

**IATA's COMMENTS ON CONSULTATION PAPER No.09/2013-14
 – DETERMINATION OF AERONAUTICAL TARIFFS IN RESPECT OF
 RAJIV GANDHI INTERNATIONAL AIRPORT, SHAMSHABAD, HYDERABAD
 FOR THE 1st CONTROL PERIOD (01.04.2011 – 31.03.2016)**

Subject	Comment/Proposal in Consultation Paper	IATA's Comments
(1) Recognition of revenue from cargo services	... The Authority, therefore, proposes to reckon the revenues accruing to airport operator on account of aeronautical assets on its books to be aeronautical revenue, regardless of whether the aeronautical service is provided by the airport operator or has been concessioned out by him to third party concessionaires. (Para 3.15, page 34 of 363)	<ul style="list-style-type: none"> IATA agrees with the Authority's treatment of revenues from cargo service accruing to the airport operator as aeronautical revenue. In addition, IATA asserts that since cargo service is defined as an aeronautical service under the AERA Act to be regulated by AERA, any revenue (e.g. concession fee, revenue share, rental etc) derived by <u>the airport</u> from provision of this aeronautical service (regardless of whether the service is provided by the airport itself, by concessionaires or by the airport's appointed agent) should be treated as aeronautical revenue.
(2) Recognition of revenue from ground handling services	... Ground Handling service has been concessioned out by HIAL to a third party concessionaire and as per information available, the assets pertaining to this service are not in the books of HIAL. Thus, following the above principle, the Authority proposes to consider revenue from such third party Ground Handling service provider accruing to HIAL	<ul style="list-style-type: none"> Under the AERA Act, ground handling service is an aeronautical service. Regardless of who provides the service, the airport has the monopoly power to affect the cost which is a significant component of industry cost. In order to curb any monopolistic tendency of the airport to treat ground handling services as a convenient source of revenue which could then lead to runaway cost for the airlines and the industry, IATA asserts that revenue in any form (including royalties and concession revenue) derived by the airport from ground handling services should be treated as aeronautical revenue.

- 106 -

Subject	Comment/Proposal in Consultation Paper	IATA's Comments
	as non-aeronautical revenue in the hands of HIAL. <i>(Para 3.16, page 34 of 363)</i>	
(3) Recognition of revenue from fuel services	...HIAL is providing fuel farm service (i.e. falling under the supply of fuel – an aeronautical service) itself and the assets of which are in the books of HIAL. Thus, the Authority proposes to consider revenue from the aeronautical service of fuel farm as aeronautical revenue in the hands of HIAL. <i>(Para 3.16, page 34 of 363)</i>	<ul style="list-style-type: none"> IATA agrees with the Authority's treatment of revenues from fuel services as aeronautical revenue. In addition, IATA asserts that a primary reason for fuel services to be regarded as an aeronautical service is because the airport can abuse its monopolistic position in this area and cause fuel costs to go up unreasonably and unnecessarily. Hence, any form of revenue derived by the airport from fuel services (e.g. concession fee, rentals, fuel facility fees etc.) should be treated as aeronautical revenue to curb the ability of the airport to treat fuel services as a convenient source of revenue that will have repercussions on the cost efficiency of the aviation industry.
(4) Pre-control period losses	...The Authority would be required to address the issue of past losses if any during the pre-control period viz 23.04.2008 till 31.03.2011. <i>(Para 4.10, page 44 of 363)</i>	<ul style="list-style-type: none"> AERA was established by the Indian Government through notification no GSR 317 (E) dated 12 May 2009. Prior to the establishment of AERA, the Ministry of Civil Aviation was the de facto economic regulator. IATA is of the strong view that legally, the Authority does not have jurisdiction over the period prior to its establishment and especially since there was a separate entity performing the regulator's role at that time i.e. the Ministry. In assessing the pre-control period claim, the period between 23 April 2008 and May 2009 (the establishment of AERA) should be excluded. Therefore, the Authority's proposed pre-control period losses (Rs260.68 crores under single till and Rs447.14 crores under dual till) should be re-computed.
(5) Asset Allocation (Aeronautical / Non-Aeronautical)	...(The Authority) proposes to commission an independent study to assess the reasonableness of this allocation and to consider the conclusions thereof at the time of tariffs for aeronautical services in	<ul style="list-style-type: none"> It is noted that asset allocation only emerges as an issue if dual till is applied. The Authority had recognized the need for an independent assessment of asset allocation in early 2012 during the tariff determination process for Indira Gandhi International Airport, Delhi but had not taken any action between then and this instance of tariff determination for Rajiv Gandhi International Airport. The absence of an

Subject	Comment/Proposal in Consultation Paper	IATA's Comments
	<p>the next control period as may be relevant. (Para 7.4, page 59 of 363)</p>	<p>independent study has left this issue in a non-ideal situation of having to rely on the airport's allocation formula and to endure an unverified allocation formula until the next control period. In the event that a decision to adopt dual till is taken, IATA does not support the unverified use of the airport's allocation formula but instead requests the Authority to adopt a nominal asset allocation percentage of 70% to the aeronautical category which is in line with the experience seen at a number of European airports (please see Appendix 1).</p>
(6) Future Capital Expenditure	<p>...The Authority proposes to consider these expenditure at the time of determination of tariffs in the next control period. (Para 8.3, page 106 of 363)</p> <p>...the proposed future capex in respect of the subsidiaries of Hotel, SEZ and Duty Free by HIAL has not been considered for calculation of aeronautical tariff for the current control period. (Para 8.4, page 106 of 363)</p>	<ul style="list-style-type: none"> • IATA agrees with the Authority's proposal given that: <ul style="list-style-type: none"> - The costs submitted by the airport operator are only broad estimates - Capital expenditure taken on by a separate entity should not in normal circumstances be included for tariff determination of the airport entity.
(7) General Capital Expenditure	<p>...The Authority proposes to true-up the difference between the General Capital Expenditure considered now and that actually incurred based on evidential submissions along with auditor certificates thereof at the time of determination of aeronautical tariff for the next control period. (Para 8.6, page 107 of 363)</p>	<ul style="list-style-type: none"> • Admission of the General Capital Expenditure proposed by the airport in the Regulatory Asset Base for tariff determination in the current control period would necessitate that the estimated costs quoted are realistic and the eventual actual costs would not vary significantly from these estimates. To ensure proper cost control measures are practiced by the airport, there should be a cap on the upward variation of the costs allowable for trueing up (e.g. up to 5%) notwithstanding that evidential submissions along with auditor certificates are required.

-108-

Subject	Comment/Proposal in Consultation Paper	IATA's Comments
(8) Treatment of land granted by the State Government	...One of the mechanisms that the Authority had thus contemplated was to reduce the market value from RAB so as to lower the charges on the passengers which, in its view, is consistent with the scheme of the grant of lease to HIAL for the project. <i>(Para 9.23, page 120 of 363)</i>	<ul style="list-style-type: none"> IATA agrees that land provided by the State for the airport project should result in benefits to the industry by way of lowering the cost environment at the airport which would in turn support aviation growth and drive economic growth within the state. IATA fully supports the Authority's proposal to bring such intended benefits to the fore through a fair mechanism such as one that reduces the RAB by the market value of the land.
(9) Treatment of Forex Losses	...The Authority proposes not to consider any adjustments related to foreign exchange variations in its determination of tariff for aeronautical services , <i>(Para 9.40, page 125 of 363)</i>	<ul style="list-style-type: none"> IATA agrees with the Authority's proposal. Variations in foreign exchange can result in gains or losses which should be absorbed by the business entity as part of the risks of conducting business.
(10) Cost of equity	...Rounding it to 16% thus appears to the Authority an appropriate fair estimate of the cost of equity of HIAL. <i>(Para 11.35, page 156 of 363)</i>	<ul style="list-style-type: none"> IATA views that the cost of equity of 13.2% calculated by NIPFP is a reasonable reflection of HIAL's cost of equity and disagrees with the Authority's tentative proposal to round the figure up to 16%. IATA believes that there is no need for rounding up and the value of 13.2% should be used as it is. This value of 13.2% should also be used for computation of HIAL's WACC as well as for assessment of pre-control period losses from September 2009 to March 2011.
(11) Operating Expenses	...Considering these numbers and the need to introduce efficiency and cost control measures, the Authority expects that the real increase in operating and maintenance costs should be contained within 3% increase in real terms. <i>(Para 14.24, page 204 of 363)</i>	<ul style="list-style-type: none"> IATA disagrees that a real increase of 3% over and above the current inflation of 6.5% provides a reasonable incentive for the airport operator to improve operating efficiency. The average used by the Authority to derive the 3% figure is flawed as three data points is far too few to provide a reliable and accurate average. Also, using data for the first three years of the airport's operations to represent that of future years is not reasonable as the nature of costs at start-up is unlikely to be the same as the steady-state costs. IATA notes that as a result of the assumptions used by the Authority to

-109-

Subject	Comment/Proposal in Consultation Paper	IATA's Comments
		<p>grant a 3% real increase, it has unfairly provided an operating expense budget that is even higher than what the airport had asked for. This should be reviewed especially given that the airport's proposal would have more likely than not already built in some buffer.</p> <ul style="list-style-type: none"> • IATA also notes that the 3% real increase have been approved across the board, even for irregular or ad hoc expense categories such as "Consultancy" and "Other Miscellaneous+Business Promotion" that do not necessarily increase over time. This has resulted in provision of budget that is more than necessary for the airport and has led to additional buffer that does not incentivize operational efficiency. • IATA would propose that in order to provide a reasonable challenge for the airport to push for operational efficiency, the allowable annual increase in operating expenses needs to be below the inflation rate which is currently at 6.5%.
(12) Treatment of Cargo Revenue	<p>...Upon receiving this information, revenue from cargo service in the hands of HIAL is also proposed to be shifted to aeronautical revenue. (Para 17.10, page 239 of 363)</p>	<ul style="list-style-type: none"> • IATA is concerned that while the assets used for provision of cargo services are in the books of the airport thus requiring the users to shoulder the burden of depreciation and WACC payable to the airport, the revenue that goes back to the airport to be treated as aeronautical revenue (which is a minor portion of the amount earned by the concessionaire) may not be commensurate with the costs borne by the users. Furthermore, the users could already be paying to the concessionaire (Hyderabad Menzies Air Cargo Pvt Ltd) cargo rates that are far in excess of the returns that the airport is entitled to should it be handling the cargo services itself. In other words, the users could be hit with a double whammy. IATA urges the Authority to re-examine the situation thoroughly and in conjunction with the returns that HMA CPL is getting to ensure that users do not end up shouldering unnecessary high costs for cargo services.
(13) Treatment of Ground Handling Revenue	<p>...HIAL has concession out provision of Ground Handling services to third party independent service providers and thus the</p>	<ul style="list-style-type: none"> • Under the AERA Act, ground handling service is an aeronautical service. Regardless of who provides the service, the airport has the monopoly power to affect the cost which is a significant component of industry cost. In order to curb any monopolistic tendency of the airport

Subject	Comment/Proposal in Consultation Paper	IATA's Comments
	<p>revenue accruing to HIAL from these third party independent service providers is proposed to be considered as non-aeronautical revenue in the hands of HIAL. (Para 17.20, page 241 of 363)</p>	<p>to treat ground handling services as a convenient source of revenue which could then lead to runaway cost for the airlines and the industry, IATA asserts that revenue in any form (including royalties and concession revenue) derived by the airport from ground handling services should be treated as aeronautical revenue.</p>
(14) Fuel throughput charge	<p>...Based on the ARR and the projected fuel throughput, it has worked out the Eligible Yield per kiloliter of Rs828.29 per kiloliter for the control period. However, HIAL has been charging the existing users at a yield of Rs2,170 per kiloliter. (Para 17.26, page 242 of 363)</p>	<ul style="list-style-type: none"> IATA is of the strong view that the sanctity of the tariff determination process should not be compromised by allowing the airport to levy a fuel throughput charge that is 2.6 times higher than what is allowed based on the ARR. AERA must preserve an orderly process by only allowing the ARR for fuel services to be collected through the fuel throughput charge and not allow a huge over-collection above the ARR to take place on the weak justification that it would be compensated through a lower YPP. It is unfair and indefensible to have the airlines pay a much higher rate just because they had been grossly over-charged all along. IATA also disagrees with the Authority's observation that the fuel farm agreements had been reasonable because the Authority was not aware of reasonable objections from the users of fuel farm services. The airlines had all along vehemently objected to the high fuel throughput charge at HYD but had no recourse since the airport had absolute monopoly over fuel services. IATA urges AERA to redress this unfair situation and reduce the fuel throughput charge to what is permissible based on ARR i.e at Rs 828.29 per kiloliter.
(15) Tariff Structure / Rate Card	<p>...the Authority has considered the aeronautical revenue under the other heads namely, Landing and Parking charges, Common Infrastructure Charges, Fixed Electricity Ground Power charges and Fuel Charges, the same as proposed by HIAL. (Para 22.6, page 268 of 363)</p>	<ul style="list-style-type: none"> IATA is strongly opposed to the 100% increase in landing fee for international flights as that would present a significant shock to airlines' operating costs. IATA urges a significantly more moderate increase, if need be, that will support a cost environment more conducive for airlines to operate in and be able to grow services. From international experience, a 10% increase in landing fee would already be considered as at the high end. IATA reiterates its rejection of a differential in landing fee between international and domestic flights as this is in gross contravention of

Subject	Comment/Proposal in Consultation Paper	IATA's Comments
		<p>ICAO principles and a highly unfair situation to have one airline subsidizing another airline for the same usage of facilities on account of the flights' origins.</p> <ul style="list-style-type: none"> • IATA notes that the ratio of UDF between domestic to international has been kept the same as the existing rate of 1:3.95. IATA believes that this ratio is unfair. IATA urges the use of a more equitable ratio of 1:2 or lower. • IATA believes that as with the proposal by AERA in the tariff determination consultation paper for BLR, the Common Infrastructure Charge proposed for HYD should be disallowed for the sake of rate card simplicity and the revenue requirement be merged into the UDF. • As per the comments in point (14), the fuel throughput charge should be set at the correct level of Rs 828.29 per kiloliter. • IATA agrees with AERA's rejection of charging UDF for arriving passengers.
(16) Regulatory till	<p>...The Authority thus tentatively proposes to adopt single till for RGI Airport, Hyderabad on account of these considerations. <i>(Para 23.148, page 340 of 363)</i></p>	<ul style="list-style-type: none"> • IATA is fully supportive of AERA's proposal to determine aeronautical tariffs at RGI Airport, Hyderabad under single till. AERA had arrived at its conclusion after having gone through a comprehensive study and extensive consultation that the most appropriate approach in the context of India that best protects the interests of passengers is the single till approach and this should be used for regulation of tariffs at HYD.
(17) Quality of Service	<p>...the Authority tentatively proposes to use the rebate mechanism as indicated in the Airport Order and the Airport Guidelines for HIAL. <i>(Para 24.10, page 343-344 of 363)</i></p>	<ul style="list-style-type: none"> • IATA agrees with the proposal for the rebate mechanism and the proposal for a transition period of six months for implementation but implementation should take place no later than 1 April 2014.

