Regional Express Submission to the

Productivity Commission

Economic Regulation of Airports

September 2018

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1. BACKGROUND

Regional Express (Rex) was founded in 2002 as the merger of Ansett subsidiary Airlines Hazelton and Kendell following the collapse of Ansett in 2001. Both Hazelton and Kendell airlines had over 30 years' experience prior to the collapse of Ansett.

Rex is a dedicated regional airline that operates 55 Saab 340 turbo-prop aircraft (34 seats) to 60 destinations in every State in Australia. Rex carries around 1.2 million passengers on some 75,000 flights per year. Rex is a publicly listed company on the ASX since 2005.

Rex, with its' more than 45 years of experience in regional aviation, operating the largest number of regional routes of any operator and the winner of the most State Government tenders for regulated routes, is a pre-eminent authority on the operation, regulation and funding of air route service delivery to rural, regional and remote communities. Rex welcomes the opportunity to share our experience on these matters and our proposals on the effective measures that could be taken to reduce significantly the cost of regional airfares.

Rex possesses great experience in servicing sparse population centres with most of the regional centres on its network having a population of fewer than 30,000 with the largest regional cities having only around 60,000. As a dedicated regional airline Rex is solely focused on the provision of regional air services.

Over the past 15 years Rex has been successful in growing regional passenger numbers to record levels with annual passenger numbers growing from around 600,000 in 2002/03 to around 1.2 million currently. This has been achieved through keeping fares affordable, focusing on efficiencies and on-time performance, all with heartfelt country hospitality.

In addition to Rex's focus on service reliability, Rex is mindful of the tremendous social and economic impact its services have on the regional communities and strives to work in partnership with these communities to balance their socio-economic needs against the commercial imperatives of providing a sustainable and safe regional air service.

Of the 60 routes that Rex services, Rex is the sole operator on about 80% of the routes. Far from exploiting its privileged monopolistic position, Rex actually practices the virtuous cycle whereby it intentionally lowers fares and increases capacity. This drives up passenger numbers which in turn allows us to further increase capacity and cut fares. Since 2002/03 Rex's average network ticket price has only increased by around 1% per annum which means in real terms Rex's fares are actually coming down. All this in the context of a very difficult regional aviation environment where 18 airlines have gone into administration in the last 15 years.

Rex is also committed to giving back to regional communities by supporting worthy charitable causes which are focused on helping those in need. In FY18, which is typical of prior years, Rex contributed over $300K to various worthy causes ranging from fundraisers and sponsorships to important community events around regional Australia. Rex also places a high priority on supporting cases of hardship, particularly out in the regions. More recently Rex has set up a $1M drought relief travel fund that is available to all community groups working to alleviate the impact of the drought.

Rex has frequently been recognised as the world's best regional airline by aviation experts, which includes being named Asia Pacific Regional Airline of the Year for 2017, for the fourth time, by CAPA Centre for Aviation.

2. AIRPORT CASE STUDIES

Rex operates to 60 airports in total of which more than 50 are regional airports. The vast majority of the regional airports are owned by local councils. Regional airports were vested to the local councils at no cost (often with a large sum to offset future maintenance costs) by the Federal Government prior to 1991.

Regional airports are a vital piece of community infrastructure and form a valuable community asset and should be treated no differently than local roads and bridges as critical local infrastructure that has broad ranging benefits across the entire council municipalities. Yet, many regional airports adopt a user-pays approach that requires the 'airport business' to stand-alone at no cost to the council (ratepayer) and in many cases generate a healthy surplus back to council, although in a disguised manner.

Many local councils argue that a $3.00 increase in head tax is not such a big deal compared to the overall $200 cost of the ticket. However $3.00 is extremely significant compared to thin operating margins associated with the provision of regional air services. One only has to look at Rex's FY16 profit per passenger which was only $4.00 to put a $3.00 airport head tax into context. These councils have no understanding at all on the price elasticity of demand.

In WA in FY18 the airport costs associated with operating to Perth, Albany and Esperance airports (the only 3 airports serviced by Rex in FY18) was approximately double that of Rex's fuel cost for these routes.

Rex can see three main areas of concern in regards to regional airport monopolistic behaviour;

1. Generation of excessive revenue surplus via the airport head tax revenue stream and using this to fund the local Council's other losses. This results in the airfare being higher and passenger demand dropping accordingly. While all taxes are inefficient in the economic sense and therefore to be avoided, the impact of higher airfares will have a significant negative socio-economic impact on the poor and marginalised.
2. Building of grandiose airport terminals for prestige purposes that exceed the current and forecast requirements of the airport which result in high annual depreciation and operational overheads.
3. Expansion of runways, taxiways and apron to cater for potential larger jet aircraft that exceeds current and future requirements of the airport, again resulting in high depreciation and operational costs. Often this is driven by pie-in-the-sky wishful thinking by the council and the airline is left to pick up the bill when the initiative fails to bear fruit.

Across Rex's vast regional network there is much contrast in the approach that is adopted by regional airports. There are those that truly value their regional air service, whilst others choose to embark on grand plans based on the 'build it and they will come' approach or a cash cow approach.

The 'build it and they will come' approach in particular comes with extremely high risk. Infrastructural developments of regional airports should be undertaken with a phased and rational approach. Questions do need to be asked when some regional airports embark on plans to accommodate A320 and 737 jets when the regional airport's current and forecast demand can be readily accommodated with turbo-prop aircraft that don't require any upgrades. When the grand plans fail to come to fruition, the existing service may be jeopardised as it has to carry the burden of the unnecessary but substantial depreciation.

Many regional airports have not placed appropriate revenues into necessary sinking funds, using the surplus to cross subsidise other council activities, for the major capital investment that will be required in maintaining and upgrading airport infrastructure and years later seek to recoup this mismanagement through increasing airport charges to the detriment of regional airlines and regional customers.

Many local councils do not acknowledge the simple logic that it is airport revenue growth that is important, not the unit airport charges growth. If regional airport passenger numbers have grown significantly, which in turn increases airport head tax revenue (in many cases by much more than CPI) then it defies economic logic for a council to state that due to its airport charges (head tax) not increasing for a number of years that this then represents a "fee reduction in real terms".

Rex is providing here some airport case studies in order to provide the PC with real life examples that will provide much clarity in the often intellectual discussion on the abuse of market power by airports. It is not a full list of all cases but it does provide good examples to illustrate the key areas that the PC should focus on.

When reading these examples, it is important to bear in mind that the average cost of running a regional airport is less than $500,000 (security screening excluded) based on Rex's experience with over 50 regional airports. It is also to be remembered that 30,000 passengers a year would be the bare minimum to sustain a regular RPT service with frequencies suitable for business purposes (i.e. 3 returns a day).

Regional Airports

2.1 Mildura Airport

Excessive Government Funding Causing Airport Costs to Spiral Out of Control

In 2008 Mildura Rural City Council decided to appoint an independent board and management team to operate Mildura Airport Pty Ltd (MAPL). Since Mildura Airport was corporatised in 2008 MAPL's revenue has sky rocketed as it pursued purely financial returns to the detriment of other community benefits. It is an objective of MAPL to deliver an annual dividend back to Mildura Rural City Council.

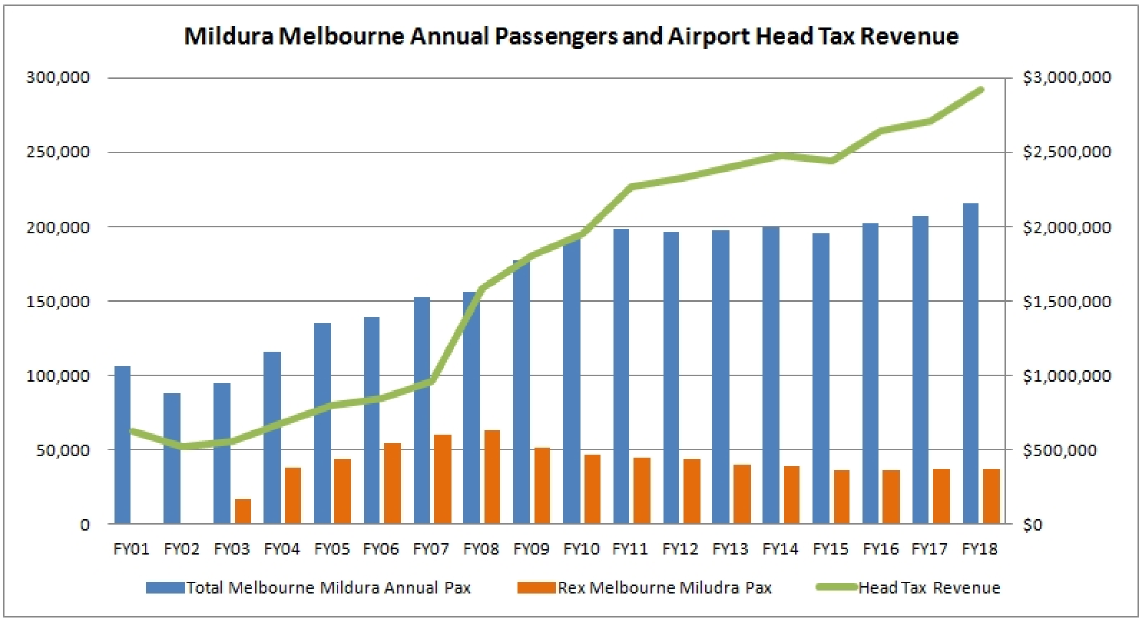
Over the past 10 years MAPL has secured a significant amount of Federal and State Government funding. This funding has gone towards significant infrastructure upgrades (runway, taxiway, apron and terminal funding) that has been beyond what is necessary. This is now contributing to increased airport costs which are putting continued upward pressure on airport charges which in turn is threatening the viability of the regional air services.

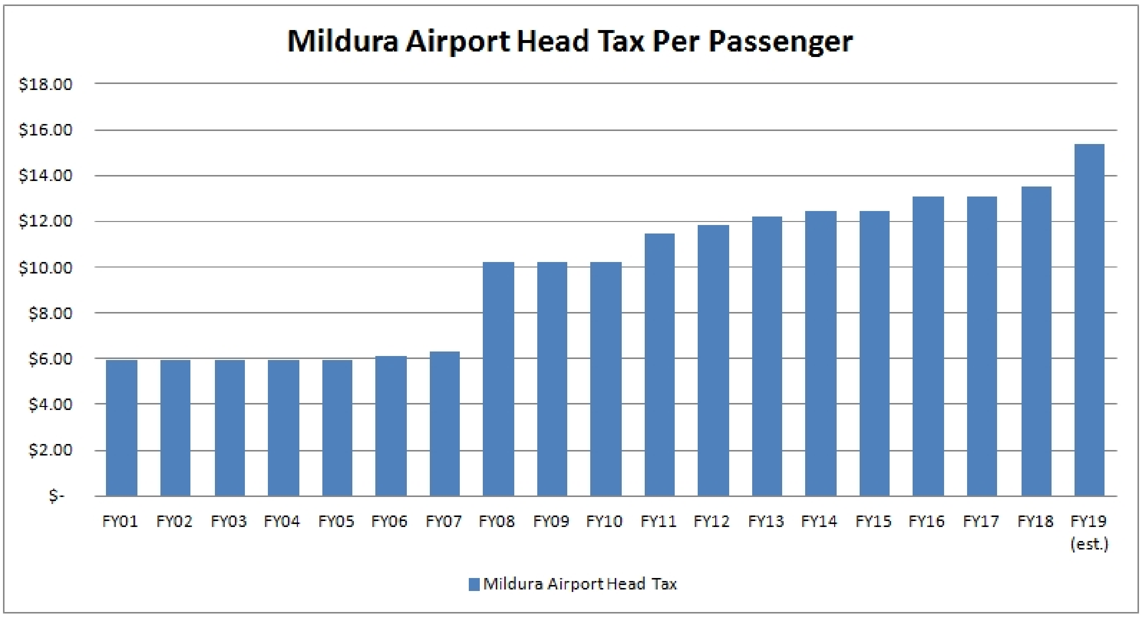
The City of Mildura is currently serviced by Rex, QantasLink and Virgin Australia with all 3 airlines operating services between Mildura and Melbourne. Rex also operates services between Mildura and Adelaide, Sydney and Broken Hill. On 12 September 2018 Rex announced that it was terminating the service between Mildura and Sydney due to exorbitant increases in airport charges at Mildura Airport.

Rex has not contributed to the rapid escalation of Mildura Airport's operating costs and the significant expenditure in infrastructure improvements that are primarily for the larger aircraft operated by QantasLink and Virgin Australia. Mildura Airport has also experienced significant total market passenger growth that should not only negate rising airport charges but should see the passenger tax lowered due to improved operating efficiencies.

Between FY08 and FY10 Mildura to Melbourne passengers increased from around 155,000 to 190,000 on the back of Virgin commencing services on the route. This represented 22% passenger growth in a short 2 years with a similar corresponding increase in airport tax revenue. Yet, MAPL continued to apply annual airport head tax increases in isolation to the passenger growth.

In FY08 Mildura airport did remove the combination of a per passenger head tax and an aircraft weight based landing fee, opting to move to a per passenger head tax only, however the end result was a massive airport revenue increase of more than 60% in that one year alone.





Rex has recently announced the exit of the Mildura – Sydney sector as a consequence of the exorbitant 13% increase in head tax to commence October 2018. As further background to Rex exiting the Mildura to Sydney route from 28 October 2018, this is now the second time that Rex has exited the route due to the greedy and myopic approach adopted by Mildura Airport. Rex first exited the Mildura to Sydney route 10 years ago in October 2008. Also back in 2008 Sharp Airways also cited future uncertainty relating to Mildura Airport security charges as a contributing factor to their withdrawal of services between Mildura and Adelaide. The Annex contains media releases from Rex that gave the reasons for our decisions.

Rex resumed the Mildura to Sydney route in mid-2012 and at the same time commenced the Mildura to Adelaide and Mildura to Broken Hill services. This formed part of a broader partnership agreement between Rex and MAPL that was effective through until 2017. This meant that Mildura has for the first time an air service to 3 capital cities, Sydney, Melbourne and Adelaide, in addition to an air link to Broken Hill. No other regional city in Australia of similar size has such extensive links to the capital cities.

In May 2017, Rex and MAPL extended the partnership for a further 3 years. This saw Rex continue providing daily direct flights from Mildura to Adelaide, Sydney and Broken Hill, in addition to the core service to Melbourne. However less than 13 months later, on 15 June 2018, MAPL provided notice to Rex of a 22.5%

increase to the Mildura Airport head tax with effect from 1 July 2018 to be applied across all routes. This was later revised by MAPL, after significant push back by Rex, to a 13.7% increase with effect from 1 October 2018 and applicable to the Melbourne route only. Rex considered this increase to be a serious breach of the commercial agreement and a blatant money grab by MAPL especially since its total airport revenue is about 6 times the amount needed to run a regional airport.

History has now repeated itself with Rex again exiting the Mildura to Sydney route and entering instead into a 5 year partnership agreement with Griffith City Council. This will see Rex's Mildura to Sydney resources redeployed across to the Griffith to Sydney route to the benefit of the Griffith community.

Mildura is one of the most blatant examples of abuse of market power as the local council simply treats the airport as a cash cow to be milked as hard as possible to finance council's inefficiencies elsewhere. It has nearly $3,000,000 in airport revenue, making a surplus of $2,500,000 per year, and it still felt that was not enough and had to raise the per passenger head tax rates by another 13%.

2.2 Orange Airport

Build It and They Will Come Approach

The Orange City Council (OCC) owns and operates Orange Airport. Orange Airport is the most expensive airport that Rex operates to across its traditional network excluding QLD and WA. Whilst Rex has recently entered into a 5-year fixed annual airport revenue agreement (with annual CPI) the airport cost per passenger is equivalent to $17.85.

Rex has been servicing the Orange to Sydney route since 2002 as the sole operator (except for a brief period in 2013). Between 2003 and 2008 Rex increased Orange Airport's revenue from approx $480K to $900K exclusive of GST. Rex believes that this was generating a significant surplus in airport revenue to the tune of about $400K annually. Yet, in spite of the profits that Rex has generated for the airport, the OCC continued to apply annual increases to its unit head tax, treating the airport as a cash cow.

In 2009 the OCC undertook an airport masterplan review. Rex did not agree with the majority of assumptions made in relation to future projections, particularly in relation to possible (bigger) aircraft types that could be used on the route within the next 10-year window.

Rex advised OCC that the planned upgrade was unnecessary given the current and forecast passenger numbers. Rex had a number of sole-operator ports that had between 65,000 passengers and 150,000 passengers per year (passenger numbers on the Orange to Sydney route were at 54,000 per year in 2009) and this was adequately serviced by Rex's Saab 340 aircraft with up to 10 returns a day. Even if the Orange to Sydney route grew to +100,000 passengers per year (which was between their low and medium passenger forecast), Rex could easily service it with a core Saab 340 frequency of 6 return Saab 340 flights per day without any need for runway and terminal upgrade.

However on the back of Rex's feedback, the OCC embarked in 2013 upon a grandiose plan to build a new terminal, extend the runway and upgrade the apron and taxiways at a total cost of some $19M with the "build it and they will come" belief. OCC also initiated a head tax increment of 1.9%, no doubt to partially finance the construction of the upgrades. OCC communicated to Rex on 6 December 2013;

"Council at its meeting on 3 December considered the fees for the Orange airport. It was resolved to increase the passenger tax to $16.25 per passenger inclusive of GST."

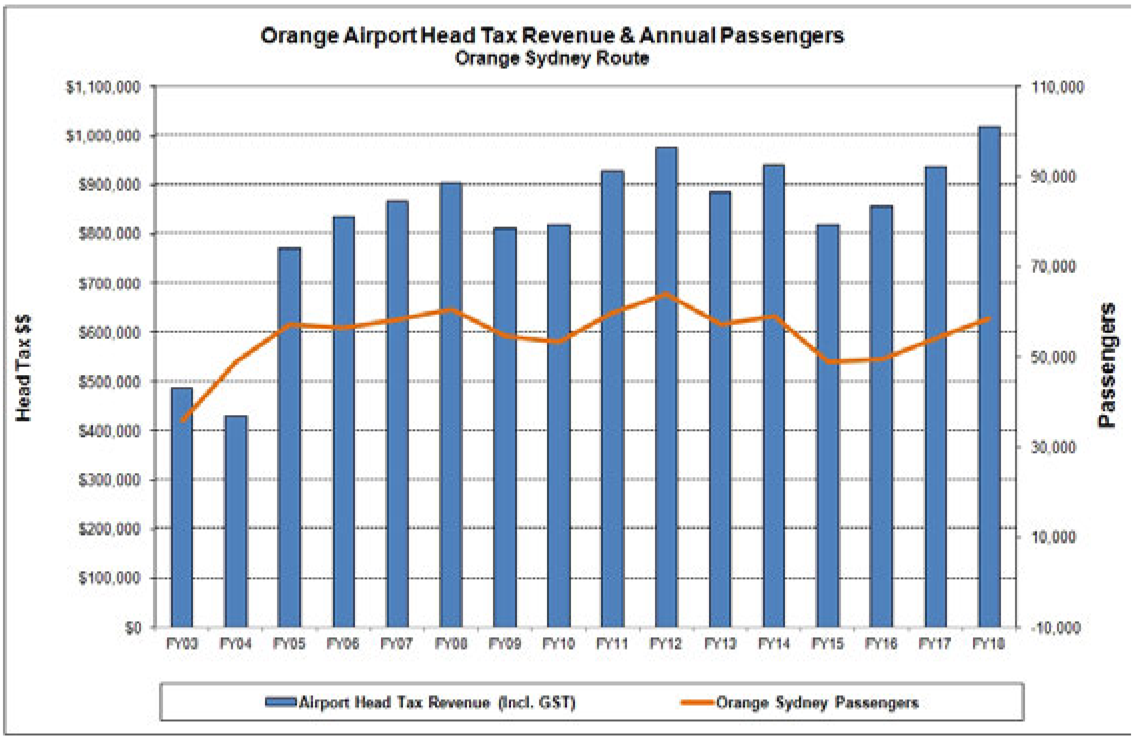
The works were completed in 2015.

Comparing the situation prior to the upgrade in 2013 and today, it is disheartening to note that after spending $19M, the situation has only deteriorated:

- No larger aircraft being used for RPT services besides the Saab 340 used originally and certainly no A320 or 737 in sight;
- Airport head tax per passenger has increased from $15.50 to $17.85 (+15.2%);
- Airport head tax revenue has increased from approx $885K to $1.01M (14.9%);
- Rex Average fare on the Orange to Sydney route has decreased by (-1%) or by below CPI;

- Orange to Sydney route passenger numbers has remained stagnant with only 2% growth compared to a network average growth of 10% in the same period;
- Daily return services reduced from 5 to 4 (before the new partnership agreement in 2018).

The above statistics are for the Orange to Sydney route only and do not include services operated by Brindabella airlines from Orange to Brisbane and Essendon.



The media releases and correspondences mentioned above are attached in the Annex.

OCC today finally realises that its aspirations for narrow body jet services will remain nothing but a pipe dream and has for the first time signed a partnership agreement with Rex from 1 May 2018 that would see an additional service permanently added and the introduction of the Community Fare scheme.

Orange Airport is one of the best examples of airports that are comfortably making a tidy surplus from airport revenue and having a good reliable service, thanks mainly to the huge operating efficiencies of Rex, who then started having aspirations for jet-load of passengers based on wishful projections by consultants hired precisely for churning out such rosy outcomes.

2.3 Kangaroo Island (Kingscote) Airport

Build It And They Will Come Approach – part 2

In 2016 the Kangaroo Island Council commenced construction work to undertake an $18M major upgrade of the Kangaroo Island Airport. In a letter sent from Council to Rex in March 2016 formally advising of the works, Council outlined that';

"the purpose of the upgrade [of Kangaroo Island Airport] is to establish the infrastructure that can service direct flight SYD / MEL – KGC services in Q400 / ATR72 / B717 / F100 / EMB 190 or similar operating aircraft".

Funding for the airport works consisted of a split contribution from State and Federal Government. The airport redevelopment included an extension and hardening of the existing sealed runway, improvements to the navigational lights and other aids, and a significant extension to the terminal building to allow for increased passenger numbers and new airport security. It was later identified that the airport redevelopment ran a further $3 million over budget resulting in an incredible $21 million total spend. Both Federal and State governments subsequently contributed a further $1.25 million each toward the cost blowout.

After being alerted to the council's initial plans in September 2015, Rex promptly communicated to council in that same month that;

"Regional Express (Rex) is deeply concerned about Kangaroo Island council's plans to upgrade Kangaroo Island airport with both State and Federal Government tax payer funding. Rex does not believe that the airport upgrade would attract the required interstate travel to financially support the significant $18M investment and no airlines have any firm plans to service KI with such services. As a result Rex is extremely concerned about KI airport costs spiralling out of control and being passed on to Rex as the only airline servicing KI"

Council subsequently replied to Rex to advise that with the assistance of their accountants that;

"council have been able to utilise innovative accounting practices to ensure that the depreciation implications of the $18M investment do not have the usual adverse impact on the profitability of the airport from day one across the life of the asset – this fundamentally ensures that even if passenger numbers do not build as we expect with new services direct to east coast markets and international gateways then the airport will still be able to operate without the need for inflation of passenger landing fees to compensate."

This statement made by Kangaroo Island Council is of major concern to Rex because innovative accounting practices is very often associated with delaying the cost impact until later.

The justification for the major redevelopment was based on a council produced report published in 2013 where council projected significant increased passenger throughput directly from the east coast of Australia citing economic benefits to the Island community of between $12 million and $49 million after the re-establishing of tourism growth by air.

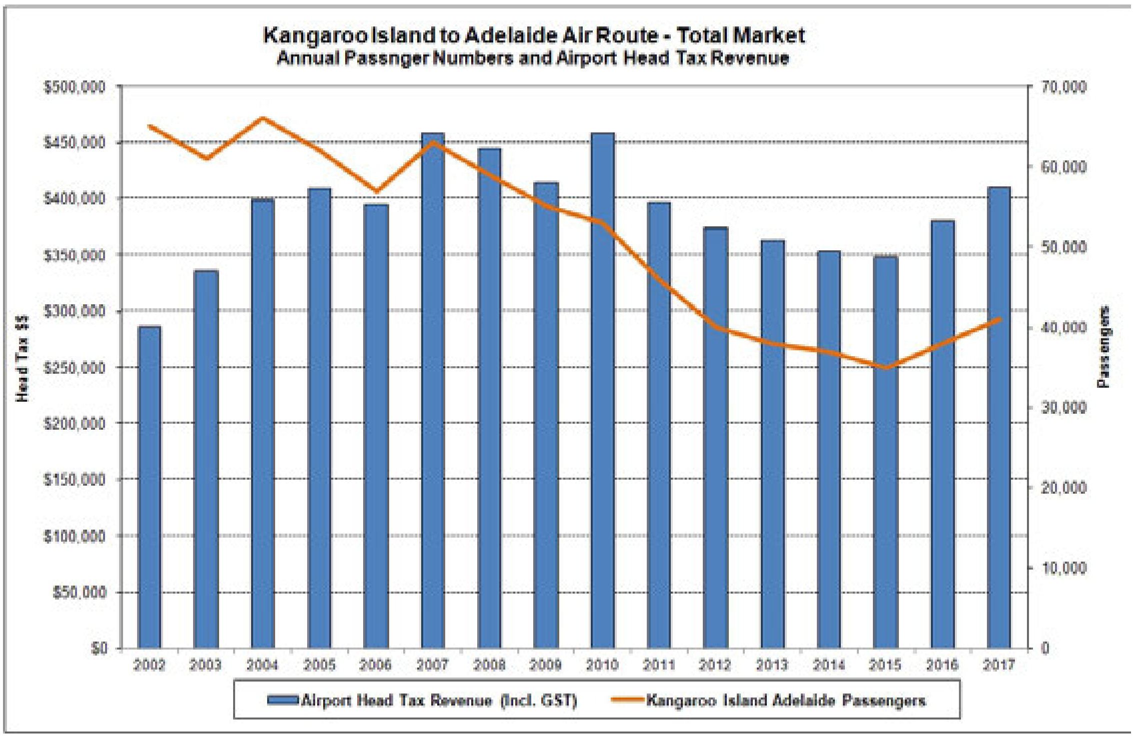
Council also outlined in their report the alarming threat that the risk of not proceeding with the significant airport upgrade works that;

"there is a high risk that without the airport upgrade, regular passenger services to the Island could be interrupted in the future for a significant period of time, leaving the Kangaroo Island Community effectively isolated from RPT air services. Small aircraft (<20 seat) charters operating out of Adelaide peri-urban airports (e.g. Parafield) might still continue to use the Airport but would be unlikely to provide a mainstream RPT service into Adelaide Airport."

What was most concerning to Rex in relation to the council developed business case for the multi-million dollar, taxpayer funded airport redevelopment project (May-2013) was that just 1 year earlier (May-2012), a previously commissioned report for Kangaroo Island Futures Authority Advisory Board, cited that *"there is certainly no evident business case for an upgrade of the airport"*. This initial report was conducted by Aviation Expert, Phil Baker, a former CEO of Adelaide Airport.

The approach undertaken by Kangaroo Island Council and supported by both State and Federal Government, demonstrates a completely economically irresponsible and misguided approach to infrastructure spending. Some $21 million has now been spent on Kangaroo Island Airport with no guarantee of any airline commencing new services.

Today Rex is servicing the Kangaroo Island route with up to 4 return daily services between Kangaroo Island and Adelaide as it has since 2002. QantasLink are currently servicing Kangaroo Island with less than daily service between Kangaroo Island and Adelaide and a seasonal December / January service between Kangaroo Island and Melbourne. Total passenger numbers through Kangaroo Island Airport in FY18 were approximately 41,000 on the Adelaide route and 1,600 on the Melbourne route.



It is simply incomprehensible to think that a $21M spend on a regional airport at the taxpayers' expense is facilitating less than 50,000 annual passengers and that all of this activity could have been accommodated by the airport prior to the upgrade. In Rex's experience, 150,000 passengers could be accommodated on facilities more modest than that at the Island before the upgrade.

Rex has grave concerns about the future financial situation of Kangaroo Island that will undoubtedly put upward pressure on airport charges that in turn will threaten the viability of existing air services. Sadly this is again another example of the build-it-and-they-will-come approach adopted by councils for self serving purposes.

2.4 Mount Gambier Airport

Monopolistic Behaviour

An example of regional airport monopolistic behaviour is at Mount Gambier airport in South Australia, which has also followed a 'build it and they will come' philosophy.

Mount Gambier Airport (owned by the District Council of Grant (DCC)) unilaterally imposed a hefty 46% airport head tax increase on to Rex during FY11, which followed prior increases of 9% and 8% during FY09. Such unjustified increases in the passenger tax (in spite of the fact that airport revenues had grown significantly because of the increased throughput of Rex passengers) have a significant impact on ticket pricing and a subsequent impact to passenger demand.

In 2010, at the time of the 46% head tax increase, the DCC communicated that the unilaterally decided increase was necessary to;

"cater for charter planes and larger aircraft like QantasLink which presently cannot land here" and that "Port Lincoln (SA) already has QantasLink and as a regional airport we also deserve to have this ability".

Rex warned the District Council of the predicted outcomes, stating that;

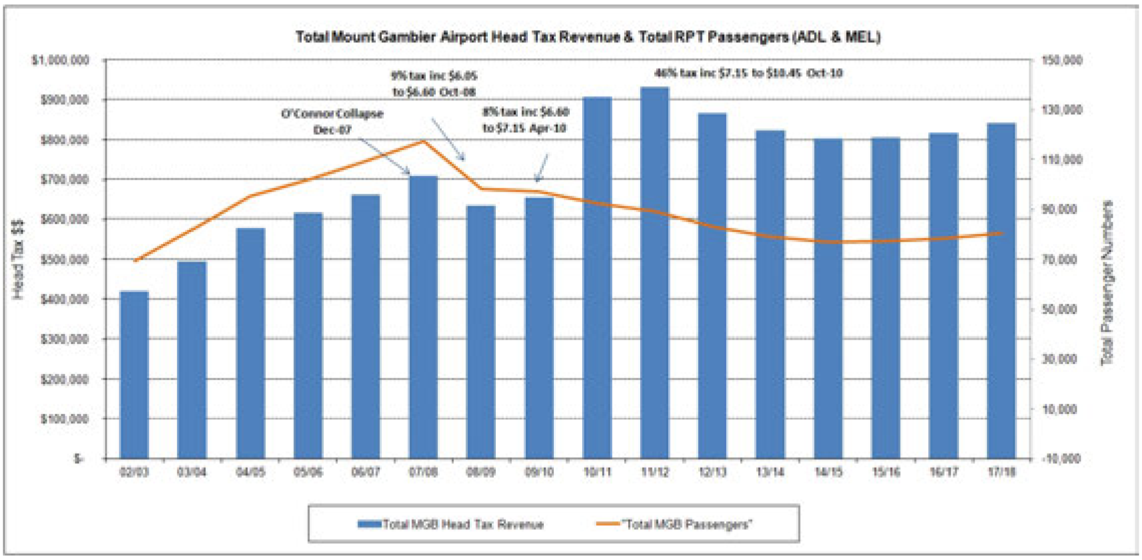
"the council's actions were economically and socially irresponsible as the community will end up paying for the additional costs through higher ticket prices. This will have a negative downward spiral effect as higher fares will mean fewer passengers which in turn will translate into a reduction of services which in turn will lead to a further reduction of passengers" and "In the not too distant future the District Council will have to explain to the

community why it had spent millions on additional airport infrastructure to welcome an ever decreasing number of passengers". The full exchanges are reproduced in the Annex

Very sadly, Rex's prediction in 2010 was borne out almost 100%. Compared to before the 3 rounds of price increases (FY08 to FY18), Mount Gambier airport today:

- is only generating around 19% more airport head tax revenue (total of around $840K per year);
- lost over 35,000 passengers down from 117,000 passengers;
- average fares have gone up 5% more than on the rest of Rex's network;
- daily frequencies between Mount Gambier and Adelaide have progressively reduced by up to 40%;
- Rex is still the only airline interested in the route; and
- Rex's profits have reduced.

So after 3 massive rounds of price increases, we see that the airport has slightly benefited with a 20% increase in revenue over 3 years but at a massive cost to the community, losing a massive 35,000 passengers a year and having sharply degraded frequencies.



Not seeing any light at the end of the tunnel, and after spending millions on the upgrade, the DCC finally decided to seek a partnership with Rex to reverse the situation. The 5-year partnership agreement saw the DCC lowering the head tax rate by $2 per departing and arriving passenger with Rex matching the reduction to result in an overall reduction of $4.40 on all fares inclusive of GST.

In addition to the overall reduction on all fares, Rex agreed to introduce a $129.00 (the lowest fare prior was at $177.00) fully inclusive 'Community Fare' on the Mount Gambier routes. The Community Fare will be available for sale on 25% of total seats outside of 30 days prior to departure. In addition, 100% of unsold seats within 24 hours of departure will be listed at $129.00. The agreement commenced in September 2018 and has instantly seen passenger numbers on the route increase significantly.

The Mount Gambier example is an excellent case study of one full cycle of boom to bust to boom - council's myopic folly in its irresponsible money grab, followed by the sharp decline in passenger numbers and frequency of services and finishing by rational and forward looking decision to return to collaborative partnership. While ultimately the outcome is very promising, it has cost all stakeholders over 8 years of pain. Not all regional carriers will be able to withstand negative outcomes for so long and it worthwhile remembering that 18 regional carriers have folded in Australia over the past 15 years.

2.5 King Island Airport

Fictitious Deficit Claims

In June 2018 the King Island Council (KIC) undertook a review of its airport fees and charges. This resulted in Rex's cost of operating to King Island Airport increasing by more than 100% or $127K annually. The change in fee structure was apparently driven by council's need to pay for amortisation of assets (which it did not pay for) which it has revalued upwards significantly.

Up until the notification of the more than doubling of airport charges, Rex operated one return daily flight between Melbourne (Tullamarine) and King Island.

Rex has operated to King Island airport since 2002 and prior to this as Kendell Airlines since 1980 - almost 40 years ago. King Island is one of Rex's most marginal routes across its network of 60 ports with only 14,000 annual passengers and operates at a loss to Rex for much of the year. A doubling of airport charges bringing an additional $127,000 in cost will surely make the services in its current form completely unviable.

KIC's basis of the significant increase was that Council was acting on advice from the Tasmanian Auditor General and KIC's own external audit panel advising KIC of the need to return the airport to a financially breakeven position. This came after it was reported that King Island Airport was operating at a loss of some $470,000 per annum.

It was subsequently uncovered by Rex that the vast majority of the book loss being recorded by KIC was as a result of a depreciation expense of some $415,000 annually. KIC advised that council had reverted from using the Valuer General's capital value of the Airport precinct and instead engaged a valuer to asses each element of the Airport precinct. As such the value of the airport assets was revised upward from $3.225M to $11.939M, resulting in the annual depreciation skyrocketing from $88k to $415k annually. This is all despite the fact that the ownership of the King Island Airport was in fact gifted to Council by the Federal Government in 1991, along with a sizable cash reserve. As it stands currently the true loss to council as a result of operating the airport is in the order of $55,000 annually of which, a large portion is understood to be council rates.

Rex does not dispute the fact that an airport with such low annual passenger traffic will inevitably make losses. More than two dozen of Rex's ports are in a similar situation and none of them would have any aspirations to break even on airport operations. KIC too would not expect its local infrastructure like the library, swimming pool, roads and bridges to be profit centres. The airport is a community asset gifted to the KIC from the Federal Government with reserves of over $450,000 and is a strategic economic asset to attract air services.

It is myopic to talk in terms of profits for this asset as the socio-economic benefits which it brings to the island far outweighs the cost of maintaining it. If the island loses its air service, it would undoubtedly spiral into a terminal economic decline.

Furthermore Rex believes that KIC and other similar councils are completely misguided in how it should be accounting for assets that are gifted by the Federal or State governments. Rex believes that the appropriate accounting treatment is found in AASB 120 where grants relating to assets have to be treated in one of two ways. Either as deferred income over the life of the asset or as a deduction to depreciation of the asset over the life of the asset.

If the above accounting treatments were applied, council should not be able to claim that airport upgrades have led to higher depreciation rates which need to be recovered through head taxes. Yet we still see this used as a reason for increased head taxes

KIC had also in mid-2016 attempted to increase the airport charges by 75%. This increase was subsequently revoked following similar outrage from Rex and the State Government.

These misguided actions by KIC resulted in Rex announcing on 18 July 2018 that its flight schedule to King Island was being reduced by 30% from 14 August 2018 in order to protect its operating margins from the doubling of airport charges.

The Tasmanian State Government has intervened and has mediated a suspension of all increases for 6 months in exchange for resumption of Rex's full services. The State Government is hopeful a more permanent solution could be found within the 6 months.

This example of the KIC shows that some communities need to be protected from its council who could be making decisions that may actually result in gravely negative outcomes that could be irreversible.

2.6 Wagga Wagga Airport

Airport Asset Depreciation Out of Control

Over the past 10 year Rex has been seeing a worrying trend with regional airport asset depreciation spiralling out of control. The high depreciation cost is often cited as the basis for needing much higher airport revenue.

As mentioned earlier, Rex believes that such an approach is wrong and not in accordance with prescribed government accounting practice (AASB 120). Many councils, including the Wagga Wagga City Council (WWCC), are choosing to ignore these guidelines, intentionally or otherwise, for its own agenda.

It is well and good for regional airports to receive State and Federal Government funding for airport investment however this increases the asset value of the airport which in turn causes airport depreciation to increase by significant levels. Government is providing airport funding to regional airports with a view that it is assisting the airport to keep its costs down, however in practice it is having the opposite effect if councils uses the depreciation as a basis for hiking the head tax. In addition, the upgraded airport infrastructure is more expensive to operate and maintain, and the additional costs are then passed on to the carrier.

Over recent years the Wagga airport assets have been revalued with the most significant revaluation occurring on FY2015/16. The FY2015/16 asset revaluation also saw for the first time airport assets being individually valued as opposed to assets being more broadly grouped.

As a result of the FY2015/16 asset revaluation process the Wagga airports annual depreciation expense increased from $890K in FY2015/16 to $2.78M in FY2016/17. WWCC then expects the carriers to bear the nearly $2M additional annual depreciation expense. It is clear to see that the WWCC is clearly just out to make a money grab and using the revaluation as an excuse to extort more money from the carriers.

The example of Wagga Wagga airport shows how certain airports that are clearly able to sustain its airport operations get greedy so as to finance its incompetence (and its dubious practices in the case of Wagga Wagga) by fudging the airport accounts.

2.7 Dubbo Airport

Dubbo Airport imposing Unnecessary Cost on airport Operators

In September 2012 QantasLink decided to operate their Dash 8-Q400 aircraft on one of its four daily services between Sydney and Dubbo. As the Dash 8-Q400 was above the 20 tonne MTOW threshold for passenger and baggage screening (as imposed by the Federal Government and OTS), full screening became a requirement for the single daily QantasLink departure only.

QantasLink's Dash 8-300 aircraft and Rex's Saab 340 aircraft that were also deployed on the Dubbo route were both below the 20 tonne threshold and did not require screening. Federal regulations also allow for both screened and unscreened simultaneous operations from the same airport under an approved Transport Security Plan (TSP) from the then Office of Transport Security (OTS). This practice is currently in place at a number of airports where Rex operates alongside larger aircraft and similar times of the day.

Dubbo City Council (DCC) as owners of Dubbo Airport proceeded to implement a requirement to fully screen all departing passengers and baggage for every flights departing Dubbo Airport across the entire day and impose a fee on all airlines, despite size of aircraft, based on a pro-rated proportion of departing passengers. This cost Rex an additional $320,000 a year which would be borne by QantasLink otherwise. This results in Rex subsidising QantasLink's need for security screening.

The actions of DCC by imposing a significant charge to Rex for passenger and baggage screening when it is legally not required is an abuse of power by the airport by favouring one of the operators against the other and in the process is distorting the competitive landscape.

Considerable information about DCC's actions in regards to security screening can be found on the Rex website at the following links;

http://www.rex.com.au/AboutRex/InTheCommunity/Petition/DBO/background.aspx
http://www.rex.com.au/AboutRex/InTheCommunity/Petition/DBO/Media.aspx
http://www.rex.com.au/AboutRex/InTheCommunity/Petition/DBO/AviationPolicy.aspx
http://www.rex.com.au/AboutRex/InTheCommunity/Petition/DBO/MakeASubmission.aspx
http://www.rex.com.au/AboutRex/InTheCommunity/Petition/DBO/ViewPetitions.aspx
http://www.rex.com.au/AboutRex/InTheCommunity/Petition/DBO/RexSubmission.aspx

Capital City Airports

2.8 Perth Airport

Peak Period Minimum Charges

Rex has operated to Perth Airport Pty Ltd (PAPL) since February 2016. On 28 February 2016 Rex commenced the Perth Albany and Perth Esperance routes under a five year Deed of Agreement with the Western Australian (WA) government. This confers onto Rex the sole right to operate on the Perth Albany and Perth Esperance routes for a five year term beginning on 28 February 2016. This was a major milestone for Rex as it resulted in Rex establishing operations in WA for the first time.

In July 2018 Rex also began servicing the Perth to Carnarvon / Monkey Mia (Shark Bay) route, also under a five year Deed of Agreement with the WA Government.

The published airport charges (excluding GST) applicable to Rex (Domestic) at Perth Airport prior to 30 June 2018 were as follows;

- $5.251 - RPT Airfield Charge per departing and arriving passenger
- **$247.263 - Peak Period* Minimum Aircraft Movement Charge**
- $19.408 – Terminal 2 Usage Charge per departing and arriving passenger
- $0.045 – Terminal 2 ACUS System Charge per departing passenger
- $1.222 – Terminal 2 Security Recovery per departing passenger
- $4.863 – Terminal 2 Passenger and Baggage Security Screening per departing passenger

Note: * the peak periods nominated by PAPL were 0530 to 0730 and 1500 to 1600 and applicable to Monday to Friday operations.

After converting the per departing passenger charges into an equivalent per arriving and departing charge, the above charges equate to $27.724 per arriving and departing passenger. This makes Perth airport, by far, the most expensive capital city airport that Rex operates to.

In regards to the peak period minimum airfield charge, any Rex aircraft movement (departure or arrival) that falls within the periods of (0530 to 0730 and 1500 to 1600) incur a minimum airfield charge of $247.263.

Rex operates a 34 seat Saab 340 aircraft so even with a 100% load factor Rex can only generate airfield charge revenue of 34 x $5.251 = $178.534. Even with 100% load factor this falls $68.729 short of the $247.263 minimum and a flight with only 10 passengers on board (10 x $5.25 = $52.51) would fall $194.753 short of the peak period minimum.

This is a significant penalty for the regional carriers operating smaller capacity aircraft and it is a measure imposed by PAPL to price the smaller regional airlines out of the busier periods so that PAPL can generate more profits from the larger aircraft within the busier periods. This is not at all a scheme to force the carriers to efficiently allocate their resources over the different periods of the day as PAPL would like to claim since the larger aircrafts are never affected.

It is therefore not surprising that Rex has always avoided the peak periods due to the significant financial penalty that is being imposed by PAPL Furthermore, it is also impossible for Rex to pass such a penalty on to fare paying passengers who are paying the standard published airport charges as part of their total fare. In addition, the minimum peak time charge is dependent on how many passengers are on-board a single flight making it totally impossible for the airline to know what its costs will be.

Since late 2017 Rex has been working with PAPL on entering a 7-Year Airline Services Agreement (ASA) to be effective from 1 July 2018. In the final stages of reaching the agreement, PAPL unilaterally changed the peak time periods and also added 2 more 2.5 hour peak periods (effectively almost tripling the number of hours subjected to the peak period surcharge). This was supposed to be based on serious economic modelling by PAPL on the demand patterns.

The revised and new peak periods were as follows (items in bold are new additions);

- 0500 to 0700, **0900 to 1130**, 1400 to 1500 and **1700 to 1930.**

This increased the PAPL nominated peak hours from 3 hours each day to 8 hours each day. In addition to the revised and new peak time periods PAPL also proposed to increase the minimum peak period airfield charge from $247.263 to $279.924 excluding GST, with further annual increases during the 7 year term of the ASA. These changes were being imposed on to all airlines however those operating smaller regional aircraft are by nature of the charge the most impacted. For example a 100 seat would broadly achieve the minimum airfield charge with a 50% load factor.

The 3 Rex regulated route (Albany, Esperance and Carnarvon / Monkey Mia) flight schedules form part of a Deed of Agreement between Rex and the WA Government. Due to the regulated route schedules being governed by the Deed of Agreements and Rex having confirmed Perth airport slots, Rex has next to no ability to reschedule flights away from the new peak time periods that are arbitrarily nominated by PAPL.

These peak time changes saw Rex go from having no flights operating within the peak time periods to having 40 weekly flights operating within peak periods and with an assumed average load factor of 65% (typical average) the cost impact to Rex equated to $330K per year.

Rex opposed the changes to the peak time periods and challenged PAPL to produce evidence to support the changes. Indeed the peak periods were in place during the peak of the resource boom and with the severe downturn of movements at PAPL in the last 3 years, it appeared bizarre that the number of hours subject to peak period surcharge should almost treble. Rex also threatened to complain to the Productivity Commission and the State Government.

Within 3 weeks PAPL has withdrawn all of the changes relating to the peak time periods (including the increased charge) and reverted back to what was in place prior to 30 June 2018.

Whilst a reasonable outcome has been achieved in the end, Rex believes that this outcome would not have happened if there were not an on-going Productivity Commission enquiry. It is most revealing to note that the afternoon peak period of 3-4 pm that is now currently in force was only 3 weeks ago considered not to be a peak period according to PAPL's rigorous economic modelling. This clearly shows the sort of unethical behaviour that capital city airports are given to if left unchecked.

2.9 Melbourne Airport

A Big Cheat

Melbourne's Tullamarine Airport (APAM) has experienced significant growth in air traffic movements in recent years, particularly through increased international traffic and specifically at defined peak periods during the day. In an attempt to manage the increasing rate of aircraft congestion and airborne holding experienced by airlines on route to Melbourne Airport, and noting safety concerns, Airservices Australia introduced an Air Traffic Flow Management tool (Harmony) at Melbourne in March 2014. Harmony is a pre-tactical flow management tool that works by applying a Ground Delay Program (GDP) at congested airports where a ground delay is allocated to aircraft at their departing port, theoretically to avoid excessive airborne holding. Harmony is used to run arrival Ground Delay Programs (GDP) for Sydney, Brisbane, Melbourne and Perth airports.

The significant difference between Melbourne and other major ports where GDP has been implemented is that Sydney, Brisbane and Perth all have some form of a Runway Demand Management System (RDMS), where slots are allocated in accordance with the actual movement capacity of the respective airport, meaning that adequate sequencing exists to meet any traffic constraints, particularly at peak periods, thereby avoiding the likelihood of significant and chronic airborne congestion/holding.

An RDMS is an internationally recognised IATA mechanism for controlling airport demand where limitations in capacity exist. It would appear APAM is unwilling to limit capacity at the risk of impacting their profit margins but instead would accept any airline's demand for a slot regardless of the congestion level at that particular time.

The end result is that APAM would reap the commercial benefits from having the additional head tax and landing fee from the new entrant and, in cases where the runway capacity is inadequate, because all the other existing carriers pay the penalty by having all their existing flights delayed to share the pain.

To rub insult to injury, APAM has capitalised on these periods of congestion where significant delays are experienced to push its agenda of building an additional parallel runway at a cost of well over 1 Billion dollars funded partially by levying the existing airport users.

In an attempt to achieve this, APAM has proposed during their most recent Aeronautical Services Agreement negotiations that APAM would agree to implement a RDMS only on the proviso that airlines agree to APAM plans to build and contribute to fund a new parallel third runway. It was further proposed that first round slots as part of the RDMS would only be granted to those airlines who signed up to support APAM plans and funding methods of building a new runway. This approach by APAM was subsequently revoked following extensive backlash by airlines against APAM.

While the levy for the third runway has gone away, carriers are still faced with the continued and further degradation of service levels with extensive GDP attributed delays experienced by Rex and other carriers at Melbourne Airport. Rex has statistics to prove that since the RDMS was implemented, Rex's On Time Performance (OTP) reduced by up to 15% for the Victorian network with resulting operational and financial consequences which have proved to be financially and operationally very detrimental to Rex.

A party that accepts 61 movements an hour on a runway that could take say only 50 movements is clearly a cheat and a fraud. It not only cheats the new entrant by promising a service it knows it cannot deliver, it is also cheating the other 60 existing customers by increasing the delays that they will have to bear. Rex cannot state strongly enough that the actions of APAM is an extreme abuse of its market power and is both morally and ethically reprehensible.

Rex would strongly urge the Productivity Commission to take all necessary steps to rein in such reprehensible behaviour with the full weight of available regulations. APAM should also be directed to compensate all the carriers who have suffered damages as a result of its greedy and unethical behaviour.

3. VARIOUS AIRPORT ISSUES

3.1 CAPITAL CITY AIRPORTS

Continued access by regional airlines to Capital City Airports remains critical to the sustainable provision of regional air services due to the essential nature of regional air travel. Regional communities depend on a reliable and sustainable regional air service for medical, business and government related travel. It is crucial to the socio-economic fabric of regional communities and the benefits are far-reaching across local, state and federal government levels.

There are several key issues with regards to capital city airports;

3.1.1 Airport Pricing

Sydney Airport is the only Capital City airport in Australia where aeronautical services and facilities provided by Sydney Airport to regional air services are declared under the Federal Governments Declaration no. 94. The current declaration commenced on 1 July 2016 and ceases on 30 June 2019. This was previously Declaration no. 93.

This important Declaration means that Sydney Airport must provide a price notification to the ACCC prior to increasing its prices for regional air services. This ensures that any increases to core Sydney Airport pricing for regional air services is capped at CPI and must be submitted to the ACCC for scrutiny. This arrangement was enacted in 2002 as part of the Sydney Airport Sales Act.

In assessing any such notified price increases the ACCC must have regard to the Direction which requires that Sydney Airport price increases relating to regional air services should not exceed the percentage increase in the Consumer Price Index (CPI).The value of this ACCC protection was proven back in 2010 when Sydney Airport sought to impose massive and unjustified price increases on Rex. The end result was that Sydney Airport dropped the unjust proposal.

Another recent example was when SACL wanted to raise the hangar lease amounts significantly about 3 years ago. After months of haggling, the initiative stopped. Rex understands that the management was reluctant to have the increase scrutinised by the ACCC. There is no further mention of this since.

This clearly shows that the intended objective of such declaration is working well. Rex believes that without the Declaration and Direction, Rex would have been priced out of Sydney Airport in 2010.

While Sydney Airport pricing is declared, all other capital city airports are not similarly regulated resulting in unbelievably high airport charges in places like Perth and to a smaller extent Brisbane and Melbourne. We have cited above the blatant and extreme abuse of market power by both Perth and Melbourne airports which clearly call for a declaration as a counterweight to their market power. Brisbane Airport has also pushed for making existing operators pay for building runways to serve future customers and only abandoned their plans upon strong resistance from the carriers.

Regional air services are as equally critical and essential right across Australia and Rex believes that all Capital City aeronautical services and facilities to regional air services should be declared under the Federal Governments Declaration no. 94.

3.1.2 Airport Non-Pricing Pressure Points

In addition to Capital City airport core pricing arrangements for regional air services being Declared, there are also additional protection measures required.

For example, a regional airline has a broad range of infrastructure requirements at a capital city airport. This includes hangar space to undertake necessary aircraft maintenance, office space for staff including airport staff and flight crew, ground support equipment storage areas, check-in desks and customer waiting areas, including airline lounges. These are all mandatory requirements for a regional airline to operate, yet they are not covered by any regulatory protection.

This leaves the smaller independent regional airlines highly exposed to both price increases associated with mandatory airport requirements and airport decision making that can lead to a significant negative impact to the airline and its customers. What maximises profitability for a Capital City airport may make an airline less efficient or add cost or reduce the quality of service and quite often all three of these outcomes are incurred.

Without regulatory oversight there is no ‘check and balance’.

For example, the regional airlines arrivals area could be relocated requiring a greater walk for regional customers, inadequate access to ground transport and an inability to connect with other regional, domestic and international services. This has a commercial impact to the airline which is a real cost and in addition, the airline incurs inefficiencies and additional staffing costs.

Regional airlines could also be directed to park aircraft in an area that is further away from the passenger terminal due to the prioritisation of larger aircraft. In the case of Sydney this requires additional bussing time (Rex owns 4 busses at Sydney Airport with bussing cost of about $800,000 a year) between the terminal and the aircraft with a consequential negative impact to on-time-performance due to the further distances and the busses having to cross live taxi lanes and holding for departing and arriving aircraft.

The airport does not offer any compensation for the deterioration of service levels, lost efficiencies and additional airline operating costs. In fact the airport attempts to impose additional aircraft parking charges due to the aircraft being directed to park in a General Aviation area.

Another area of concern is the benchmarking of the market rate. As airlines bring in more and more passengers, the retail business of the airport will thrive and the retailers are willing to pay more for the retail spaces. The airline then uses such higher retail rates to benchmark the rates to charge the airlines for office and lounge spaces, forgetting that it is the airlines that help the airport grow its retail business.

3.1.3 Access (Including Slot Availability)

At Sydney Airport the protection of NSW regional slots recognises Sydney Airport’s role as an essential transport hub for regional NSW.

The ring-fence protection of NSW regional slots formed part of the important legislative arrangements prior to the sale / privatisation of Sydney Airport in 2002. The ring-fence protection of NSW regional slots was a result of the strong commitment of both Coalition and Labor Governments to ensure that regional NSW continues to have guaranteed access to regional air services at Sydney Airport and this important measure is enshrined in legislation.

Sydney Airport tendered for the purchase of the airport on the basis of NSW regional slots being protected and would have accordingly reflected the legislated needs of regional NSW in their tender price.

Importantly, under the slots compliance scheme, all airlines have to comply with strict ‘use-it-or-lose-it’ provisions in order to maintain usage of the slots and this is equally applicable to the regional airlines operating with protected NSW slots. These historic precedence provisions require regional airlines to use at least 80% of their NSW regional slots in any given schedule period, otherwise the slots will be returned to the regional slot pool for alternative NSW intrastate regional usage.

It has been demonstrated that demand for NSW regional slots has been maintained between 2002 and 2018, as evidenced by the NSW regional slot pool being fully allocated in the legislated peak periods (6.00am – 11.00am and 3.00pm until 8.00pm) of operation at Sydney Airport.

Under the Sydney Airport Demand Management Act, Sydney Airport is also constrained by the arbitrary movement cap of 80 movements per hour which does not reflect the true current capacity of Sydney Airport. This arbitrary restriction was implemented more than 20 years ago in 1997, with only minor regulatory reform being applied during this period.

Whilst other Capital City airports (including Brisbane and Perth) have Slots or Runway Demand Management Systems (RDMS) in place, such systems are not legislated by Government.

In Rex's experience the risk is that Capital City airports can use a RDMS for commercial gain as opposed to using the system to fairly and equitably manage runway demand. This is done through the inclusion of "local rules" that unfairly treat smaller regional aircraft due to such aircraft representing a lower commercial return to the Capital City Airport.

An example of this was the RDMS implemented by Brisbane Airport in 2013 that does not grant historical slot precedence for regular scheduled charter services for regional aircraft with less than 50 seats. This means that an operator like Rex, who operates a 34 seat aircraft, cannot confidently bid for regular schedule charter work due to the airport slot uncertainty. Whilst an airport slot may be available at the time of the bid, it may be taken by a larger aircraft due to no historic slot precedence being accorded to the smaller aircraft.

Airports should not be allowed to use their monopoly position to achieve a better financial outcome than would be possible in either a competitive market or under regulated pricing. Rex does not believe that airports are presently subject to sufficient oversight. They can hide their conduct under the guise of rationales that, at face value, seem legitimate (e.g. legal requirements, safety, runway demand management schemes etc.) but in truth are not substantiated.

We have also seen examples of Capital City airports wanting to link a proposed RDMS with the aeronautical charges by saying that if the airline does not accept the airport charges then they won't be granted airport slots under the RDMS.

3.2 Government Grants

Rex has witnessed firsthand the irrational allocation of Government funding to regional airports by both State and Federal Governments. Rex supports rational airport upgrades that are commensurate to the needs of the regional community and there are many examples where Rex has provided local councils with letters of support to assist with such funding application.

However there are numerous examples where there has been a significant over allocation of funding for non-essential airport expenditure. Rex would direct the committee to examine how much State and Federal Government funding has been allocated to regional airports, such as Dubbo (NSW), Orange (NSW) and Kangaroo Island to suggest a few.

Kangaroo Island is in the final stages of a $20M airport upgrade which has so far resulted in QantasLink mounting a less than daily service between Kangaroo Island and Adelaide (in competition to Rex's 3-4 daily services to Adelaide) and a limited trial service by QantasLink between Kangaroo Island and Melbourne, both of which could have occurred prior to the extensive airport upgrade being undertaken. The $20M funding is a significant taxpayer spend and there is no sound business case to support it. In Mount Gambier, they are looking across the fence to Kangaroo Island and wanting to do the same based on a misguided view that Kangaroo Island airport upgrade is responsible for QantasLink bringing competition.

It is well and good for a regional airport to receive State or Federal Government funding for airport works however from Rex's experience it will result in the ongoing airport costs – depreciation, operating and maintenance costs - spiralling out of control.

The airport will inevitably try to pass these huge cost increases on to passengers. Fewer passengers will travel and in turn the remaining passengers will face even higher airport charges. This will cause a downward spiral in passenger numbers to a level where the regional air service is no longer viable.

In the case of Kangaroo Island, depreciating an additional $20M spend over 10 years would see additional depreciation costs of $2M which equates to around $40 per air ticket based on approximately 50,000 passengers per year. When it is realised that this far exceeds the airline's profit per ticket we can easily determine what will ultimately happen to the air service if the unrealistic assumptions in the funding application do come to fruition.

Rex also questions the manner in which these grants are treated in the accounts of the various Councils. According to AASB 120 grants relating to assets have to be treated in one of two ways. Either as deferred income over the life of the asset or as a deduction to depreciation of the asset over the life of the asset.
If the above accounting treatments were applied, council should not be able to claim that airport upgrades have led to higher depreciation rates which need to be recovered through head taxes. Yet we still see this

used as a reason for increased head taxes. **One such blatant example is Wagga Wagga that has booked in an increase of depreciation of $2M a year due simply to a revaluation of assets**.

3.3 Difference in Behaviour of 'For Profit Airports' and the Council Owned Airports

Regional airports were vested to the local councils at no cost (often with a large sum to offset future maintenance costs) by the Federal Government prior to 1991. Regional airports are a vital piece of community infrastructure and form a valuable community asset.

In Rex's vast network of 60 airports, around 70% of the council owned regional airports are not able to recover the operating expenses from the airport charges. Most council's understand that charging a head tax rate to cover operating expenses would make the marginal air service completely unviable.

Local Councils should not consider the airport as a cash cow. Regional airports should be treated no differently than local roads and bridges as critical local infrastructure that has broad ranging benefits across the entire council municipalities. Yet, many regional airports adopt a user pays approach that requires the 'airport business' to stand-alone at no cost to the council ratepayer and in many cases generate a substantial surplus back to council.

Rex estimates that it costs about $500,000 annually to effectively operate a regional airport, which includes having an adequate sinking fund to undertake significant airport works. From Rex's experience, the high cost of depreciation is often cited as the basis for needing much higher airport revenue. As outlined earlier, it is well and good for regional airports to receive State and Federal Government funding for airport investment however this increases the asset value of the airport which in turn makes the council want to claim higher airport depreciation costs as a pretext for raising head tax.

The concrete steps that the local councils can take to lower the cost of airfares are:

- Reduce airport charges / reduce the airport passenger tax. If this reduction is translated into lower ticket fares (through partnership agreements with the operators), there will be a stimulatory effect on passenger numbers. More importantly it will create a positive impact on the socio-economic well-being of the community. The net gain to the community far outweighs, in our opinion, the potential drop of airport revenue (airport revenue may actually increase if the price elasticity of demand works in the airport favour). Local councils should get out of the myopic mindset and think of the bigger and longer term good of their community. Separate from the social advantages, the economic activity generated through a regional airport far exceeds any perceived short-falls in a regional airport's financial position.

- Work in partnership with the airline. Rex has pioneered and successfully implemented many innovative partnership programmes with various cities where both parties invest into growing passenger numbers by reducing airfares.

- State Governments can effectively reduce airfares by tendering out the larger routes to a sole successful tenderer. The tenderer has to commit to an average fare and capacity/frequency level and in exchange will have the sole right to the route. Load factors for the successful operator will shoot up and this will allow the tenderers to commit to a lower average fare as it is able to harvest a higher per trip revenue in spite of the average fare being lower. This model has been successfully implemented by the Queensland Government for several years now.

4. CONCLUSION AND RECOMMENDATIONS

In this submission, Rex has attempted to provide first hand examples of the challengers faced by Rex, as Australia's largest independent regional airline. It has been clearly demonstrated in the above examples that the airport owners, councils for the majority, are often misguided, political and myopic and would not hesitate to abuse market power for their self serving purposes even if that would result in long term damage to the local community.

As can be seen in the case studies, Rex does make every effort to challenge an airport owner when faced with an unreasonable attempt to increase airport charges that will inevitable drive up the cost of an airfare. Often Rex is forced to go to extreme lengths to hold its ground following irresponsible attempts by airports. Unfortunately it is often the local community that suffers as a result of the airports irresponsible actions with increased cost of air travel or in some instances the reduction or even complete loss of services entirely.

Rex is strongly of the belief that regional airports need to be regulated to dissuade the local councils from acting in a myopic manner that could end up destroying the local community.

Rex would recommend a framework whereby the airline and the regional airport owner would negotiate in good faith but if agreement could not be reached then either party could request the ACCC to make a decision as to which of the 2 positions to accept and such a decision would be binding on both parties.

Such an approach would be the most cost effective as the very threat of intervention by the ACCC and the negative publicity that would generate in the local community would be sufficient in most cases for the local councils to act responsibly.

As for the capital city airports and other bigger airports, Rex believes that they should all be declared just like Sydney Airport is. In addition for commercial disputes not covered by the declaration, the same framework for the regional airports could be used i.e. negotiate then arbitrate by the ACCC.

RECOMENDATIONS

R1 – That greater regulatory provisions be imposed to allow Airlines (and Airports) to evoke the negotiate - arbitrate model in the event of a dispute impasse

R2 – No change be made to the existing declaration status of Sydney Airport

R3 – No change be made to the ring-fence protection on regional slots at Sydney Airport

R4 – That the ACCC review the current 'light handed' approach of economic regulation at major airports

5. ANNEX

[IN CONFIDENCE]