- * Netaji Subhash Chandra Bose International Airport (NSCBIA), Kolkata and
 - * Goa International Airport
- for the second Control Period**

IATA is pleased to have the opportunity to provide comments to AERA. May we again take the opportunity to request AERA that deadlines for stakeholders to submit their comments are extended in the future, as consultation timeframes are insufficient to enable us to provide comprehensive feedback given our many other pre-existing commitments. With the best of intentions we request AERA extends consultation timeframes to a **4 weeks minimum**, as is common best practice. As a result we are required to prioritise our feedback to only 2 airports as part of this consultation.

We also request an acknowledgment and response from AERA regarding our comments, as this has not been forthcoming from recent previous consultation responses, and we would like to know our points are being duly considered and acted on as the representative and voice of the airline industry and over 280 airlines globally.

A) NSCBIA Kolkata Airport

Usage of the Hybrid till

We see that once again AERA has adopted the hybrid till approach for setting charges. This approach not only increase costs to consumers, but also goes against the well-reasoned position that AERA took when defining its regulatory philosophy. AERA has adopted the usage of the hybrid till approach solely because the NCAP said so, without discussing the merits of such a change. We urge AERA to revisit this issue, as the latest chosen path causes harm to consumers.



First control period true-up

We observe that in its true up calculations, AERA has used lower non-aeronautical contributions than it originally envisaged for the period. This is a matter of concern, since adopting lower figures gives very little incentives to meet such targets.

We have also noted that for the second control period AERA does mention that it would need proper justifications from the airport if non-aeronautical revenues are lower than expected. However, we do believe that some action would need to be taken for the first control period as well.

Traffic Forecasts

- To more accurately predict future growth trends and ensure a comprehensive approach to forecasting is taken, we recommend the following in addition to taking account of historical trends over 10 years:
 - Consultation with airlines currently operating at the airport to understand and their plans over the next 5 years, including route development and aircraft acquisitions. This should be an integral part of the consultation process to inform the airports and AERA's thinking from an early stage in the process and a pre-requisite to forecasts being agreed i.e. when forecasts are initially being revised or formed for the net 5 year period. The airport authority can then aggregate the information from multiple airlines and consider its impact on forecasts.
 - We also request AAI consults on its traffic forecast assumption in more detail than the high level information provided. For instance:
 - Are any demand shocks built into the baseline?
 - A more detailed explanation of why a shift to larger aircraft has resulted in negative INT carrier growth, as we would usually expect this to increase capacity unless there is a reduction in frequency
 - Will the loss of United Bangla airlines from Kolkata be an ongoing trend, or will this demand be replaced.
 - Macroeconomic forecasts should also be considered in addition to historical growth trends to take broader economic factors into account, such as GDP and living standards, and airport demographics. While these factors are more relevant to longer term forecasting, some consideration and weightage should be considered in-line with industry best practices
 - At larger airports we would generally recommend a Baseline, High and Low forecast is plotted to account for any depressions or shocks in the market, or

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account for any unforeseen elements. Similarly, what if traffic forecast growth materialises at a faster rate of growth than the agreed base?

We suggest this information is provided and consulted upon before any final decision is taken by AERA on traffic forecasts for the second control period.

Cost allocation

We have raised concerns about cost allocation throughout all our submissions to AERA, and this is no exception. While the proposed adjustment for the terminal building cost allocation is better than that proposed by AAI (92.1% to aeronautical vs 94% proposed by AAI), we still strongly believe that common assets should be allocated in a more equitable way (i.e. 50:50) rather than the 92.5/7.5 ratio assumed by AERA.

To put things into perspective, and based on the figures provided for 2015-16, and based on AERA's cost allocation we have calculated that the return on non-aeronautical activities (before tax) are higher than 40%.

Capital Expenditure

We appreciate AERA's efforts to hold AAI and airports to account in the consumer and Users interests, however meaningful consultation with the airline community from an early stage in the design process is a critical element that has been lacking in every capital investment programme to date that IATA has been involved with or made aware of. As per our previous meetings and comments, we implore AERA to fulfil its duties and enforce its Consultation Protocol in the consumers and Users interests. The alternative is to continue with mock consultations when decisions have already been taken by airports, and are subsequently marginally adjusted by AERA that is both ineffective, nor takes passengers or Users interest or requirements into account.

The only way consumer and User interests will be taken into account is if AERA supports IATA and the airline community to encourage and oblige Kolkata, and other major airports in India to constructively engage through a consultation process i.e.

- Ongoing consultation with subject matter experts on design and business case element (costs and benefits) from an early stage
- A dedicated consultation forum, with regular schedule meetings
- The requirement for transparency and details to be shared in order to enable Users to provide informed feedback

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- The presence of AERA or its nominated third party specialists to observe proceedings
- Where no forum exists, setting up an Airport Consultative Committee (ACC) will help to facilitate effective consultation
- As a pre-requisite to investment we strongly recommend Airline support and consensus should be sought for each major project across the airline community as a key objective of the consultation process. This follows best practice consultation (i.e. UKCAA and London Heathrow).

- For Kolkata, without a process of consultation or ability to at least review the capital expenditures on a project by project basis it is impossible to comment with any certainty from a User's perspective on the requirement for these investments. It is within this context that we would make the following points:

- We support the application of AERA's approach to implement normative cost benchmarks to ensure a degree of capital efficiency and value for money is applied by constructively challenging AAI's cost plans. IATA strongly supports the need for detailed scrutiny from an independent third party to review the costs of major projects, however in addition we again reiterate the need for consultation with airlines, in order to ensure:
 - Solutions are fit for purpose and meet the needs of airlines i.e. Levels of Service, operational efficiency, asset reliability
 - Recognise that it is only through detailed consultation with Users that discussion on specification can be held.

- Regarding airfield works (code F taxi extension, southern apron extension, construction of remote bays) as the airport is growing these projects may be appropriate to invest in, however we request further information to understand the benefits of each project i.e. specific metrics and benefits to demonstrate the need to invest to reduce congestion, taxi time or fuel burn, to support improvement in flow rates or reduce runway occupancy times.

- We support AERA's assessment to reduce the capex regarding AAI's high terminal specification – at least until that has been consulted upon with Users in detail, until a Business Case is shared, and airline support secured.

- We agree with AERA that costs associated with the construction of 3 new hangars is disallowed.

- We would like to understand the Business case regarding installation of a solar power plant and the detailed rationale of its 92.5% allocation to aeronautical capital

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expenditure before allocating our support to it. Any benefits resulting from a reduction in utilities costs should be passed through to Users funding the investments.

- Further comments we would make on capital expenditure that apply to Kolkata, Goa and any other major aeronautical expenditures are:
 - Inflation costs should be scrutinised by AERA's independent third party as part of its overall scrutiny of costs, as we should expect AAI's procurement team to offset a % of these costs through its buying power and a competitive tendering process
 - As IATA has previously discussed with AERA, we strongly recommend the introduction of incentives to encourage the on-time delivery of major projects to the quality and specification agreed. Well proven regulatory mechanism such as "capital triggers" have been applied and had a positive impact at airports like London Heathrow.

Depreciation allowance

We agree with the Authority's proposals for adjusting depreciation.

Cost of capital (FRoR)

We disagree with the approach taken by AERA for setting the cost of capital at 14%. Despite the fact that AERA concedes AAI's almost 100% equity funded capital structure may not be an efficient one, it is still condoning such practice by rewarding AAI with a higher than necessary WACC (and the higher than necessary tax effects).

While we appreciate that AERA indicates that it expects AAI to optimize its gearing over time and that it will also carry out a study on the best FRoR, we believe that AERA should already apply a notional gearing for this regulatory period. Users cannot be negatively affected (i.e. being asked to pay higher charges) by the fact that AAI has not managed its capital structure in an optimal way in the past. At the very least, we urge AERA to set minimum gearing targets (which grow over the regulatory period).

Operating costs

We do not see how it can be justified to assume a 25% growth in personnel expenses in 2017-18 (even if this is already a lower percentage than the originally proposed 40%). Assuming such large growth percentage, with no real justification, does not provide the right incentives to the airport to manage its costs efficiently. At the most, it should be the same percentage as in the rest of the financial years of the regulatory period (i.e. 7%)

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We note that the authority has allocated CHQ/RHQ related costs in a 88:12 ratio between aeronautical and non aeronautical activities. However, we note that these costs were allocated among airports on the basis of their revenue. Therefore, we don't understand why these costs are not being allocated on a revenue basis among aeronautical and non-aeronautical activities. We request that AERA, for consistency, also allocates these costs between aeronautical and non-aeronautical activities on a revenue basis.

We support the removal of financing costs. We also agree with the reduction of energy costs.

We note the comments that the authority that it expects AAI to reduce its O&M costs over time. However, the Authority's O&M proposals do not follow these expectations. Particularly, and as commented above, we do not see how allowing a 25% increase in staff costs in 2017/18 is consistent with such a view.

We note the Authority's statement that it intends to carry an independent assessment of the reasonableness of O&M expenditure and consider the results as part of the true up exercise for the 3rd regulatory period. It would be important that in the future such assessments are carried out ahead of the period, rather than on an ex-post basis. This allows to set challenging efficiency targets on an ex-ante basis, and provides certainty of the regulatory framework.

Tax

We could not understand how the aeronautical revenues were arrived at in Table 43. We would much appreciate if AERA could provide a more detailed explanation as to how these numbers were calculated. Then we will be better able to provide our views.

Structure of tariffs

We do not see any justification on why there are charges differentials between international and domestic flights. In particular, we do not see why, in terms of landing charges, the same type of aircraft, with the same number of passengers, would pay different charges. This is discriminatory. We urge AERA to take the steps to gradually eliminate differences in charges where there is no justification behind them.



B) Goa International Airport

Usage of the Hybrid till

Similarly to our comments on Kolkata, we believe that by deciding to use hybrid till, AERA is going against its well-reasoned conclusion that Single till should be the best mechanism for calculating charges. No proper reasoning has been provided for such a shift.

True up of first regulatory period

Similar to all recent determinations, AERA mentions that it will carry out a study on whether to include land on the RAB. We urge AERA to carry out such a study and consult on its results as soon as possible.

Cost allocation

Our comments are the same as per Kolkata. We believe that the cost allocation calculations are extremely biased towards aeronautical activities. Based on the AERA's cost allocation assumptions, we have calculated that the return on non-aeronautical RAB was around 140%, which hints that something is wrong in the allocation.

Capital expenditure

The same points apply to Goa as to Kolkata regarding:

- The need to consult with the airline community from an early stage
- Support for normative costs recognising the need for third part independent checks
- Airline consensus and support before projects are approved
- Scrutiny of inflation with a target to off-set construction inflation
- Need to consider regulatory incentives to ensure the beneficial use of assets when to the programme and specification selected.

In this context we provide the following comments for AERA to consider:

- Similar to Kolkata, we are unable to assess or provide any meaningful feedback regarding any of the projects mentioned unless costs, benefits, and designs are shared with Users.
- Regarding the terminal extension we request AAI shares information regarding the Levels of Service intended to process the 3,450 passengers during the peak hours. This is an essential measure that should be shared, otherwise Users are



not able to understand and assess whether this meets their needs, cost effectively.

- We appreciate the terminal expansion details, however are unable to assess whether this option described meet is airline User needs, or is a cost effective solution. IATA suggests the terminal design plans are shared amongst all stakeholders, along with a Business Case so airlines are able to understand the options selection and benefits of the project including capacity enhancement elements.
- Regarding the West Side Finger pier extension, we support the principle of high levels of pier service and equal access to contact gates through provision of a Code E gate. The Business Case for investment however needs to be shared and along with the levels of pier service expected to be delivered so Users can understand the costs, benefits and passenger experience to understand whether it meets their needs.
- A significant concern is AAI's assumption there is a requirement to invest in high-end finishes that is likely to result in unnecessary gold plating of projects – were these finishes and the associated costs agreed with airline Users funding the investment? If not, why not? Investment is clearly not at any cost.
- IATA supports AERA's suggestion to scrutinise the costs of terminals and other infrastructure, and also supports the principle to split the cost proportionately between the Navy and Civil elements
- IATA does however wish to challenge the cost allocations of assets for both electrical installations and the terminal building – what are the underlying assumptions leading to such as high proportion being allocated to aeronautical charges i.e. 92.5% for terminals (despite the revisions).

Cost of capital (FRoR)

Similar to our comments for Kolkata, we don't believe that it would be appropriate to benefit GOA airport with a cost of capital that resembles an inefficient capital structure. Users are being asked to pay more than what they should and therefore we urge AERA to reconsider its approach, and assume a minimum level of gearing in its calculations.



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Operating costs

As in the case of Kolkata, we believe that AERA should also assume revenue as the driver for allocating CHQ/RHQ costs (which would be then consistent with how these costs have been allocated among AAI airports).

Again, and similar to the case of Kolkata, we do not understand why AERA should be allowing a 25% increase in staff costs for 2017-18. Such an approach does not provide the company with the incentives to deliver costs in an efficient manner.

We would also query as to why AERA is assuming a higher than proposed growth rate for CHQ/RHQ costs.

While we see that some ANS staff appears to have been working on airport activities, we would appreciate in having further details as to why 50% (and not a lower percentage) has been allocated to airport costs. The majority of ANS costs usually relate to ATCOs so it is unclear how the 50% was arrived at.

As mentioned previously, we believe that using a 95:5 ratio for allocating common costs as extremely high towards regulated activities. We urge AERA to reassess such an assumption.

Similar to the comments made for Kolkata, AERA indicates that GOA's O&M costs are on the higher side. We would there appreciate that AERA sets O&M efficiency targets that are consistent with such a view.

Rate card

Similar to comments made at previous submission, we request that there are no differential tariffs between domestic and international flights, unless there is a cost that justifies such a differential.

Yours sincerely,

Amitabh Khosla
Country Director - India

