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13 March 2014

By Electronic Transmission

Senator David Bushby
Chairman
Senate Economics Legislation Committee
PO Box 6100
Parliament House
CANBERRA ACT 2600

Email: economics.sen@aph.gov.au

Our Ref: I200-882

Dear Chairman,

SUBMISSION TO THE SENATE ECONOMICS LEGISLATION COMMITTEE ON THE *QANTAS SALE AMENDMENT BILL 2014*

The Australian and International Pilots' Association (AIPA) is the largest Association of professional airline pilots in Australia. We represent nearly all Qantas pilots and a significant percentage of pilots flying for the Qantas subsidiaries (including Jetstar Airways Pty Ltd). AIPA represents over 2,300 professional airline transport category flight crew and we are a key member of the International Federation of Airline Pilot Associations (IFALPA) which represents over 100,000 pilots in 100 countries.

AIPA, through its Safety and Technical Sub-Committee, is committed to protecting and advancing aviation safety standards and operations. We are grateful for the opportunity to make a submission to the Senate Economics Legislation Committee on the *Qantas Sale Amendment Bill 2014*.

The Terms of Reference

In its examination of the provisions of the Bill, the Committee has been asked to:

- evaluate the effect of the proposed amendments on the aviation sector and the broader Australian economy;
- scrutinise the detail and impact of the legislation, including any potential impact on other legislation; and
- consider the opportunities the amendments will provide for Qantas to increase its competitiveness through the harmonisation of Australia's aviation regulatory framework.

Australia's current aviation regulatory framework for international airlines

In preparation for Cabinet considering the Qantas request for financial assistance, AIPA produced a Parliamentary Brief that addressed Australia's current aviation regulatory framework for international airlines. We have attached the Brief and its covering letter to this submission for the benefit of the Committee, noting that some of the widely-discussed policy options have now been clarified in the bill

before this Committee. Nonetheless, we believe that the context of our recommendations is important, if only to fully inform any future proposals to liberalise beyond what is proposed in this current bill.

Under our current aviation regulatory framework, an airline is designated as an Australian international airline through the Department of Infrastructure and Regional Development ("the Department") issuing an International Airline Licence pursuant to section 13 of the *Air Navigation Act 1920* (*ANA 20*). The sections of the *ANA 20* relevant to the designation of Australian international airlines form two groups: first, the foreign ownership limits (ss11A and 11B); and second, the International Airline Licence provisions (ss12 and 13).

The foreign ownership limits apply to all Australian international airlines other than Qantas. Qantas is excluded solely on the basis of the mutually exclusive but entirely complementary foreign ownership limits set out in s7 of the *Qantas Sale Act 1992 (QSA 92)*.

The International Airline Licence provisions apply to all Australian international airlines, including Qantas. However, there are no specific requirements to qualify for the grant of an International Airline Licence – instead, s13 merely provides the head of power for specific licensing regulations. Despite that head of power, there are no requirements prescribed as conditions precedent for the grant of an International Airline Licence in the *Air Navigation Regulations 1947* (*ANR 47*), as the regulations refer only to the things to be included in the application and, in regard to making a decision on the application, grant the Secretary unlimited discretion. Ultimately, the actual requirements that are necessary to satisfy our most conservative bilateral and multilateral Air Service Agreements (ASAs) are set out in an entirely discretionary Departmental Guidance Note [1]. That Guidance Note is not even a Legislative Instrument and thus is not subject to oversight by the Parliament.

On the other hand, the *QSA 92* is highly prescriptive. Part 3 of the *QSA 92* is the only active provision (the remainder being historical mechanisms for the transfer from public to private ownership) and s7 sets out restrictions on foreign ownership, voting restrictions, use of the name "Qantas", location of the Head Office and majority of facilities, Board membership and incorporation restrictions.

In all respects, compliance with the *QSA 92* is more stringent than any requirement placed on other Australian airlines.

Should the *QSA 92* be more stringent than the *ASA 20*?

Clearly, the effect of the *Qantas Sale Amendment Bill 2014* indicates that the Government does not think so.

AIPA does not wholly share that view. We consider the Explanatory Memorandum for the *Qantas Sale Amendment Bill 2014* to be misleading to the extent that it implies that Qantas will be subject to international airline designation criteria under a legislative regime very similar to that of the *QSA 92*. As we have discussed above, that is not true – the international airline designation criteria are solely at the discretion of the Secretary of the Department.

Perhaps, in regard to this discretion, Ralph Willis as Minister for Finance had a crystal ball. In his Second Reading speech on the *Qantas Sale Bill 1992*, he said:

> The fundamentals of the national interest safeguards, referred to earlier, need to be enshrined in legislation.
>
> These safeguards are important to maintain the basic Australian character of Qantas, as well as to ensure that Qantas's operating rights under Australia's various bilateral air service agreements and arrangements with other countries are not put under threat. Once in legislation, these safeguards will not be subject to the whim of the Government of the day.[2] [emphasis added]

AIPA maintains the view that his approach to the issue was correct.

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1 Department of Infrastructure and Regional Development, *International Airline Licences—Guidance Notes*, January 2014, at: http://www.infrastructure.gov.au/aviation/international/files/20140109-IAL_guidance_notes.pdf (accessed 13 March 2014)

2 Mr Willis (Minister for Finance), House Hansard, 04 November 1992, Page 2588

Foreign Ownership

As indicated in the attached Parliamentary Brief [3], AIPA has examined the history of the 25% and 35% foreign ownership limits in the *QSA 92* and consequently strongly recommended that all Parliamentary parties and members agree to immediately amend the *QSA 92* to delete paragraphs 7(1)(aa) and (b), as they no longer serve any useful purpose.

COMPARISON OF FOREIGN OWNERSHIP PROVISIONS	
QSA 92	**DIRD IAL GUIDANCE NOTE**
(a) impose restrictions on the issue and ownership (including joint ownership) of shares in Qantas so as to prevent foreign persons having relevant interests in shares in Qantas that represent, in total, more than 49% of the total value of the issued share capital of Qantas;	Foreign shareholdings be limited to no more than 49 per cent of the total value of the issued share capital of the Australian airline.
(aa) impose restrictions on the issue and ownership (including joint ownership) of shares in Qantas so as to prevent foreign airlines having relevant interests in shares in Qantas that represent, in total, more than 35% of the total value of the issued share capital of Qantas;	No restriction
(b) impose restrictions on the issue and ownership (including joint ownership) of shares in Qantas so as to prevent any one foreign person having relevant interests in shares in Qantas that represent more than 25% of the total value of the issued share capital of Qantas;	No restriction
(c) impose restrictions on the counting of votes in respect of the appointment, replacement and removal of a director of Qantas so as to prevent the votes attaching to all substantial foreign shareholdings being counted in respect of the appointment, replacement or removal of more than one-third of the directors of Qantas who hold office, at any particular time;	No restriction

We also explained why we need to retain the 49% foreign ownership limit for all Australian international airlines in order to partially satisfy the "substantial ownership and effective control" concept contained in many of Australia's international ASAs. We argued that it makes no sense at all to retain that same limit in two places and consequently strongly recommended that all Parliamentary parties and members agree to immediately amend the *QSA 92* to delete paragraph 7(1)(a) and the *ANA 20* to remove the Qantas exception, with the intention of imposing on Australian-designated international airlines only one set of foreign investment limits.

AIPA is agnostic about restrictions on voting rights of foreign shareholders for Board elections.

The Effective Control Provisions

AIPA agrees that the rules related to the Board are identical, rendering paragraphs 7(1)(i) and (j) redundant.

COMPARISON OF EFFECTIVE CONTROL PROVISIONS	
QSA 92	**DIRD IAL GUIDANCE NOTE**
(i) require that, at all times, at least two-thirds of the directors of Qantas are to be Australian citizens;	At least two-thirds of the Board members are Australian citizens;
(j) require that, at a meeting of the board of directors of Qantas, the director presiding at the meeting (however described) must be an Australian citizen;	The Chairperson of the Board is an Australian citizen;

3 AIPA Parliamentary Brief, "Changing the *Qantas Sale Act 1992*", 26 February 2014

The National Interest Provisions

AIPA believes that protecting the company name and place of incorporation is reasonable, even though there appears to be no sound basis for Qantas management to abandon the historical goodwill associated with Qantas. Prohibiting the conduct of scheduled international air transport passenger services under a different name is also reasonable in a heritage sense, but we would argue that both Jetstar and Jetconnect violate that clause on a "see-through" basis, despite the argument that both of those wholly-owned subsidiaries are separate corporate entities. Unfortunately, that legal/policy distinction has now also been given the Department's imprimatur in relation to the Virgin restructure, thus neutering another *QSA 92* restriction through the creation of a regulatory *fait accompli*.

AIPA agrees that the rules related to the location of the head office are identical, rendering paragraphs 7(1)(g) redundant.

COMPARISON OF NATIONAL INTEREST PROVISIONS	
QSA 92	**DIRD IAL GUIDANCE NOTE**
(e) prohibit Qantas from taking any action to bring about a change of its company name to a name that does not include the expression "Qantas";	No restriction
(f) prohibit Qantas from conducting scheduled international air transport passenger services under a name other than: (i) its company name; or (ii) a registered business name that includes the expression "Qantas";	No restriction
(g) require that the head office of Qantas always be located in Australia;	The airline's head office is in Australia;
(h) require that of the facilities, taken in aggregate, which are used by Qantas in the provision of scheduled international air transport services (for example, facilities for the maintenance and housing of aircraft, catering, flight operations, training and administration), the facilities located in Australia, when compared with those located in any other country, must represent the principal operational centre for Qantas;	The airline's operational base is in Australia.
(k) prohibit Qantas, at all times, from taking any action to become incorporated outside Australia.	No restriction[4]

In all other respects, we are particularly concerned that the abandonment of the national interest 'facilities' provisions of paragraph 7(1)(h) of the *QSA 92* as a consequence of repealing Part 3 has not been fully examined.

Before we discuss the existing provisions, AIPA notes that, while the Department's IAL Guidance Notes may appear to provide some form of equivalence to paragraph 7(1)(h) of the *QSA 92* , that is <u>not</u> the case.

The term "operational base" is not defined in the IAL Guidance Notes. It is not a term used in the *ANA 20* or the *ANR 47*. Even ICAO does not use the term in its *Manual on the Regulation of International Air Transport*[5]. AIPA finds it frustrating that there is effectively no transparency in what again seems to be an unfettered discretion of the Secretary to accept as much or as little as is on offer or as suits the shaping of policy application.

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4 There is a presumption that an Australian-designated airline would be incorporated in Australia, but the requirement is not specific in the IAL Guidance Notes.

5 ICAO, 2004, *Manual on the Regulation of International Air Transport, Doc 9626*. International Civil Aviation Organisation, Montreal

AIPA has consistently advised the Parliament about the dangers inherent in relaxing or removing the national interest provisions of the *QSA 92* for at least the last seven years. Indeed, we have supported a number of Bills that have sought to strengthen those provisions, the most recent of which was the *Qantas Sale Amendment (Still Call Australia Home) Bill 2011*. Our submission[6] to the Senate Inquiry into that Bill encapsulated the vast majority of considerations surrounding the *QSA 92* and the national interest provisions in particular.

Our initial concerns were triggered by the Airline Partners Australia Limited (APA) bid for Qantas and the historical approach of private equity in extracting "value" from such assets. As part of that proposed buy-out, APA signed a Deed of Undertaking with the Treasurer that demonstrably extended the 'restraints" of the QSA 92, although we expressed the view that the enforceability and true long-term commitment were doubtful[7]. It is noteworthy that APA did not seek to diminish the national interest provisions of the *QSA 92* and, *prima facie*, gave every indication that they believed that they could sustain a viable Qantas business despite the *QSA 92*.

Our position on the historical application of the national interest provisions of the *QSA 92* is that they represented the price (and a form of trailing commission) to be paid as consideration to the Australian public for the transfer of a substantial national asset to private ownership.

The drafting of the national interest 'facilities' provisions of the *QSA 92* occurred at a time when Qantas was a substantial international airline, particularly compared to its newly absorbed domestic partner Australian Airlines. Qantas was the largest civil source of transport category aircraft engineering and maintenance expertise, operational training and related support services in this country.

AIPA believes that Qantas still retains that position, albeit in a much diminished way. We also believe that the architects of the QSA 92 did not want the Qantas contribution to the national store of technical knowledge and skills or the economic multiplier that accompanied that contribution to be at the mercy of commercial expediency in the hands of short-sighted opportunists. While there was, in our view, a presumption that domestic aircraft maintenance, catering, flight operations, training and administration would never be shifted offshore, it was clear that international operations could easily shift the provision of operational and support activities to one or more of the many destinations in the international network.

That risk clearly remains.

AIPA accepts that the aviation world is constantly changing. We accept that it is a business imperative to seek efficiencies at all times. We accept that Australia struggles to provide markets of sufficient scale to sustain a wish list of national industries. However, we also believe that there are sound reasons to retain certain national capabilities as a hedge against a growing dependency on overseas suppliers of goods and services, particularly when there are credible circumstances where one or more suppliers of critical goods and services may prove to be unable or unwilling to meet our needs in the required timeframe.

As a fundamental tenet, AIPA believes that the retention of certain national capabilities can justify a price premium in the provision of certain goods and services.

We recognise that there are two facets to justifying a premium: within the business and external to the business. Within the business, simple manpower cost comparisons in labour-intensive areas need to be replaced with proper value assessments, particularly in business continuity and crisis management planning. Externally, governments need to consider incentives that induce businesses to continue to contribute to the national interest.

However, we also recognise that there are cross-over points where the size of a particular market provides insufficient scale to constrain a local price premium to acceptable levels. One reading of the demise of Australian car manufacturing is that once Ford decided that its market share couldn't support its internal premium and terminated production, it had little or no effect on the declining

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6 AIPA, Submission 4 to the Senate Rural Affairs and Transport Legislation Committee Inquiry into the *Qantas Sale Amendment (Still Call Australia Home) Bill 2011*, 14 October 2011

7 Senate Standing Committee on Economics, Report of the *Inquiry into the Qantas Sale (Keep Jetstar Australian) Amendment Bill 2007*, 20 March 2007 at http://www.aph.gov.au/Senate/committee/economics_ctte/completed_inquiries/2004-07/qantas/report/index.htm (accessed 23 September 2011), pp 13-14

market for the other local producers while further reducing scale for the component industries, thus triggering a systemic review where both internal and external price premiums were judged to be unsustainable. Large aircraft heavy maintenance appears to be headed down the same path.

AIPA sees this as a significant policy conundrum which, in large measure, informs our continued quest for a Productivity Commission review of its 1998 report on International Air Services and related national interest issues. In many ways, the future policies are being shaped by a series of *fait accomplis* created by actions and inactions by both the Department and Qantas – the coordination of which seems improbable – when AIPA believes those policies desperately need to be shaped in the light of the broader economic view that the Productivity Commission provides.

For example, in the international airline space, we have already surrendered our large jet engine overhaul capability on a simple cost basis. Consequently, to the best of our knowledge, the engines on our new RAAF A330 tankers cannot be serviced in Australia. In parallel, Qantas fleet decisions are well on the way to removing the scale for heavy maintenance facilities in Australia, regardless of any cost versus value debate on the labour element. Once the Boeing 767 fleet is retired next year, the few Qantas international aircraft maintained to any degree in Australia will contribute very little to "the facilities, taken in aggregate" equation required by paragraph 7(1)(h) of the *QSA 92*. Arguably, the economic benefit associated with large aircraft heavy maintenance has already been transferred offshore.

AIPA sees that situation as a major national interest mistake.

<u>Protecting the National Interest without the *QSA 92*</u>

AIPA has seen no evidence of the Department ever enforcing the *QSA 92*. If Qantas is heading towards non-compliance with paragraph 7(1)(h) as a consequence of offshoring the vast majority of the heavy maintenance of the international fleet, it appears that the Department would consciously "let it go through to the keeper" on the premise that enforcement would create a need for Government to provide significant incentives to maintain an uneconomic business. Clearly, that is not the tenor of the current Government.

If the Cabinet decided to abandon the national interest 'facilities' provisions of paragraph 7(1)(h) of the *QSA 92* on the basis of levelling the playing field with Virgin by relying on the requirements for international airline licensing under the *ANA 20*, we think that the latter requirements are inadequate to achieve that purpose.

In our Parliamentary Briefing, we said that our main concern about the IAL Guidance Notes is the lack of precision, undoubtedly deliberate in a quest for flexibility, in the prescription and enforceability of the economic benefits that may have to be paid by the applicant as consideration for the commercial advantage that accrues from being granted an Australian International Airline Licence. AIPA holds the view that access to the Australian market and Australian air rights in the past may well have been given away far too cheaply and that the benefits that have purportedly accrued to the Australian public may be exaggerated.

While AIPA holds the current Secretary and his senior managers in high regard, we are philosophically opposed to "government in secrecy" through a lack of transparency in critical decision-making. In that context, we went on to say:

> We also respect the need for flexibility, particularly so that our approach to aviation liberalisation is not determined by the most conservative of our ASAs. However, in balance, we are not convinced that the exercise by the Department of its very wide discretions necessarily benefits all aviation stakeholders. Some greater formal prescription seems justified: first, to clarify what the continuing requirements placed on licence holder may be, and second, to fetter Departmental discretion.[8]

AIPA proposes that any repeal of paragraph 7(1)(h) of the *QSA 92* must be matched by a corresponding amendment to the *ASA 20* that formalises the ICAO advice on what might reasonably constitute a test of the evidence of:

> **principal place of business** may be predicated upon the following: the airline is established and incorporated in the territory of the designating party in accordance with relevant national laws and regulations, has a substantial amount of its operations and capital investment in physical facilities in the

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8 AIPA Parliamentary Brief, *op. cit.*, page 11

> territory of the designating party, pays income tax, registers and bases its aircraft there, and employs a significant number of nationals in managerial, technical and operational positions. [9]

The various elements of this definition and that of 'effective regulatory control'[10] appear within the IAL Guidance Notes, but not in our view in any coherent fashion. Given that Australia is moving towards 'principal place of business' as our preferred basis for negotiating ASAs, AIPA see no problem in structuring the *ANA 20* to require applicants seeking Australian designation to satisfy requirements for the modern 'incorporation, principle place of business and effective regulatory control' approach in parallel with those of the traditional 'substantial ownership and effective control' approach.

WHERE WE STAND

The Effect of the Proposed Amendments on the Aviation Sector and the Broader Australian Economy

AIPA believes that the proposed amendments, unamended, will allow Qantas to replicate the Virgin restructure and, subject to Foreign Investment Review Board (FIRB) approval, sell off up to 100% of Qantas Domestic. We note that Qantas currently has that option with Jetstar, but has made no moves in that direction.

There would be no immediate benefit to the broader Australian economy because any initial foreign capital investment will flow to the shareholders rather than Qantas. Qantas would not gain a capital benefit until such time that there is one or more major shareholders on the register who have the capacity and willingness to participate in a capital raising.

There may be an overall loss of benefit to the broader Australian economy if the ACCC is unable to restrain a cashed-up Qantas in the domestic market, based on the "two for one" threat to Virgin.

Given the vagueness of the requirements for international airline licensing under the *ANA 20*, there may be an overall loss of benefit to the aviation sector and the broader Australian economy if a Qantas freed from the restraints of the *QSA 92* moves quickly to offshore as much of operational and support functions as the Department will permit but fails to achieve a consequent improvement in downstream economic benefit to Australia.

There would be no immediate direct benefit to the broader Australian economy since the proposed amendments are a rearguard domestic action that does nothing to address the distortions in the international market faced by all Australian international airlines.

The Detail and Impact of the Legislation, including any Potential Impact on other Legislation

AIPA strongly recommends repealing the 25% and 35% foreign ownership limits as they serve no useful purpose.

AIPA strongly recommends repealing the 49% foreign ownership limit placed on Qantas by the *QSA 92*, provided that all Australian-designated international airlines are subject to the foreign ownership limits in the *ANA 20*.

AIPA is agnostic about restrictions on voting rights of foreign shareholders for Board elections. If no other legislation so limits voting rights of foreign shareholders, then there seems to be no rational reason for Qantas to be different.

Subject to formalising the IAL Guidance Notes in the *ANA 20*, AIPA has no objection to repealing the *QSA 92* provisions relating to the make-up of the Board or the location of the Qantas headquarters.

AIPA believes that protecting the company name and place of incorporation is reasonable, even though there appears to be no sound basis to abandon the historical goodwill associated with Qantas. Amending the *ANA 20* to include 'incorporation, principle place of business and effective regulatory control' would satisfy that position.

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[9] ICAO, 2004, *op.cit.*, page 4.4-5

[10] *Ibid.*, page4.4-5

AIPA is strongly opposed to the repeal of the national interest ‘facilities’ provisions of paragraph 7(1)(h) of the *QSA 92* unless the *ANA 20* is amended to include ‘incorporation, principle place of business and effective regulatory control’ requirements.

The Opportunities the Amendments will provide for Qantas to Increase its Competitiveness through the Harmonisation of Australia's Aviation Regulatory Framework.

AIPA understands the use of the term “harmonisation” to apply to the domestic framework rather than to any international regulatory arrangements. All of the Qantas commentary that led to the *Qantas Sale Amendment Bill 2014* was in the domestic context and, to the best of our knowledge, the capital situation of Virgin Australia International remains unchanged.

Qantas has dominated the domestic market since its privatisation. The competitiveness of Qantas in the domestic market is an outcome of management decisions on product and aircraft investments. The domestic facilities and infrastructure are not regulated by the *QSA 92*. Foreign investment in the domestic operation has been restricted by the additional limits in the *QSA 92* affecting single and total airline holdings, but until the recent Virgin restructure, Virgin, Jetstar and Qantas were each limited to 49% in total due to their international licence conditions.

The competitiveness of Qantas in the international market depends on the same investment decisions but the vast majority of competitors do not share the same base economic conditions as Australia and many have stricter limits on foreign investment.

To the best of AIPA‘s knowledge, there has never been a public assessment of the impact of the *QSA 92* on the capital position of Qantas. It is therefore difficult to project what effect the proposed legislative changes will generate, either in terms of reduced costs or in terms of attracting greater interest among foreign investors. Unfortunately, the proposed changes do not necessarily have a direct correlation with competitiveness, since poor decisions on aircraft, product and capacity allocation can all easily negate any improvements in the capital position.

AIPA suggests that this particular subject reinforces the need for a broader Productivity Commission review and we seek the Committee’s endorsement of our proposed Terms of Reference, which form part of our attached letter to the Treasurer.

Nathan Safe
President
Australian & International Pilots Association

Attachments: 1. AIPA Covering Letter and Parliamentary Briefing of 26 February 2014

2. Letter to the Treasurer and Proposed PC terms of Reference of 18 November 2013

Attachment 1 to
AIPA Submission to the Senate Economics
Legislation Committee 13 March 2014

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26 February 2014

Dear Parliamentary Representative,

WHY WE NEED TO BRING SOME RATIONAL THOUGHT TO THE *QANTAS SALE ACT 1992* DEBATE

The attached Briefing was prepared in response to the debate conducted in the Australian media about the continued relevance of the *Qantas Sale Act 1992 (QSA 92)*. The debate has involved many parties who, in AIPA's opinion, have little knowledge of the background to the *QSA 92* and seem to have limited knowledge of the consequences of their recommendations.

Our Concerns

While AIPA notes the widespread public commentary about amending or repealing the foreign ownership limits of the QSA 92 either specifically or by repealing the entire Act, we are most concerned about the shallowness of the commentary from both a domestic and an international policy perspective. It is clear to us that many of the commentators have no real understanding of the complex web of policy and regulatory interactions involved in the trading and management of international air rights.

The attached briefing is intended to provide some context to the issues, as well as to some of the historical issues related to the Australian legislation.

AIPA has examined the history of the 25% and 35% foreign ownership limits in the *QSA 92* and consequently strongly believes that it is appropriate to repeal both limits as they serve no useful purpose.

AIPA reminds interested parties that the 49% foreign ownership limit placed on Qantas by the *QSA 92* is tied to the 49% foreign ownership limit placed on all other Australian-designated international airlines by the *Air Navigation Act 1920* (*ANA 20*). In both cases, the limit reflects partial satisfaction of the predominant 'substantial ownership and effective control' clause of our Air Service Agreements (ASAs) – a clause that reflects the agreed position between the signatories of the ASA. That 'substantial ownership' clause relates to <u>any</u> Australian-designated international airline and is a default trigger clause if the 49% foreign ownership limit is abrogated.

AIPA reminds interested parties that a unilateral repeal of the 49% foreign ownership limit placed on Qantas by the *QSA 92* may breach many of our ASAs and the underpinning treaties and <u>could result in the suspension or cancellation of the very traffic rights upon which Qantas depends to survive</u>. Such a repeal would also place Qantas in an privileged financial position and would unfairly restrict all other Australian-designated international airlines.

AIPA notes that the *ANA 20* includes an exception provision ("the Qantas exception") that ensures that the foreign ownership limits in the *ANA 20* do not apply to Qantas because of the separate but matching restrictions in the *QSA 92*. Further, we note that the *ANA 20* does not include any 'national interest' provisions such as those that apply in the *QSA 92.*

AIPA strongly believes that the repeal of the Qantas exception in the *ANA 20* would be an essential precondition to any repeal of the 49% foreign ownership limit placed on Qantas by the

QSA 92, in order for the playing field to remain level by ensuring all Australian-designated international airlines are subject to the foreign ownership limits in the *ANA 20*.

AIPA strongly recommends that suitable national interest requirements based on the ICAO guidance on 'principal place of business' are inserted into the *ANA 20* before any consideration is given to repealing the national interest provisions of the *QSA 92*.

Our Recommendations

AIPA strongly recommends that all Parliamentary parties and members agree to immediately amend the *QSA 92* to delete paragraphs 7(1)(aa) and (b) as they no longer serve any useful purpose.

AIPA strongly recommends that all Parliamentary parties and members reject any proposal to unilaterally free Qantas of all foreign ownership limits until such time as the Parliament is assured that there will be no consequential effect on any international capacity allocations to Qantas.

AIPA strongly recommends that all Parliamentary parties and members agree to immediately amend the *QSA 92* to delete paragraph 7(1)(a) and the *ANA 20* to remove the Qantas exception, with the intention of imposing on Australian-designated international airlines only one set of foreign investment limits.

AIPA strongly recommends that all Parliamentary parties and members agree that the national interest provisions set out in s7 of the *QSA 92* should not be repealed until the *ANA 20* is amended to impose on Australian-designated international airlines one set of national interest requirements based on the ICAO guidance on 'principal place of business'.

We ask that you consider that attached brief before deciding upon your Parliamentary response to any actions in regard to the QSA 92.

Yours sincerely,

Nathan Safe
President
Australian & International Pilots Association

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PARLIAMENTARY BRIEF

26 FEBRUARY 2014

CHANGING THE *QANTAS SALE ACT 1992*

Why is the *Qantas Sale Act 1992* suddenly the 'Talk of the Town'?

The *Qantas Sale Act 1992* ("the *QSA 92*") has leapt into prominence in the political and public debate because the management of Qantas have made a case that Qantas is mortally, if not fatally, financially disadvantaged on virtually every front because Qantas alone is subject to the constraints of the *QSA 92*. The debate seems to have rapidly polarised into ideological positions, rather than technically informed positions.

Much of the public debate on the *QSA 92* has focused on the foreign ownership restrictions, since Qantas management have argued that the capital requirements of the business have not and will not be provided from the Australian capital markets and, by implication, have not and will not be attractive to foreign investors limited to a maximum individual shareholding of 25% or as part of a maximum airline pool of 35%.

AIPA has for some time maintained a philosophical position that the nationality of the ownership is largely irrelevant provided that the economic benefit of the investment is essentially retained in Australia. While we recognise the complex web of policy and regulatory interactions involved, we are very concerned that much of the current political and public rhetoric does not reflect the same understanding of the real issues.

As we will explain, the 25% and 35% foreign ownership limitations should be removed immediately as they are irrelevant leftovers from a bygone era of international aviation regulation, but varying the 49% limit propels us into the world of treaties and bilateral/multilateral arrangements with other countries with arrange of potential consequences. Importantly, repealing the QSA 92 does much more than removing foreign investment constraints – it also removes the other 'national interest' requirements that tie Qantas to Australia. This, in itself, necessitates a much more considered approach to changing the legislation than merely adopting an 'all or nothing' stance in the media.

What has suddenly changed about the *Qantas Sale Act 1992?*

In terms of the *QSA 92* itself – nothing! However, the environment within which Qantas works has undergone a couple of recent step-changes and the combination of the consequences of the regulatory/policy shift and the recent economic environment have reignited the debate about the role of the QSA 92 in modern Australian aviation.

The history, or at least that which is in the public arena, will demonstrate how messy things have become in a very short time.

On 06 February 2012, Qantas appeared before the Senate Rural Affairs and Transport Legislation Committee to give evidence to assist the Senate in its Inquiry into the *Air Navigation and Civil Aviation Amendment (Aircraft Crew) Bill 2011* and the *Qantas Sale Amendment (Still Call Australia Home) Bill 2011*. The CEO of Qantas, Mr Alan Joyce, was asked a very specific question and gave a very specific answer:

> **Senator GALLACHER**: ... What is your view on the Qantas Sale Act per se? Is it still relevant current or do you have it removed?
>
> **Mr Joyce**: We support the government's view on this that the Qantas Sale Act has a purpose. We support the minister's position, which is a modification of the Qantas Sale Act, in his white paper which I believe would review the 25 per cent ownership requirements but keep the 51 per cent ownership requirements, which we think is appropriate. We obviously as an Australian carrier also have the Air traffic act and Air Navigation Act requirements which means for traffic rights we have that 51 per cent. Qantas today has well over 60 per cent of its ownership in Australia so that those requirements under the act we agree with. Of course the other requirements that require us to have the chairman and the majority of the board being Australian we totally support.[1]

It is noteworthy that the *Qantas Sale Amendment (Still Call Australia Home) Bill 2011* was primarily about strengthening the so-called 'facilities' provisions of the QSA 92, yet nowhere in the debate was there any suggestion by Mr Joyce that the original provisions should be 'watered down' or repealed altogether.

Mr Joyce refers to the *Air Navigation Act 1920* ("the *ANA 20*") in his uncritical acceptance of the role and appropriateness of the *QSA 92*. However, that public acceptance of the *QSA 92* was undoubtedly predicated on the historically complementary nature and application of the two acts by the then Department of Infrastructure and Transport ("the Department"). We will discuss the role of the Department in disrupting the harmony of the two acts, but first we need to establish the context and relevance of the *ANA 20* as the sibling of the *QSA 92*.

The *Air Navigation Act 1920*

The *ANA 20* provides for the economic regulation of aviation in Australia. It provides for the codification of our International Civil Aviation Organisation (ICAO) obligations and relevantly at Schedule 2 sets out the International Air Services Transit Agreement (IASTA) , the source of the foreign ownership limitations in bilateral and multilateral Air Service Agreements (ASAs). Australia ratified that Agreement on 28 August 1945. Section 5 of Article I of the IASTA states:

> Each contracting State reserves the right to withhold or revoke a certificate or permit to an air transport enterprise of another State in any case where it is not satisfied that **substantial ownership and effective control** are vested in nationals of a contracting State, or in case of failure of such air transport enterprise to comply with the laws of the State over which it operates, or to perform its obligations under this Agreement. [emphasis added]

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[1] Qantas Group, Senate Committee Hansard, Senate Rural Affairs and Transport Legislation Committee *Inquiry into the Air Navigation and Civil Aviation Amendment (Aircraft Crew) Bill 2011 and the Qantas Sale Amendment (Still Call Australia Home) Bill 2011*, 06 February 2012, page 28

The majority of Australia's treaties related to international air services include the phrase "substantial ownership and effective control" and section 11A was introduced into the *ANA 20* specifically to set out the foreign ownership limits announced on 22 December 1992:

> The object of the amendments in this bill is to enable the Government to ensure that any Australian carrier seeking designation or already designated on an international route can demonstrate its **compliance with bilateral requirements** that it is substantially owned and effectively controlled by Australian nationals. [emphasis added] [2]

This legislative approach was entirely consistent with the philosophy expressed by Prime Minister Hawke to the House on 08 November 1990:

> ...In order to strengthen the hand of current and future entrants into domestic aviation, and in order to provide an appropriate environment for the sale of Australian Airlines and part of Qantas Airways Ltd, the Government has decided to lift the foreign investment limits relating to investment in Australian domestic airlines by foreign airlines servicing Australia from 15 per cent to 25 per cent for an individual holding, and to 40 per cent in aggregate; and maintain a stable policy environment for aviation for the remainder of this Parliament...
>
> ...Special arrangements will apply to the part sale of Qantas. In order **to accord with our bilateral air service agreements**, the foreign investment limit in Qantas will be set at the generally accepted international benchmark of 35 per cent... [emphasis added] [3]

The significant point here is that the foreign ownership limits of both the *ANA 20* and the *QSA 92* are predicated on the common purpose of meeting our ASA and treaty obligations.

Despite that common purpose, the two Acts deal with the specifics differently. Importantly, while Qantas is subject to compliance with the *ANA 20* in general, that is not the case in regard to foreign ownership limits, as explained in the relevant Explanatory Memorandum:

> **Amendments to the Air Navigation Act 1920**
>
> Section 11A of the Air Navigation Act 1920 deals with foreign shareholdings in Australian international airlines. The principal effect of section 11A is to give the Minister power to require the articles of an Australian international airline to restrict the issue, transfer and ownership of shares in the airline so as to:
>
> prevent foreign airlines from collectively owning more than 35% of issued capital; and
>
> prevent an individual foreign airline from owning more than 25% of issued capital.
>
> The term "Australian international airline" is defined to mean an international airline that may be allowed to carry passengers or freight, or both, under a bilateral arrangement as an airline designated by Australia to operate a scheduled international air service.
>
> The effect of item 21 is to exclude Qantas from the definition of "Australian international airline". The rationale given by the Minister in the Second Reading Speech for the amendment is that:

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[2] Senator Sherry, Second Reading Speech, *Transport and Communications Legislation Amendment Bill (no. 3) 1993*, Senate Hansard, 16 December 1993, page 4761

[3] Prime Minister Hawke, *Ministerial Statement on Transport and Telecommunications Reform*, House Hansard, 08 November 1990, page 3595

> Qantas is subject to its own controls under the Sale Act, it was not intended that the Air Navigation Act measures should also apply to Qantas. However, as the wording of the Air Navigation Act is ambiguous, it will be amended to confirm that this measure does not apply to Qantas. [4]

The amendment to s11A of the *ANA 20* on 16 December 1994 made the foreign ownership limits of the two Acts mutually exclusive but entirely complementary – repeal of the foreign ownership limits of the *QSA 92* without amending s11A of the *ANA 20* to re-include Qantas would jeopardise the very ASAs upon which Qantas International depends for its business.

Why are the foreign ownership limits different?

Despite the complementary nature of the *QSA 92* and the *ANA 20*, each has evolved at a different synchronicity with the policy cycle and thus with each other.

In December 1992, the *QSA 92* at s7 limited **foreign persons** having relevant interests in shares in Qantas to a maximum of 25% individually or 35% in aggregate. Two years later, in 1994, s11A was added to the *ANA 20*, which set the **foreign airline** (not foreigners in general, as in the *QSA 92*) ownership limits for all Australian-designated international airlines at 25% for an individual holding and 35% in aggregate.

In June 1995, s7 of the *QSA 92* was amended to increase the maximum aggregate for **foreign persons** having relevant interests in shares in Qantas to **49%**, leaving the maximum holding for an individual foreign person at 25%, but introducing a new provision that limited the maximum holding in aggregate for **foreign airlines** to 35%. That *QSA 92* amendment was specifically intended to align the restrictions on the holdings of foreign airlines with those of the *ANA 20*[5] and, interestingly, "to give Qantas increased access to international equity markets, placing it in a similar situation to Ansett." [6]

Then, in May 2000, s11A of the *Air Navigation Act 1920* was amended to delete reference to **foreign airline** ownership limits, as well as the 25% and 35% limits, instead substituting limits on **foreign persons having relevant interests in shares** to a maximum of **49%**. This seminal change was explained in June 2000, when the Hon John Anderson MP, Deputy Prime Minister and Minister for Transport and Regional Services, released a Policy Statement on International Air Services which included four significant strategies:

> 1. The Government has amended the *Air Navigation Act 1920* to free up current ownership restrictions without surrendering Australian control of Australian international airlines.
> 2. The Government has amended foreign investment guidelines to allow foreign persons (including foreign airlines) to acquire up to 100 per cent of the equity of an Australian domestic airline, unless this is contrary to the national interest.
> 3. Australia's bilateral negotiating strategy will, in all cases, investigate and aim to achieve a more liberal means of designating international airlines which does not rely on ownership restrictions, but rather bases designation on place of

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4 Bills Digest Service, *Qantas Sale Amendment Bill 1994*, Department of the Parliamentary Library, 1994.

5 Explanatory Memorandum, *Qantas Sale Amendment Bill 1995*, page 1

6 *Ibid.*, page 2

incorporation, principal place of business or other evidence of commitment to providing air services from the territory of the other country.

4. The Government will seek to negotiate a more liberal universal framework for ownership and control of international airlines in the WTO.[7]

The Policy Statement went on to say:

> **Ownership and Control**
>
> The use of national ownership and control restrictions to regulate entry to the international aviation market is universally applied and one of the most restrictive elements of a highly regulated bilateral regime.
>
> It is the tool used to limit the benefits traded in bilateral air services arrangements to the parties to the arrangement.
>
> Airlines can be unilaterally barred from a route if either of the partners is not satisfied that those airlines are substantially owned and effectively controlled by citizens of the designating party.
>
> To meet these international obligations, Australian law contains statutory limits on ownership and control of our airlines. However, the Government can see no sustainable reason why all potential investors in our international airlines should not be treated equally.
>
> The Government has therefore amended the Air Navigation Act to put those statutory requirements at the limit of what our bilateral partners will accept (49% foreign ownership with no distinction between foreign airlines and other foreign investors)…[8]

Given that the previous amendment to the *QSA 92* was specifically to align with the *ANA 20*, it seems entirely logical that the *QSA 92* would again be amended to keep step with more liberalised approach to foreign ownership.

However, the Minister went on to say:

> The ownership and control provisions for Qantas are however set in a different context to other Australian international airlines, and are dealt with separately under the provisions of the *Qantas Sale Act 1992.* At the time Qantas was fully privatised in 1995, undertakings were provided to the Australian people that the *Qantas Sale Act* would ensure that Qantas would remain Australian.
>
> The Government will not change the ownership and control rules for Qantas without further and separate public consideration.[9]

There have been **no** corresponding amendments to the *QSA 92* to this day!

Fourteen years ago, the rationale for limiting foreign airline holdings (which was solely related to bilateral air service agreement requirements) disappeared. The rationale for limiting foreign ownership limits for individual shareholders, which was always amenable to be controlled through the *Foreign Acquisitions and Takeovers Act 1975*, also disappeared almost 14 years ago.

What possible justification could there be to retain those completely obsolete and irrelevant foreign airline and foreign individual limits for Qantas, but not for any other Australian international airline?

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[7] Australian Government Policy Statement, *International Air Services*, June 2000, page 9

[8] *Ibid.*, page 10

[9] *Ibid.*, page 11

AIPA strongly recommends that all Parliamentary parties and members agree to immediately amend the QSA 92 to delete paragraphs 7(1)(aa) and (b) as they no longer serve any useful purpose.

The 49% limit on Qantas

There have been many public comments about removing the 49% limit in paragraph 7(1)(a) in the *QSA 92*, which reads:

> (a) impose restrictions on the issue and ownership (including joint ownership) of shares in Qantas so as to prevent foreign persons having relevant interests in shares in Qantas that represent, in total, more than 49% of the total value of the issued share capital of Qantas;...

There have been no public comments about related amendments to the *ANA 20* and almost nothing to indicate an understanding of the context of that limit. There has been no debate about the potential consequences of a unilateral repeal of that provision.

While there is no doubt that the Parliament has the power to repeal the 49% limit in either the *QSA 93* or the *ANA 20* or, more logically and defensibly, **both**, the consequences of such a repeal are primarily extra-territorial in the first instance, as our trading partners consider the effects of our behaviour as treaty signatories. Whatever response may be forthcoming will then directly affect the Australian economy through the commercial enterprises that rely on the Government steering a steady course in international relations.

Why will there be an international reaction to a change to a national law?

There is a great deal of literature on the economic regulation of international air services and there is little doubt that the globalisation of aviation is outpacing the legacy frameworks that seek to balance the sovereign and financial interests of the stakeholders.[10] Unlike other markets, it is still true to say that international aviation is different. Issues of sovereignty, security, safety, economic benefit and political alignment have all conspired to varying degrees to continue what is generally a relatively closed protectionist market.

As part of the preceding discussion on the 25% and 35% limits, we established the aviation context of foreign ownership limits as being in partial satisfaction of the *substantial ownership and effective control* concept in international ASAs.

Auguste Hocking has this to say about Australia's current situation:

> Australian bilateral air services agreements – like those all around the world – invariably contain an airline nationality clause. Most such clauses restrict designation to airlines "substantially owned and effectively controlled" by the state of designation and/or its nationals. A key feature of the bilateral regulatory framework, ownership and control clauses work to restrict the benefit of an air services agreement to the signatory states and lock out third parties. Uncontroversial and rarely problematic in the days of the government-owned flag carrier, the requirement is now a serious obstacle to meaningful liberalisation in the commercial aviation sector.

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[10] See Lelieur, I. (2003). *Law and Policy of Substantial Ownership and Effective Control of Airlines*. Aldershot: Ashgate.

> The free flow of capital is axiomatic of globalisation. Commercial decisions can be taken with relative freedom from artificial nationality distinctions. Rationalisation along efficiency lines, accordingly, is the norm in global markets. The airline business, however, is treated differently. Ownership and control restrictions isolate the airlines and curtail the ability to access capital, consolidate across borders and establish in new markets. Prospective efficiency gains are forgone. Many suggest, on reasonable grounds, that the future health and prosperity of the industry and the broader marketplace is dependent on relaxation of these restrictions. Commercial aviation, they posit, should be treated "just like any other business".
>
> Australia considers itself at the forefront of liberalisation initiatives. It is party to 3 'open skies' agreements, one of which comprises the Single Aviation Market with New Zealand, and is presently, it is reported, negotiating a further substantive agreement with the EU. Foreign ownership restrictions for Australian airlines have been progressively reduced and, most notably, 100% foreign ownership is permitted for domestic airlines. However, like many other nations, **Australia is still bound by traditional ownership and control restrictions in many of its approximately 70 bilateral agreements**. Reform on a point has been slow and ... further action is needed. [emphasis added] [11]

In other words, the rational economic nirvana still has to negotiate a jungle of conservative international politics and the pace of progress is far from rapid. AIPA has been fortunate to have been given some limited insight into the difficulties faced by the Department in negotiating ASA reforms, which leads us to share David Duval's recent caution:

> As a result, the speed at which one State wishes to liberalise the ownership provisions it applies to its own airlines <u>is dictated ultimately by the speed at which its bilateral partners are also willing to liberalise ownership provisions for their own carriers</u>. [emphasis added] [12]

While noting that AIPA does not share Hocking's view that the recent agreements reflect an Australian policy intent rather than our partner's policy intransigence, he goes on to describe Australia's ASA dilemma:

> Another difficulty facing Australian policy is the continued application of the substantial ownership and effective control requirement in many agreements. Indeed, of the 34 post-1990 agreements reviewed for the purpose of this paper, some 23 contained the traditional ownership and control clause. It should be noted, however, that some agreements may have been amended by memorandum or diplomatic note and, under government policy, the details of such arrangements are not publically available. That aside, however, the real policy inconsistency arises in Australia's continued practice of signing new agreements with substantial ownership and effective control clauses. For instance, Australia's most recent agreements with Turkey (2010), Mexico (2010), Brazil (2010) and the United States (2008) all include a traditional ownership and control requirement. [13]

The traditional ownership and control requirements are actually a "nationality test" to assure an airline of continued access to air traffic rights. The clear modern consensus is that "substantial ownership" has been accepted in practice as meaning majority

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[11] Hocking, A. J. (2011). *Ownership and control in Australia's air services agreements: Further reform needed for genuine commercial freedom?* SSRN: available at *http://ssrn.com/abstract=1881693*, pages 4-5

[12] Duval, D.T. (2012). *The Principles of Market Access: The Aeropolitics of Ownership and Control,* Centre For Air Transport Research, The University of Otago, Dunedin, page 4

[13] Hocking, *op. cit.*, page 25

ownership[14] and, most commonly, defined as either 'at least 51% national ownership' or 'not more than 49% foreign ownership'. "Effective control" can be a more vexed assessment – there is lots of case law in the US and in Europe, but closer to home, for example, it appears that Indonesia concentrates only on majority ownership while ignoring 'effective control' yet Hong Kong's much vaunted "incorporation and principle place of business" test is actually overwhelmed by detailed examination of 'effective control'.

As Duval explains:

> ...control refers to operational oversight of a carrier, and thus the notion of "effective control" is designed to test whether, put simply, decision-making within an airline is vested with nationals of the designating State. The *ICAO Manual on the Regulation of International Air Transport* offers guidance on interpretation:
>
> > "effective control" may be exercised by different entities depending on the activity of the air carrier. For example, air carrier management may exercise effective control over certain operations, such as opening a new route, while financial entities, shareholders or a government might exercise effective control for the purpose of increasing the air carrier's capital, merging it with another air carrier or dissolving the company.
>
> The question, then, is whether an airline that is majority owned by nationals of a State but effectively controlled by non–nationals can be considered a designated carrier where both substantial ownership and effective control are required to be met. An example serves to illustrate this point. Tiger Airways Australia operates domestic services in Australia, but cannot operate trans-Tasman services because it is wholly owned by Tiger Airways Holdings in Singapore. This example does not pass the test for effective control of Australian airlines operating between New Zealand and Australia[4].
>
> > 4 New Zealand has exchanged Seventh Freedom rights with Singapore, which would permit trans–Tasman operations by a Singaporean airline without the service having to originate in Singapore. The Australia–Singapore ASA does not permit this.

AIPA cannot say with any real certainty what reaction Australia would face from the signatories to our ASAs should we remove the 49% foreign ownership restrictions from the *QSA 92*. Given the predominance of traditional ownership and control clauses in the post-1990 ASAs, it seems highly unlikely that our treaty partners will be indifferent.

Notwithstanding our limited knowledge of what other trade-related issues might prevail, we are extremely concerned that removing the 49% foreign ownership restrictions from the *QSA 92* might well <u>lead to the withdrawal or restrictions of the very traffic rights upon which the already diminished Qantas relies for its commercial viability</u>.

AIPA strongly recommends that all Parliamentary parties and members reject any proposal to unilaterally free Qantas of all foreign ownership limits until such time as the Parliament is assured that there will be no consequential effect on any international capacity allocations to Qantas.

The level playing field

AIPA has long argued for a level playing field upon which all Australian-designated international carriers can compete. Our proposals have all been non-company specific because we have a strong belief all Australian international airlines face the same market distortions and any solutions should be universally available.

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14 Lelieur, *op. cit.*, page 9; Hocking, *op. cit.*, page 9; Duval, *op. cit.*, page 2

Our focus was on international market distortions because, until recently, we viewed the domestic market to be relatively balanced. However, we have absolutely no doubt that, when the Department chose to do nothing in relation to the Virgin Australia restructure, that the domestic playing field (and its financial synergy with international operations) was sharply tilted away from Qantas.

Unfortunately, at least in the current timeframe, the Australian public has no way of knowing whether any of our treaty partners who value 'effective control' tests have queried the propriety of the corporate façade of independence that the Virgin arrangements purport to maintain. While acknowledging that it would remain in the Department's best interests to keep any adverse commentary confidential, it does raise the question as to who monitors the appropriateness of the decision to accept the corporate re-engineering as acceptable compliance with the *ANA 20*.

AIPA does not believe that it should be necessary for any aggrieved stakeholders to initiate and fund a legal challenge through the Australian Courts in order to gain some sort of independent review of the handling of this issue. AIPA has, on a number of occasions, sought Government review of the Virgin restructure. Our most recent attempt was a letter to the Treasurer late last year, which said in pertinent part:

> **The case for a Productivity Review & Parliamentary Inquiry**
>
> AIPA also strongly suggests that the Productivity Commission needs to review the 1998 International Air Services Inquiry Report and the subsequent policy levers to ensure that the Government's policy settings reflect the realities of today's markets. Right now Australian aviation is working from 15 year old policy settings – a time before 9/11, before the Bali bombing, before the collapse of Ansett, the onset of SARS and the arrival of the tax-free, State-owned airlines from the Middle East.
>
> AIPA also calls for your support for a Parliamentary inquiry into the issue of foreign ownership in Australia's aviation industry, beyond the current Qantas Sales Act 1992. This inquiry should publicly examine the Virgin restructure, the Air Navigation Act 1920 foreign ownership limits, the issue of Principle Place of Business and the national interest test for aviation that underpins the Foreign Investment Review Board advice to you.[15]

Our argument for a review of the acceptability, for the purpose of qualifying for designation as an Australian international airline in accordance with the requirements of the *ANA 20*, of the Virgin structure is twofold: first, it would confirm or otherwise whether the inaction of the Department was consistent with the intent of the Parliament in enacting the *ASA 20*; and second, it would confirm the benchmark to level the playing field between Qantas, Virgin and any other airline seeking designation as an Australian international airline.

AIPA has a longstanding view that the Department failed in its duty as the respondent agency for the *QSA 92* to properly manage the issue of the application of the *QSA 92* to subsidiary companies, in particular to Jetconnect and Jetstar, which in our view created the environment for the 'shelling out' of Qantas in favour of the subsidiaries. Indeed, in our view there appears to be nothing in the *status quo* of Departmental enforcement of the *QSA 92* to prevent Qantas from incorporating an Australian subsidiary company to conduct international operations (subject to the ANA 20 and not, in accordance with the *status quo*, the *QSA 92*) along identical lines to Virgin Australia International Holdings. Qantas Airways could then resort to being a domestic airline and an international service provider as is Virgin Australia Holdings, clearing the

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[15] AIPA, Letter to the Treasurer, 18 November 2013.

way to removing the 49% foreign ownership limit from paragraph 7(1)(a) of the *QSA 92* but only if paired with an amendment to s11A of the *ANA 20* to remove the Qantas exceptions.

Given our previous discussion about the perils of unilaterally repealing the 49% foreign ownership restrictions from the *QSA 92*, AIPA could not rationally support any legislative arrangements that created different foreign ownership limits for Qantas vis-á-vis other Australian designated international airlines.

AIPA strongly recommends that all Parliamentary parties and members agree to immediately amend the *QSA 92* to delete paragraph 7(1)(a) and the *ANA 20* to remove the Qantas exception, with the intention of imposing on Australian-designated international airlines only one set of foreign investment limits.

Greater foreign ownership of Australian-designated international airlines and the national interest

AIPA does not believe that the ASA environment is ready for the abandonment of foreign ownership limits on a broad scale. The reality is that most countries value traffic rights as a sovereign asset to be traded to maximise their national interest. AIPA believes that the circumstances that underpinned the International Aviation chapter of the Government's 2009 Aviation White Paper are largely unchanged and we support the 'pragmatic approach':

> Like many areas of international trade, international aviation is subject to a range of market distortions that advantage some airlines and disadvantage others. Continued government ownership of some international airlines, the presence of government subsidies and support, differing approaches to bankruptcy protection and divergent tax regimes create market distortions beyond the scope of bilateral air services agreements.
>
> The Australian Government will continue to take a pragmatic approach to liberalisation, based around achieving a balance between the trade, tourism and consumer benefits and the objective of maintaining a strong Australian-based aviation sector...
>
> ...Australia's negotiating priorities are designed to ensure that opportunities in both mature and emerging markets can be taken up and that capacity remains ahead of demand. Already, nearly half of Australia's international passengers travel under open skies or open capacity agreements (with the United States, United Kingdom, New Zealand and Singapore). Australia's airlines need opportunities to pursue new and growing markets, engaging strategically with key economies to expand Australia's global network and harness emerging tourism and trade markets.
>
> Australia's broader economic concerns, of which airline interests are one part, determine Australia's negotiating priorities. The Government is committed to ongoing consultation to plan our forward negotiating priorities to ensure that all the interests that go to make up the broader national interest are taken into account. [16]

AIPA is of the strong view that public utterings about waiving all foreign ownership limits are a complete nonsense. We have argued above the case for being very careful about upsetting ASAs based on 'substantial ownership and effective control' by unilateral actions rather than by negotiation. While we support the shift to 'principal place of business' and 'effective regulatory control', we need to reiterate our basic

[16] Commonwealth of Australia, 2009, *The National Aviation Policy White Paper: "Flight Path to the Future*, page 42

tenet that any and all arrangements must have strong national interest provisions to ensure 'the economic benefit stays here'.

Currently, the *QSA 92* has quite strong national interest provisions in regard to the economic benefit flowing from Qantas International operations. Of course, those people calling for the total repeal of the *QSA 92* are actually calling for the repeal of the only thing preventing the large scale off-shoring of the operational, training and maintenance activities of Qantas International. Those same people, presumably fully informed of the consequences of their demands, are offering nothing by way of replacement controls over that economic activity.

With the exception of the foreign ownership limitations in s11A, there are no requirements prescribed as conditions precedent for the grant of an International Airline Licence. The legislative structure refers to the licence being "granted by the Secretary in accordance with the regulations". The regulations refer only to the things to be included in the application and, in regard to making a decision on the application, perhaps the ultimate discretion:

> **17 Matters to be taken into account**
>
> In making a decision on the application, the Secretary may take into account:
>
> (a) anything in the application or in any other document submitted by the applicant to the Secretary; and
>
> (b) any other matter the Secretary considers relevant.[17]

In the end, we find that the alternative 'national interest' provisions, should the *QSA 92* be repealed, are set out in an entirely discretionary Departmental Guidance Note. That Guidance Note is not even a Legislative Instrument and thus is not subject to oversight by the Parliament. AIPA's main concern is the lack of precision, undoubtedly deliberate in a quest for flexibility, in the economic benefits that may have to be paid by the applicant as consideration for the commercial advantage that accrues from being granted an Australian International Airline Licence.

While we respect the economic rationalist perspective that would remove all national connections, AIPA does not agree with 'giving away the farm' in the pursuit of often theoretical economic benefits while exposing our aviation industry to what we might call the 'American poker' principle, where the end point is simply determined by the player holding the largest pile of chips.

We also respect the need for flexibility, particularly so that our approach to aviation liberalisation is not determined by the most conservative of our ASAs. However, in balance, we are not convinced that the exercise by the Department of its very wide discretions necessarily benefits all aviation stakeholders. Some greater formal prescription seems justified: first, to clarify what the continuing requirements placed on licence holder may be, and second, to fetter Departmental discretion.

AIPA proposes that any repeal of the *QSA 92* that affects the 'national interest' provisions should only be matched by a corresponding amendment to the *ASA 20* that formalises the ICAO advice on what might reasonably constitute a test of the evidence of:

> **principal place of business** may be predicated upon the following: the airline is established and incorporated in the territory of the designating party in accordance with

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[17] Commonwealth of Australia, Air Navigation Regulations 1947, regulation 17.

> relevant national laws and regulations, has a substantial amount of its operations and capital investment in physical facilities in the territory of the designating party, pays income tax, registers and bases its aircraft there, and employs a significant number of nationals in managerial, technical and operational positions. [18]

as an alternative to and eventual replacement for the 'substantial ownership and effective control' concept proxied by the existing foreign ownership limitations.

AIPA strongly recommends that all Parliamentary parties and members agree that the national interest provisions set out in s7 of the *QSA 92* should not be repealed until the *ANA 20* is amended to impose on Australian-designated international airlines one set of national interest requirements based on the ICAO guidance on 'principal place of business'.

A brief comment on who benefits from foreign capital inflows

In all of the media debate about foreign ownership and freeing up access to foreign capital, little has been said about who may be the immediate beneficiaries of the inflow of foreign capital. If a foreign buyer is permitted to purchase equity in Qantas, any on-market purchase of a parcel of the existing free float of shares will certainly get that foreign investor onto the share register and potentially eligible to participate in any future capital raising. However, the immediate beneficiaries of such a purchase are the beneficial owners of the shares, with nothing flowing to Qantas!

Qantas will only gain increased capital through equity if it issues new shares. Given the current share price, a capital raising with existing shareholders is unlikely to provide any useful increase in capital and there are considerable difficulties associated with diluting existing shareholders by introducing a new equity partner by issuing shares under a scheme of arrangement. In any event, new or increased foreign equity would be subject to examination under the *Foreign Acquisitions and Takeovers Act 1975* and the *Corporations Act 2001* as well as either the *QSA 92* or the *ANA 20*.

AIPA is concerned that there seem to be many who presume that amending the foreign ownership limits will immediately solve Qantas' thirst for capital – that is not the case. The existing shareholders may benefit but there are many steps before Qantas might reasonably access a single equity dollar from changes to the number of foreign shareholders on the register.

WHERE WE STAND

AIPA notes the widespread public commentary about amending or repealing the foreign ownership limits of the QSA 92 either specifically or by repealing the entire Act.

AIPA strongly recommends repealing the 25% and 35% foreign ownership limits as they serve no useful purpose.

AIPA reminds interested parties that the 49% foreign ownership limit placed on Qantas by the *QSA 92* is tied to the 49% foreign ownership limit placed on all other Australian-designated international airlines by the *ANA 20*. In both cases, the limit reflects the predominant 'substantial ownership and effective control' clause of our ASAs. That

[18] ICAO, 2004, *Manual on the Regulation of International Air Transport, Doc 9626*. International Civil Aviation Organisation, Montreal, page 4.4-5

'substantial ownership' clause reflects the agreed position between the signatories of the ASA and relates to any Australian-designated international airline. It is a default trigger clause if the 49% foreign ownership limit is abrogated.

AIPA reminds interested parties that a unilateral repeal of the 49% foreign ownership limit placed on Qantas by the *QSA 92* may breach many of our ASAs and the underpinning treaties and could result in the suspension or cancellation of the very traffic rights upon which Qantas depends to survive. Such a repeal would also then place Qantas in an privileged financial position and would unfairly restrict all other Australian-designated international airlines.

AIPA notes that the *ANA 20* includes an exception provision ("the Qantas exception") that ensures that the foreign ownership limits in the *ANA 20* do not apply to Qantas because of the separate but matching restrictions in the *QSA 92.* Further, we note that the *ANA 20* does not include any 'national interest' provisions such as those that apply in the *QSA 92.*

AIPA strongly recommends that the repeal of the Qantas exception in the *ANA 20* is an essential precondition to any repeal of the 49% foreign ownership limit placed on Qantas by the *QSA 92*, in order for the playing field to remain level by ensuring all Australian-designated international airlines are subject to the foreign ownership limits in the *ANA 20*.

AIPA strongly recommends that suitable national interest requirements based on the ICAO guidance on 'principal place of business' are inserted into the *ANA 20* before any consideration is given to repealing the national interest provisions of the *QSA 92.*

Nathan Safe
President
Australian & International Pilots Association

Attachment 2 to
AIPA Submission to the Senate Economics Legislation Committee 13 March 2014

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18 November 2013

The Treasurer,
The Hon Joe Hockey MP
Parliament House
PARKES, ACT 2600

Dear Treasurer,

The Future of Australian Aviation Must Include Qantas as the Flagship National Airline

The Australian and International Pilots Association (AIPA) believes that a viable Qantas International airline is a key plank of Australia's national interest. Under its current management, AIPA believes that Qantas' iconic status and even its very survival in the form that we know it is under threat.

AIPA polling shows that a majority of the public wants to see Qantas succeed so that Australia benefits from that success, especially in terms of national security. In the end, Qantas represents Australia's emergency domestic and international reach. As pro-competition as AIPA is, cheap airfares and multiple carrier choices mean nothing in times of national crisis.

We would like to meet with you at a time and location of your convenience to discuss our mutual interest in maintaining the capability of conducting international operations with one or more Australian airlines, preferably with Qantas as the flagship carrier. We must be able to rely on airlines that are committed to our national interest, not that of some other country, without resorting to the nationalisation of foreign-owned assets.

AIPA is the largest association of professional airline pilots in Australia. We represent nearly all Qantas pilots and a significant percentage of pilots flying for Qantas subsidiaries (including Jetstar Airways).

Industrially, AIPA wants to move beyond the disastrous grounding of the airline in 2011 and the subsequent collapse in trust and respect for the airline's management. We have been working with all sides of politics in developing policies, which if implemented, will go a long way to ensuring Australia's aviation sector will benefit and be able to grow and compete on a level international playing field. Those policies are not limited to Qantas.

A Viable Qantas is Vital for Australia's National Interest

An Australian international airline is pivotal to Australia's economy, infrastructure and security. The International Air Transport Association (IATA) calculates that for every dollar an airline earns there is three fold impacts on the economy. Potentially this means that Qantas' effect on the national economy is $45 billion.

Qantas employs a large, skilled, Australian-based workforce and contracts services and skills from many other Australian-based companies. Qantas also supports national security by ferrying troops, rescuing civilians from natural disasters and terrorist attacks and contracting support services to the military.

The Emirates Model – What Future for Qantas?

The rationale for Qantas' global alliance with Emirates is contained in its submission to the ACCC: They said: "For many years, Qantas International has been in terminal decline and has been supported by the other profitable Qantas businesses (Qantas Domestic, QFF and Jetstar) but its losses have continued to grow, with a $450 million loss in fiscal year 2012. The growing magnitude of the losses cannot continue." While the rhetoric for last financial year has moderated somewhat, the question that still has to be asked is: "How has this come about?"

In our view, a series of management decisions have strangled Qantas' profitability. The management strategy of using Qantas as the 'cash cow' to fund the burgeoning Jetstar franchises is unsustainable, particularly as none look even close to making an operational profit. Qantas CEO Alan Joyce's constant public inference is that Qantas International is a "basket case". AIPA is unable to see who might benefit from such a strategy - clearly it is not the shareholders!

As we mentioned, one in every two Australians [1] believe that the Government should intervene in the national interest in some way to ensure that we maintain Qantas as an Australian designated international airline – one that is pivotal to our national security. AIPA believes that any intervention should benefit all Australian international carriers, not just Qantas.

AIPA's Concerns – The "Shelling Out" of Qantas

AIPA has long-running concerns about the future of Qantas as an international airline. The common thread has been the management infatuation with the low cost carrier (LCC) model at the expense of the full service airline (FSA) and as a vehicle to circumvent the *Qantas Sale Act 1992*. AIPA has put those concerns to the Senate Rural Affairs and Transport Legislation Committee, the International Air Services Commission (IASC) and the Australian Competition and Consumer Commission (ACCC). Our previous disquiet was focused on the 'shelling out' of Qantas via its subsidiaries. These concerns have in no way been diminished in the context of the recent Emirates deal.

AIPA notes the possibility that Qantas is not, in any way, legally compelled to conduct international airline operations in its own right. We are concerned that the Emirates Master Coordination Agreement might provide the very platform for Qantas to shrink from being an 'operating carrier' to becoming predominantly a 'marketing carrier' or a virtual airline – at the cost of thousands of high skilled Australian jobs. Should that occur, Qantas might even be able to relinquish its International Air Operators Certificate altogether, but still issue tickets in its own name for international flights on Emirates.

Under that scenario, Qantas' international business could mainly consist of a call centre and associated IT facilities. AIPA is concerned about the related public detriment, both economic and non-economic, when all of the outcomes of such an airline model in the international context are considered. Critically, there will be no capacity in Australia in the foreseeable future to rebuild an airline like Qantas.

Are Low Air Fares The Most Compelling Metric of Competitive Benefit?

The most ubiquitous references to competitive success in the public arena are all about cheap airfares. However, we have made the point in the Senate and elsewhere that low airfares, at least in a headline sense, may not reflect true costs of production or may result in cost pressures on areas that have significant safety-related costs.

AIPA seeks clarification on the metrics employed by the ACCC to identify benefit and detriment in the aviation industry. In particular, we seek clarification from the regulator as to whether contributions to operational and training infrastructure, national skills development, supplementation of military assets and assistance in the projection of national reach in time of emergency are metrics considered together with the more obvious and popular metrics.

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[1] AIPA, Future of Qantas n=1000 survey June 2012

A Low Water Mark

What if Qantas is “shelled out”? For at least two employment groups, pilots and maintenance engineers, there is no ready market within Australia to absorb those skilled workers. There is a real risk that these highly trained and experienced workers may be lost overseas or from aviation altogether. The recent closure of aircraft maintenance at Avalon reinforces this risk. If that scenario was to eventuate, it would be a squandered skills investment and a wasted national resource.

The Australian Government needs to revise the current policy levers to ensure Qantas remains a viable and successful flag ship international airline.

What Should Those New Policy Levers Be?

Qantas management is right to argue that the airline faces more competitive disadvantages than many of its foreign competitors. These rapidly expanding foreign carriers enjoy foreign government support through favourable regulatory regimes, taxation relief, investment guarantees, accelerated depreciation and other incentives.

Fifty or more foreign airlines compete with Qantas, Jetstar and Virgin Australia. We believe that the situation where Australian international airlines are competing with countries that have effectively no company, transaction or personal taxation is unfair and excessively detrimental to Australia’s national interest and security.

AIPA does not propose that the Government provides support to inefficient operators. We only propose that the Government moves to provide a relatively equalised cost basis. We must get ahead of the game to avoid the need for the Government to repeat for international aviation what was required to support our ailing shipping industry.

We believe that eligible Australian operators should be provided with mechanisms that redress Government-imposed cost elements, whether that is via reduced taxation, greater offsets and deductions, accelerated depreciation or capital investment guarantees.

The case for a Productivity Review & Parliamentary Inquiry

AIPA also strongly suggests that the Productivity Commission needs to review the 1998 International Air Services Inquiry Report and the subsequent policy levers to ensure that the Government’s policy settings reflect the realities of today’s markets. Right now Australian aviation is working from 15 year old policy settings – a time before 9/11, before the Bali bombing, before the collapse of Ansett, the onset of SARS and the arrival of the tax-free, State-owned airlines from the Middle East.

AIPA also calls for your support for a Parliamentary inquiry into the issue of foreign ownership in Australia’s aviation industry, beyond the current *Qantas Sales Act 1992*. This inquiry should publicly examine the Virgin restructure, the *Air Navigation Act 1920* foreign ownership limits, the issue of Principle Place of Business and the national interest test for aviation that underpins the Foreign Investment Review Board advice to you.

Conclusion

We, more than any other stakeholder, have the airline’s best interests at heart. We appreciate how very busy you are but we would welcome a meeting with you, at a date and location of your convenience, to further discuss these important national interest issues. If you require further information, please do not hesitate to contact me

Yours sincerely,

Nathan Safe
President
Australian & International Pilots Association

AIPA PROPOSED PRODUCTIVITY COMMISSION TERMS OF REFERENCE

I, Joe Hockey, Treasurer, under Part 3 of the *Productivity Commission Act 1998*, hereby refer the Commonwealth's policy on International Air Services Agreements (ASAs), the International Air Services Commission (IASC) allocation process and foreign ownership of designated Australian international airlines to the Commission for inquiry and report within (xx) months of receipt of this reference.

Background

On the 9th of December 1997, the then Treasurer referred the matters of the Commonwealth's policy on International ASAs and the IASC allocation process to the Commission for inquiry and report. Following the inquiry, the Productivity Commission published its International Air Services Inquiry Report on the 11th of September 1998.

The Report was wide-ranging and formed the basis of Australia's international aviation policies in the years that followed. While the responsible Ministers and their Departments continuously review the policy framework in light of developments in the fast moving world of international aviation, there has not been an independent economic review of the efficacies of Australia's policies or the intended economic benefits since 1998.

In 1997, Australia had 50 air services agreements/arrangements. At the end of 2012, we had air services agreements/arrangements with 78 countries/economies. In 1997, the Australian airline industry was considered to be relatively efficient and internationally competitive, carrying around 43 per cent of the approximately 14 million passengers flown to and from Australia that year — Qantas having a 39 per cent share and Ansett International having around 4 per cent. In 2012, passenger numbers had grown to nearly 29 million while Australian airlines only carried 34.6 per cent - Qantas as the only full service carrier carried 18.1 per cent and now, according to the Board, is an international airline "in terminal decline".

Clearly, circumstances have changed considerably since the economic climate in which the International Air Services Inquiry Report was framed.

In undertaking this review, the Productivity Commission should assess the outcomes of those parts of the regulatory framework which were intended to enhance competition, or were intended to reduce costs or increase benefits to the Australian economy. Due consideration should be given to the national interest outcomes in terms of sovereign capacity in times of crisis.

Scope of Inquiry

In undertaking this review the Productivity Commission should:

a) identify the current regulatory/legislative framework in which international air services operate, including multilateral as well as bilateral structures, and the objectives of the framework

   i) in this context, identify the nature and characteristics of the commercial rights being traded, including reference to airport access as an essential prerequisite to trade in aviation services;

b) identify the relative effect on competition in the global market of the bilateral and multilateral international air services agreement frameworks;

c) identify the effect on competition in Australia's existing and potential international aviation markets of Australian policy in relation to air services agreements;

d) assess whether the International Air Services Commission (IASC) allocation process provides net benefits to Australia;

e) analyse and assess the benefits, costs and overall effects of the international aviation regulatory framework and Australia's approach to negotiating air services agreements for tourism, consumers, air freight and the aviation industry;

f) in so doing, determine whether the approach currently adopted maximises the benefits to Australia possible within the bilateral and multilateral frameworks;

g) assess the options for further liberalisation:

   i) within the context of the bilateral system (including the role that bilateral partners may play in restricting entry); and

   ii) alternatives to the bilateral system;

h) assess the options for ownership structures of Australian international airlines within the context of existing bilateral and multilateral frameworks; and

j) identify the scope and consequences (costs and benefits and overall effects) for Australia of these options.

The Commission's recommendations will be considered by the Government and its decisions will be announced as soon as possible after the receipt of the Commission's report.

Joe Hockey

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