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एअर इंडिया
AIR INDIA

अरविंद जाधव
अध्यक्ष एवं प्रबंध निदेशक
Arvind Jadhav
Chairman & Managing Director

RO/CMD/HQ/12-115(4)/14/ 14.09.2010

Dear Sir

We are enclosing herewith our submissions on Consultation Paper No 5 of 2010-11 relating to determination of tariff for services provides for cargo facility, ground handling and supply of fuel to the Aircraft Guidelines 2010 placed at Anne I. These are in addition to our earlier submissions on the consultation paper on the Philosophy of Airport Economic Regulation vide letter No. RO/CMD/HQ/12-115(4)/14/3064 dated 19.03.2010 and on the Consultation Paper on Air Navigation Services vide our letter No. RO/CMD/HQ/12-115(4)/14/1256 dated 31.08.2010. You are requested to take into account our aforesaid submissions also.

At the outset our submissions are that the tariff charged for providing Cargo Facility and Ground Handling Services at airport are completely market driven. These services function in a very competitive scenario and volatile market which characterize the aviation environment in the country today. It is our understanding that economic regulation is an intervention required in a monopolistic environment and need not be applied to services functioning under competitive environment where market forces determine the correct level of tariffs to be charged. We have attached Annex II to illustrate the approach adopted by other regulatory bodies in the country. Annex III deals in brief with the regulatory position in UK and USA.

Our submissions on the independent of the above are placed at annex I. The proposed regulatory module adopts a cost plus approach. We submit that the Authority should recognize existence of price differentiation at airports. A case also exists for removing non commercial flights from the price caps. The data requested in the formats prescribed is difficult to compile. We suggest that the published accounts of the service provider may be used for materiality assessment and other workings

The Government of India have also ordered a Ground Handling policy which will be effective 01.01.2011. AERA is requested to consider the implications therein vis-à-vis regulations proposed effective 01.04.2011. We also reiterate that the Gazette Notification of January, 2000 and the regulations 3 and 5 contained therein make it clear that NACIL is put on the same footing as AAI and treated as a class apart from any other handling agency/airline.

With regards

Yours

(Arvind Jadhav)

4/15/CM/AERA/16/9/10

Shri Yeshwant Bhave,
Chairman,
AERA, New Delhi.

Encl : Annex I,II & III

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ANNEX I

GENERAL:

1. The general aim of the regulatory mechanism should be to further liberalise the market in ground handling, provide greater competition for ground handling services, and provide more choice and better value for air operators. Furthermore, any regulation which serves to liberalise a market should over time become less prescriptive. In this context, the submissions made by various stakeholders regarding the assessment of competitiveness in in CP#5 may be viewed positively.

2 The policy should be flexible and objective with a willingness to incorporate evolving regulatory best practice. As airport structures and organisations differ greatly throughout member states it will be difficult to define centralised infrastructure on a common basis for the purposes of comparing infrastructure fees and other costs at different airports. The ability of the regulatory authority to provide for traffic forecast errors will be critical in this context. Demand forecasting as a central component of the planning process as it has profound implications for the level and timing of investment.

3 The magnitude of capital spend has profound effects on the cash flow and capital structure position, its timing affects the operational throughput of the regulated company and the cost effectiveness of the capital programme will affect the regulated company's self-financing capability and the level of consumer charges. It is possible for a regulator to set a regulatory determination where short term price reductions are achieved at the expense of capital investment e.g. 73% of Dublin Airport's capital programme was rejected by the Commission for Aviation Regulation in 2001 which resulted in lower charges in the interim.

4 The economic conditions currently prevailing in the aviation marketplace mean that there is an increasing emphasis on reducing costs to airline users, sometimes irrespective of the implication this has for service levels. This has extended to the ground handling area and is having a detrimental effect on the standard of service quality being provided to the travelling public follows:

a. Passengers are experiencing long waiting times for check-in and baggage-delivery resulting in congestion and delays.

a. The airport image is seriously damaged through media reports of congestion, poor service quality etc

b. Airport companies which provide ground handling services must be subject to the same tender requirements as third party handlers. By not being subject to the same tender procedure it potentially provides the airport company with a competitive advantage against other providers.

c. However it should be recognised that companies offering handling services and some other essential services (eg emergency management) may provide important synergies with the airport operator that may benefit both airline operators and other handlers. These synergies should be considered in any new proposals.

The **AERA** can set out requirements in terms of adequate resources and service standards which must be complied with if ground handling approval under the Statutory Instrument is to be obtained and retained.

Approvals should be withdrawn if the required service standards are not delivered on a consistent basis. The level of service quality provided by ground handling operators is directly related to their level of competency It has been mentioned in the Consultation Paper that the Service Level Agreements between the Service Providers and the Users would lay down the performance / quality of service parameters; and the Authority considers such a mechanism as a reasonable safeguard against under-performance or service levels. However, while arriving on the price cap, the scope of service and the service levels need to be clearly defined and taken into account, so as to rule out the possibility of the third party providers quoting high rates for add-on services which are not taken into account while arriving at the financial figure for the price-cap.

However, AERA has adopted the view that the issue of service quality is a contractual matter between the ground handler and its client airline which may be considered for review.

5. A mechanism for the roll forward of the Regulatory Asset Base (RAB) on the basis of the actual capital expenditure – thereby ensuring that going forward the RAB accurately reflects the underlying capital costs of providing facilities, allowing prices to be equated with actual costs and promoting economic efficiency is required. Further the following may be considered :

a. Allowing for the inclusion of assets in the RAB to maintain price continuity, to reduce the risk of asset stranding and consequent cost of capital increases and to ensure investment is made at the appropriate time.

b. Avoiding revenue claw backs, which have been recognised elsewhere as undermining the incentive properties of the price cap regulatory model.

c. Ensuring that, if assets are stranded, the rationale for stranding is soundly based and a methodology by which stranded assets might be assimilated into the RAB in the future is set out, otherwise incentives to invest are weakened and the ability to meet current and prospective user requirements is constrained.

d. Recognising that the (often) short-term views of incumbents must be balanced against the long term planning required to deliver infrastructure to meet the needs of all current and prospective users in a timely manner.

e. In the Indian context the interest rate on debt keep getting re-determined, normally on annual basis. Therefore, WACC may vary within the quinquennial

cycle itself. Authority may consider this aspect before finalising its views.

f. The Authority has proposed to provision for work-in-progress only through cost of
debt whereas equity might also be invested in the same.

6. An adequate appeals procedure must be addressed. The current provisions for an appeal panel under Section 17 of the Act are inadequate and consideration should be given to a number of options for the introduction of procedure for a full appeal on merit including the possibility of an appeal of a regulator's decision to a specialist regulatory appeals panel which could hear appeals of decisions from across the range of regulatory authorities. Consistency of the appeals mechanism across regulated sectors will enable developing more quickly a corpus of relevant expertise in the appeal bodies, up to and including the courts.

7. The concession agreements treat cargo, ground handling and fuel supply as non-aero activities, whereas in terms of AERA they are defined as aero activities. The economic effect of the services may be taken as non aero as contemplated under the concessional agreements.

8. It is imperative that the Users are provided with the risk / reward profile for each airport and the weighted average cost of capital at the airports since they would vary across airports. This would enable the Airlines to provide evidence based inputs on the charges being levied and the implications thereof.

9. AERA needs to ensure that the expenditure incurred by the Ground Handling companies is appropriate and effective, and developed in consultation with the Airlines. A detailed audit of the costs needs to be carried out and extensive consultations should be undertaken to ensure that the capital expenditure model followed in future is appropriate and to the needs of the industry. The charges levied by the service provider needs to be transparent, consistent, non-discriminatory and developed in consultation with users and linked to the Service Level Agreements.

10. Proper service quality benchmarks needs to be in place to regulate whether the
service providers achieve profitability by reducing costs.

11. There is a need for the Airport Operators / Service Providers and the Airlines to work together to determine new investments, rather than seek approval of AERA for Net New Investments (NNI). There is need for a strong Competition Commission to ensure that they may be approached for areas where there are not a sufficient number of alternatives available.

12. With the increasing number of budget airlines operating in the country the development of budget terminals at airports is a necessity that cannot be discounted. These low cost carrier terminals, as in Singapore and Kuala Lumpur, would provide only the basic facilities and still let passengers take advantage of the existing travel services in the city.

Taking into consideration this fact, the offering of basic third party services

should also be taken into account and accordingly a different tariff structure and price cap should be applicable for services being rendered to low cost airlines.

13. With the Greenfield Airport Policy stating that no Greenfield airport may be set up by AAI or an Airport Company within 150 kms of an existing civilian airport without prior approval of the Central Government, it has resulted in monopolizing by the airport operators. This in turn leads to a lack of competition and lower efficiencies derived at the airports. It also enables the airport operators to abuse their market power and dictate terms to the airlines.

a. The calculation for arriving to the yield per unit takes into account both the aeronautical and non aeronautical costs and revenues at the airport, wherein a fair rate of return is applied on it and the expected traffic flow helps arrive at the final yield per unit. However, this does not provide a suitable impetus to the airport operator / service provider to try and increase the non-aeronautical revenues from different sources since the overall rate of return remains the same for the operator / provider. The operator / provider would understandably give a pessimistic estimate of the non-aeronautical revenue to be earned and the expected traffic flow. These estimates need to be validated by AERA so as to ensure that a true yield per unit is arrived at.

b. A portion of the excess revenue earned by the operator / provider may be retained by them to enable and incentivise them to innovate and operate efficiently. However, a portion of the non-aeronautical profits should also be suitably channeled to ensure that the user charges are lowered.

c. Alternatively, the airport operator may per force be compelled to invest the excess revenue earned, into airport development which would help derive better efficiencies.

d. Revenue sharing is the biggest impediment especially at BOM and DEL, wherein the service providers have to share a high percentage of revenue earned as royalty to the airport operator. This cost is in turn being borne by the airlines. The high percentage of royalty charged needs to be regulated and taken into consideration in the calculation for ARR.

d. The land constraints being faced by MIAL is causing the costs incurred at the airport to rise. The cost of acquisition of new land would result in increasing RABs, thereby causing an increase in the tariff eventually. The airport operator should arrange for alternate sources for the funding of such eventualities so as to ensure that the users are not further burdened.

15. .An analysis of the various projects undertaken in the state shows that a major proportion of the debt funding is done through public sector banks and the equity is from the markets. This holds true even in the airline industry wherein a sizeable chunk of the equity is obtained by the airport operators is through the Government owned banks. While the Government has based the privatization of airports and airports under the PPP model on the pretext of scarce resources and a dearth of private sector investment, the reality presents a different picture.

16. Considering the number of concessions being extended to the Airport Operators under various SSAs wherein land is provided at huge discounted rates, and the cooperation extended towards completion of the projects, it is highly regrettable that the users are continually being burdened by the Airport operators in form of various charges like the UDF and the increase in other aeronautical charges. The Airport Operators are allowed to charge exorbitant prices for the services rendered irrespective of the inefficiencies in their system.

17. The Government and the Public are paying prices and returns way above what is justified for costs and risks under PPP. The climax is surely airport user charges (ADF/UDF) to fund promoters' equity. The PPP at present seems to be short for arbitraging the systems for risk-free profits.

18. The Ground Handling Agreements are governed by many local factors, multiple contracts at various airports in the country and reciprocal arrangements at foreign airports. Further, as per standard practice followed internationally the GHA (Ground Handling Agreements) are for at least three years. Further, these agreements are in accordance with the standard GHA prescribed by IATA. The GHA remains in force until terminated as per Article 11.4 of the Standard GHA of IATA. Therefore, annual tariff and multi-year tariff as envisaged will conflict with ground reality.

Suggestions:

1. An approach to regulation with respect to independent service providers should be competition assessment. AERA has proposed defining 'competition' as a regulated service being provided by three or more service providers. NACIL suggests that this be reduced to two or more service providers and supports the view of various stakeholders in this regard. Our experience at Cochin airport where we compete with WFS Bird supports this view. Even for 'not material' assets, a price cap approach should be followed in airports where there is insufficient competition. A light touch approach might lead to prohibitively high prices quoted by the service providers in those airports.

2. Even if the Materiality Index (MI_F) is used for determining the airports at which a price cap model would be used, the cut-off should be lowered to the following levels:

   a. **Fuel:** The MI_F cut-off for deeming the services at an airport to be material should be revised to ensure coverage to all airports in the country. This is required since the tariff may not be restricted by fuel companies to major airports only. Alternatively, it may be revised to 1% so that all international airports come under the price cap approach rather than six airports as in the case of 5% as indicated by AERA. This would also ensure that important airports like Trivandrum, Cochin, Calicut and Ahmedabad are brought under the purview of regulation..
   b. **Cargo:** The MI_F cut-off should be brought down to 1% from the 2.5% as suggested by AERA. This would ensure that Cochin, Ahmedabad and Trivandrum are brought under the price cap approach.
   c. **Ground Handling:** We agree with the assessment of only International Aircraft Movement for calculation of the Materiality Index for Ground

Handling services. However, the MI_F cut-off should be brought down to 2% from the 5% as suggested by AERA, which would enable bring Ahmedabad under the purview of the price cap regulation too.

We understand that economic regulation should ideally be adopted where it is clear that a serious loss of economic efficiency would otherwise exist, where other solutions are not available, and where it is clear that the regulatory system itself, with the distortions that it can create, will not make the situation worse than it would otherwise be. However, an assessment of the airports as mentioned above, along with the ones suggested by AERA in the consultation paper, would ensure that a more detailed benchmarking can be done for the third party providers in different airports, and would enable form a clearer picture after the first control period.

3. In the event of an existing service provider ceasing to provide service at an airport, the scenario should be reassessed by AERA within a month, rather than continuing with the previous policy till the end of the Control period.

4. At airports where all Indian carriers are allowed self handling, special consideration should be given to the issue of capacity and space constraints. A large number of airlines opting for self handling at smaller airports would cause considerable congestion and inefficiency in operations. However, the same should not hold true for Fuel Service Providers.

5 It has been mentioned that all Service Provider(s) shall, within two months of the date of issue of these guidelines, should submit a Multi Year Tariff Proposal for the first Control Period in the form and manner prescribed in section AI.2 of Appendix 1. However, the concept of a uniform tariff might not be a right option for the Service Providers. While, the maximum permissible tariff at each airport may be submitted by the Service Providers which would help AERA regulate the same, it is imperative to have unique agreements with the different airlines since the tariffs would depend on a variety of factors viz., scale of operations, provision of services at numerous airports in India by the same service provider, etc.

6 While a price cap has been suggested for regulation for the Regulated Services deemed 'material and not competitive', there needs to be a higher and lower band within the tariff proposal. While the service providers need to adhere within the price cap, the minimum price that can be quoted would ensure that the services are not offered at prohibitively low prices in order to eliminate competition, which might eventually lead to degradation of service quality and security standards.

7 While a control period of five years with annual compliance process, tariff proposals, user consultation, etc. has been suggested by AERA for determination of Tariff, the service providers who have less than a year of validity left according to their existing contract, needs to have specific mention. The calculation should take into account the validity of the contract.

8 While there is need for regulation on prices, special audits should be carried out to ensure that the security aspect is not compromised by the service providers while rendering services. Taking into account the security threats, it should be absolutely imperative for an airport operator to ensure that the service provider

has the requisite security permits before allowing them to provide third party services at the airport.

9. The Capital Asset Pricing Model (CAPM) as suggested by AERA for determination of Aggregate Revenue Requirement (ARR) for Regulated Service(s), is a demand-side model that assumes that seeks to provide returns in proportion to the anticipated risk. However, for a highly volatile industry like aviation, several other external parameters need to be taken into account to determine the ARR viz., environmental factors, financial slumps, political unrest, etc. While the CAPM model may be followed for the first control
period, AERA might consider addressing this issue by following a supply-side model like Arbitrage Pricing Theory (APT) whose beta coefficients reflect the sensitivity of the underlying asset to economic factors. Thus, factor shocks which lead to structural changes in assets' expected returns, and the ARR can be re-ascertained accordingly.
Alternatively, AERA needs to bring in greater clarity on the calculation of X_t for each year, wherein the external factors which would directly affect the Aviation sector would play a larger role in the determination of X_t so that a clearer conclusion can be drawn on how the yield per unit needs to be adjusted each year.

10. In the procedure for determination of Tariff(s) for Regulated Service(s) deemed "not material"; or "material but competitive", it has been mentioned that the Service Provider
needs to provide evidence of agreements, if any, between the Service Provider and the User clearly indicating that the Tariff(s) as proposed by the Service Provider is agreed to by the User.

    However, it does not take into account the fact that the User has to agree to the Tariffs quoted by the Service Provider because of absence of alternatives. In order to take this into account, the views of the three/five largest users in the airport need to be assessed by AERA, along with the documents provided by the Service Provider.

11. The new cargo facilities being created charge increased tariff but do not have much of value addition in terms of automation, process, equipments, etc. at most of the locations. Similarly the systems and process in vogue at the earlier locations have been retained. The new operators should have used this as an opportunity to implement complete automation, reduce a number of process, simplify procedures so as to make the new facilities more user friendly. For instance at the new locations operators should have done away with manual documents by implementing EDI so as to move forward towards attaining e-freight. Similarly the cargo warehouses should have built made secured zones with no possibility of any cargo entering without security check.

    Agencies like customs are also partially responsible for the new facilities becoming expensive, as the customs officials being posted at these locations are on cost recovery basis. It being a common user facility, customs was not levying any charge for this function at the earlier locations hence there is no justification to do so at green field airports. The warehouse operators in turn are passing on this additional financial burden to the customers and thus making the product / facility more expensive.

ANNEX II

Government Regulatory bodies in India

Telecom Regulation Authority of India (TRAI) for the purpose of making measures to facilitate competition and promote efficiency in the operation of telecommunication services in India.

(a) Central Electricity Regulatory Commission (CERC) for the purpose of regulating the tariff of generating companies owned or controlled by the Central Government; to regulate the tariff of generating companies, other than those owned or controlled by the Central Government; to regulate the inter-State transmission of energy including tariff of the transmission utilities; to promote competition, efficiency and economy in the activities of the electricity industry, etc.

The powers of TRAI listed under Section 11 (1) of the TRAI Act, 1997 reads as follows *"Notwithstanding anything contained in the Indian Telegraph Act, 1885 the functions of the Authority shall be to-*

a. *recommend the need and timing for introduction of new service provider;*
b. *recommend the terms and conditions of license to a service provider;*
c. *ensure technical compatibility and effective inter-connection between different service providers;*
d. *regulate arrangement amongst service providers of sharing their revenue derived from providing telecommunication services;*
e. *ensure compliance of terms and conditions of license;*
f. *recommend revocation of license for non-compliance of terms and conditions of license;*
g. *lay down and ensure the time period for providing local and long distance circuits of telecommunication between different service providers;*
h. *facilitate competition and promote efficiency in the operation of telecommunication services so as to facilitate growth in such services;*
i. *protect the interest of the consumers of telecommunication service;*
j. *monitor the quality of service and conduct the periodical survey of such provided by the service providers;*
k. *inspect the equipment used in the network and recommend the type of equipment to be used by the service providers;*
l. *maintain register of interconnect agreements and of all such other matters as may be provided in the regulations;*
m. *keep register maintained under clause (l) open for inspection to any member of public on payment of such fee and compliance of such other requirements as may be provided in the regulations;*
n. *settle disputes between service providers;*

o. *render advice to the Central Government in the matters relating to the development of telecommunication technology and any other matter reliable to telecommunication industry in general;*

p. ***levy fees and other charges at such rates and in respect of such services as may be determined by regulations;***

q. *ensure effective compliance of universal service obligations;*

r. *perform such other functions including such administrative and financial functions as may be entrusted to it by the Central Government or as may be necessary to carry out the provisions of this Act".*

Comment: Thus as is evident TRAI can regulate fees and other charges at such rates and in respect of such services as may be determined by regulations. However in case of certain matters TRAI has allowed market forces to regulate the tariff. Rule 4 of Section III of the Telecommunication Tariff Order, 1999 reads as follows "***Where the Authority has for the time being, forborne from fixing tariff for any telecommunication service or part thereof, a service provider shall be at a liberty to fix any tariff for such telecommunication services: Provided that the services provider shall comply with the reporting requirements in respect of such tariff."***

For instance under this order in Schedule VI TRAI has decided to forbear tariff with regard to all internet services other than Internet leased circuits on the premise that competition already exists in the provision of these services, and such competition is likely to increase in the future.

Similarly, tariff as regards to cellular mobile telecom services (CMTS) is under forbearance, and TRAI does not interfere in pricing matters, leaving it to the market forces due to intense competition in that sector. Although recently TRAI has started intervening in this matter it is only because of the concern raised by Bharti Airtel on predatory pricing followed by new operators. Similarly TRAI has allowed cable operators to fix rates, where it does not have any slab or ceiling on rates.

Conclusion: Thus it is clear that the service providers shall only comply with the reporting requirements set out under Rule 7 of Section III of the Telecommunication Tariff Order, 1999 and no approval is required from TRAI in cases where TRAI has specifically forborne from fixing tariff, that is usually in cases where sufficient competition exists.

ANNEX III

GLOBAL LEGISLATION ON GH REULATIONS

United Kingdom

In UK unregulated activities/non-commercial activities can be divided into three broad categories:

- services and facilities which do not fall under the umbrella of regulated charges but which are nevertheless essential for users to provide services from the airport (e.g. space for check-in desks) and can only be provided economically by one supplier;

- **services and facilities provided to airlines which are not essential or which are competitively provided (e.g. business lounges, ground handling services);**

- other services and facilities provided to consumers or other service providers (e.g. retailing, provision of office space, car parks and hotels).

In the United Kingdom it is the Airports (Ground Handling) Regulations, 1997 that deal with the provisions relating to Ground Handling. Under these regulations there is managing body that manages and operates the airport.

These regulations were set up as a response to the European Commission (EC) Directive 96/67/EC dated October 15,1996. This was deemed necessary by the European Commission since the checking-in of passengers, baggage handling, the provision of catering services, and so on used to be a monopoly at many European Union (EU) airports, and many airlines complained about the relatively high prices for the services provided and sub-optimal efficiency and service quality.

The Directive essentially stipulates that at the larger EU airports access to the market by suppliers of ground handling services is free and that for certain categories of services the number of suppliers may be no fewer than two for each category of service. Moreover, at least one of these suppliers should be entirely independent of the airport or the dominant air carrier at that airport.

However the CAA determines the price cap regulating airport charges in case of aeronautical and commercial activities of an airport excluding non commercial (ground handling) activities.

Airport Charges as defined under section 36 of the Airports Act, 1986 is as follows:

airport charges ", in relation to an airport, means-

(a) charges levied on operators of aircraft in connection with the landing, parking or taking off of aircraft at the airport (including charges that are to any extent determined by reference to the number of passengers on board the aircraft, but excluding charges payable by virtue of regulations under section 73 of the 1982 Act (air navigation services etc.)) ; and

(b) charges levied on aircraft passengers in connection with their arrival at, or departure from, the airport by air.

Airport charges are those which are levied on operators of aircraft or on passengers by the airport.

In case of Airport Charges the CAA has adopted the light touch and heavy touch approach.

It is in case of Airport charges the CAA determines the tariff
Further Section 41 of the Airports Act, 1986 gives the CAA discretionary powers to impose conditions on regulated airports.
Section 41(2) sets out the CAA's discretionary powers to impose conditions where it appears to the CAA that an airport operator (For instance BAA Airports Limited) is pursuing one of a number of specified courses of conduct. The purpose of imposing conditions is to remedy or prevent the adverse effects of such conduct.
Section 41(3) specifies the courses of conduct. These fall into a number of categories which are as follows:
• unreasonable discrimination by the airport in relation to a trade practice or a pricing policy of the airport (section 41(3)(a));
• unfair exploitation by the airport of its bargaining position in relation to a trade practice or a pricing policy of the airport (section 41(3)(a));
• unreasonable discrimination by the airport against third parties who have been granted rights (section 41(3)(b)(i));
• unfair exploitation by the airport of its bargaining position in the granting of rights to third parties (section 41(3)(b)(i));
unreasonable discrimination against applicants for third party rights (section 41(3)(b)(ii));
• unreasonable limits on the number of rights granted (section 41(3)(b)(ii));
and
• predatory pricing (section 41(3)(c)).
What constitutes predatory pricing for this purpose is further defined in sections 41(4) and (5).
It is open to an airport operator to object to a condition that the CAA intends to impose upon it (section 41(6)). Where this happens, the CAA cannot implement the condition but may, instead, make a reference to the Competition Commission which determines whether the airport is pursuing a course of conduct contrary to the public interest and, if so, how that might be remedied by the CAA by way of a condition. The statutory procedure for such a reference is found in sections 43(3) to (6), 44(1)(b), 44(2) and 44(4), 44A,44B, 45 (except (2)) and 46 (except (1) and (3)) of the Act. In practice, the CAA has not made any references of this kind to the Competition Commission. Moreover, in those cases where the CAA has concluded that an airport has been pursuing one of the specified courses of conduct and that a remedy is warranted, the airport concerned has offered, and the CAA has accepted, undertakings as to its future conduct in lieu of a formal condition.
The term Airports user has been defined in the Airports (Ground Handling) Regulations, 1997 as follows:
"*Airports user means any person responsible for the carriage of passengers, mail or freight by air from or to the airport in question.*"
Comment: It is clear that the provisions in relation to ground handling in the UK are relevant in the Indian context. It is only in the case of commercial activities excluding ground handling that the CAA determines tariff on the basis of a Multi Year Tariff Proposal for a control period of five (5) years. Further it can be seen that the CAA (Regulator) has been given only discretionary powers in cases where an airport operator is either resorting to trade practice or pricing policy which unreasonably discriminates against class of users of the airport or unfairly exploits his bargaining position or adopts predatory pricing. Moreover the European Commission (EC) Directive 96/67/EC dated from October 15, 1996 has

opened up ground handling services to competition. It is evident that airports are regulated by the CAA but facilities such as ground handling have largely been unregulated due to competition in this area.

Tuesday 25 May 2010

Queen's Speech – Airport Economic Regulation Bill

"My Government will…reform the economic regulation of airports to benefit passengers."

The purpose of the Bill is to:

- Having ruled out new runways in the South East, we will engage with all stakeholders in the sector to develop a new vision for a competitive aviation industry, supporting UK economic growth and designed within the constraint of the existing runway infrastructure. This Bill will reform the framework for the economic regulation of airports to benefit passengers and drive investment in airport facilities.

The main benefits of the Bill would be:

- To sharpen incentives on airports to deliver better outcomes for passengers.
- To drive investment in improved airport facilities for passengers.
- To allow the removal of unnecessary regulation in order to help competition to thrive and deliver benefits for passengers.
- To reduce unnecessary bureaucracy and political involvement in the regulatory process.

The main elements of the Bill are:

- Replace the existing system for setting price caps at airports which are subject to economic regulation with a more flexible framework focused on the outcomes that matter to passengers.
- Ministers are considering the detailed content of these reforms and will say more in due course.

Existing legislation in this area is:

- This Bill would replace the existing system for setting price caps at airports which is set out in Part IV of the Airports Act 1986.

<u>Opinion</u>

Thus we are of the view that AERA should regulate only where necessary and not because it has the jurisdiction to do so. Determination of tariff in cases where there is sufficient competition is advisable that it should be left to market forces. Thus AERA should intervene only where there are instances of predatory pricing or monopoly. The regulator is empowered to intervene in cases where it appears that the free market forces do not exist or are disrupted due to action of dominant players or group of players.

United States of America

The position of ground handling at airports at USA can be explained as under:

Authority

It is the Federal Aviation Administration, which is an agency of the Department of Transportation, which regulates and oversees all aspects of civil aviation in the United States of America. The Federal Aviation Act of 1958 created the Federal Aviation Administration under the name of 'Federal Aviation Agency', and the Federal Aviation Administration adopted its current name in 1967 when it became a part of the United States Department of Transportation. The Federal Aviation Act, 1958, has now been repealed by the recodification of Title 49 of the United States Public Code.

Ownership and Operation

Most airports in the United States of America are owned by the cities or counties, and operated directly by government entities or government-created airport authorities, which are also known as port authorities.

Sources of Finance for airports

There are three main sources of finance for airports:

a. Tax Exempt bonds
b. Airport Improvement Program {AIP} grants Airways Trust Fund which is financed by user taxes on various sectors of the aviation community (example passenger tickets, cargo and fuel) and disbursed by the Federal Aviation Administration (FAA).
c. Passenger Facility Charges (PFCs) of up to $4.50 per passenger which have to be approved by the FAA for identifiable projects.

Hierarchy of authorities

The hierarchy of authorities as regards provision of facilities including ground handling at airports in the United States of America is as follows:

Department of Transportation

↓

Federal Aviation Administration

↓

Airport Proprietor/ Sponsor

↓

Airport Operator

↓

Aeronautical User

The term 'aeronautical user' is defined in the Federal Aviation Administration Airport Compliance Manual (Order 5190.6B), under Section 18.3(b) as follows: *"Individuals or businesses providing services involving operation of aircraft or flight support directly related to aircraft operation are considered to be aeronautical users."*

A parallel hierarchy in the case of Port Authority of New York and New Jersey will be as follows:

Department of Transportation

↓

Federal Aviation Administration

↓

Port Authority of New York and New Jersey - {Airport Proprietor/ Sponsor}

↓

Amport (for John F. Kennedy Airport) - {Airport Operator}

↓

Swissport (ground handling company) - {Aeronautical User}

However, there is not much of a separate ground-handling industry in the US; it is nearly all airline self-handling and some airport-provided services.

Provision of Facilities and Services including ground handling at the airports

The term 'aeronautical use' is defined in the Federal Aviation Administration Airport Compliance Manual (Order 5190.6B), under Section 18.3(b) as follows: *"The FAA defines "aeronautical use" as all activities that involve or are directly related to the operation of aircraft, including activities that make the operation of aircraft possible and safe. Services located on the airport that are directly and substantially related to the movement of passengers, baggage, mail, and cargo are considered aeronautical uses. While many of the provisions of the Rates and Charges Policy are oriented toward air carrier fees, the principles of the Policy apply to all aeronautical uses of the airport".*

The airport operator normally provides the basic aeronautical facilities and services. This excludes air traffic control which is provided by the FAA, and ground handling which is provided by the airlines and agencies.

At many of the airports, the airlines will lease or rent terminal space or gates on an exclusive- or joint-use basis, or may even own and operate whole terminals as at John F. Kennedy airport in New York.

Relationship of airports with airlines

The airports enter into agreements with various airlines known as airport use and lease agreements which detail the fees and rental rates which an airline has to pay. Thus the aeronautical user pays airport charges/ fees to the airports in exchange of a right or privilege granted to him at the airport for furnishing services, or by way of rent under airport use and lease agreements. For instance in case of Tampa International Airport, for the privilege of providing ground handling services, Aircrafts Services International Inc., Evergreen Aviation and Ground Logistics Enterprise Inc., etc (ground handlers) pay the Hillsborough County Aviation Authority (airport proprietor) a privilege fee of $12,000 or 5 percent of gross receipts, payable in equal monthly installments, whichever is greater.

The existing legislative and policy framework

The generation of revenues at US airports is subject to a number of statutory requirements determined by Congress and policy statements issued by the FAA/Department of Transportation. These primarily focus on the Federal Government requirement for 'reasonable' aeronautical fees at the airport and the prohibited use of airport revenues for non-airport purposes.

The Setting of Airport Fees and Charges

There are two major pieces of legislation which cover the setting of airport charges. The Airport and Airways Improvement Act, 1982, (recodified under 49 U.S.C. Section 47107) states that, on accepting federal AIP grants, an airport is under an obligation to charge 'reasonable' fees to its aeronautical users. Similarly the Anti-Head Tax Act, 1973, (recodified under 49 U.S.C. Section 40116) allows publicly-owned airports to collect 'reasonable' charges from the airlines which are using the airport facilities. In 1996, the Department of Transportation/FAA issued its Final Policy Regarding Airport Rates and Charges as required by the FAA Authorization Act, 1994 which incorporated all the statutory obligations (Federal Aviation administration/Department of Transportation, 1996). For facilities such as ground handling there is a more flexible approach, with the policy permitting fees to be set by 'any reasonable method'. In addition it restates the principle, required in the FAA Authorization Act, 1994 that airports should set charges that make the airport as self-sustaining as possible, given the specific circumstances of the airport.

Comment: Thus as is clear the provisions regarding Ground handling in United States of America are very different and thus, may not be very relevant in the Indian context. The Anti-trust laws in the US have severe criminal consequences and are strictly enforced by the Department of Justice.

However we believe that the information regarding the position of ground handling in the US market may be relevant for opining and substantiating any stand on the payment royalty issue.

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एअर इंडिया
AIR INDIA

Sent to PWC

अरविंद जाधव
अध्यक्ष एवं प्रबंध निदेशक
Arvind Jadhav
Chairman & Managing Director

RO/CMD/HQ/12-115(4)/14/ 14.09.2010

Chairmen are not seem to have gone thru final draft.

Dear Sri

We are enclosing herewith our submissions on Consultation Paper No.5 of 2010-11 relating to determination of tariff for services provides for cargo facility, ground handling and supply of fuel to the Aircraft Guidelines 2010 placed at Anne I. These are in addition to our earlier submissions on the consultation paper on the Philosophy of Airport Economic Regulation vide letter No. RO/CMD/HQ/12-115(4)/14/3064 dated 19.03.2010 and on the Consultation Paper on Air Navigation Services vide our letter No. RO/CMD/HQ/12-115(4)/14/1256 dated 31.08.2010. You are requested to take into account our aforesaid submissions also.

At the outset our submissions are that the tariff charged for providing Cargo Facility and Ground Handling Services at airport are completely market driven. These services function in a very competitive scenario and volatile market which characterize the aviation environment in the country today. It is our understanding that economic regulation is an intervention required in a monopolistic environment and need not be applied to services functioning under competitive environment where market forces determine the correct level of tariffs to be charged. We have attached Annex II to illustrate the approach adopted by other regulatory bodies in the country. Annex III deals in brief with the regulatory position in UK and USA.

Our submissions on the independent of the above are placed at annex I. The proposed regulatory module adopts a cost plus approach. We submit that the Authority should recognize existence of price differentiation at airports. A case also exists for removing non commercial flights from the price caps. The data requested in the formats prescribed is difficult to compile. We suggest that the published accounts of the service provider may be used for materiality assessment and other workings

The Government of India have also ordered a Ground Handling policy which will be effective 01.01.2011. AERA is requested to consider the implications therein vis-à-vis regulations proposed effective 01.04.2011. We also reiterate that the Gazette Notification of January, 2000 and the regulations 3 and 5 contained therein make it clear that NACIL is put on the same footing as AAI and treated as a class apart from any other handling agency/airline.

with regards

17/9/2010

Yours sincerely

(Arvind Jadhav)

Secy (AERA)

Shri Yeshwant Bhave,
Chairman,
AERA, New Delhi.

PPS/Ch/AERA 16/9/10

Encl : Annex I,II & III

18/9

DD-II

SM (ABS)

18/9/10