



DEPARTMENT OF TRANSPORT AND REGIONAL SERVICES

Secretary: *J. Luff***RECEIVED****3 SEP 2002**HOUSE OF REPRESENTATIVES
STANDING COMMITTEE ON
TRANSPORT AND
REGIONAL SERVICES

Mr Ian Dundas
Committee Secretary
House of Representatives
Standing Committee on Transport and Regional Services
Parliament House
Canberra ACT 2600

Emailed 2 / 9 / 2002

Dear Mr Dundas

I refer to your letter to the Secretary, Mr Ken Matthews of 2 July 2002 concerning the Committee's inquiry into commercial regional aviation services in Australia and alternative transport links to major populated islands.

I note that the Chair, Mr Paul Neville MP, has written to the Deputy Prime Minister welcoming a submission from his department.

Attached is the department's submission to the inquiry. Relevant officers of the department are available to discuss the issues raised in the submission and to assist the Committee in its inquiry.

The submission has been coordinated across the various areas of the department. However, should other matters come to light over the period of the inquiry I will keep you informed.

We would be very happy to discuss our submission with the Committee or expand on any points of interest.

For further assistance, please contact Marilyn Bassett on 6274 7928 about regional aviation policy matters.

Roger Fisher
First Assistant Secretary
Aviation Policy Taskforce
30 August 2002

DEPARTMENT OF TRANSPORT AND REGIONAL SERVICES

SUBMISSION TO THE STANDING COMMITTEE ON TRANSPORT
AND REGIONAL SERVICES' INQUIRY INTO COMMERCIAL
REGIONAL AVIATION SERVICES IN AUSTRALIA AND
TRANSPORT LINKS TO MAJOR POPULATED ISLANDS.

AUGUST 2002

DISCLAIMER

The views contained in this Submission are those of the Department of Transport and Regional Services (DOTARS) and do not necessarily reflect the views of the Federal Government, the Minister for Transport and Regional Services or the Minister for Regional Services, Territories and Local Government.

Standing Committee on Transport and Regional Services
Inquiry into commercial regional aviation services in Australia and
transport links to major populated islands

Terms of reference

- The adequacy of commercial air services in regional and rural Australia.
- Policies and measures required to assist in the development of regional air services, including:
 - regional hub services;
 - small scale owner-operator services; and
 - the deployment of most suitable aircraft types.
- The adequacy of commercial air services to major populated islands and the adequacy of alternative sea services.
- Interconnectivity between regional air transport systems, major national air services and international services (including on-carriage, through ticketing, freight handling, timetabling and airport slotting).
- The role of all three levels of Government in supporting and assisting the development of regional air services and island transport systems.
- The role of major air transport carriers in providing regional services.

REGIONAL AVIATION

Introduction

There are currently 31 domestic Regular Public Transport air operators in Australia travelling between 172 cities and towns Australia-wide.

The range of destinations receiving air services is continually adjusting as the industry responds to long-term shifts in demand as a result of demographic and economic changes in the regions and alternate modes of transport and communications.

Aviation is an inherently volatile industry.

There is no one factor affecting the delivery of regional air services. The issues are complex and there are no easy solutions.

Economic Regulation

Constitutional responsibility for economic regulation of air services within Australia is determined by Section 51 of the Constitution in terms of responsibilities for trade. The States and self-Governing Territories are responsible for intra-state trade and the Commonwealth is responsible for interstate trade.

The Commonwealth has exclusive responsibility for regulating air safety, air traffic services and the Sydney Airport slot management scheme. The Civil Aviation Safety Authority administers safety regulation.

Aviation, like any other business in Australia is a commercial trade and is subject to the relevant laws of the Federal, State and Territory Governments.

The Commonwealth withdrew from economic regulation of domestic aviation in Australia in 1990 as it considers that excessive regulation harms more efficient operators and retards industry innovation.

State Government regulation of intra-state air services applies only to economic aspects. New South Wales, Queensland and Western Australia maintain economic regulatory regimes for intra-state air services and most jurisdictions have indicated that they are reviewing their aviation policies in the light of the events of September 2001.

Current Policy Environment

The regional aviation industry is experiencing long-term restructuring and it faces a range of challenges due to industry, economic and demographic change. The industry has demonstrated a mixed reaction in its response to changing demand at the same time as it has faced exogenous supply side factors such as currency fluctuations and fuel price changes that are largely outside of its control.

Destinations that have lost services since 2001 include *Casino, Kempsey, Cowra, Forbes, Cootamundra, Young, West Wyalong, Gunnedah, Singleton, Scone, Coonabarabran, Maitland, Deniliquin, Wollongong, Kalbarri, Useless Loop and Denham*. However, other destinations, such as Mildura, have had increased capacity provided as operators adjust services to match supply and demand.

Over the past 20 years more than 73 domestic airlines have withdrawn services, through liquidation, bankruptcy, receivership, merger or the subject of a takeover.

Since the collapse of Ansett, the Government's priority has been to manage its interests in the Ansett administration to provide transitional support for regional communities while achieving sustainable commercial outcomes for Ansett's regional subsidiaries. Flight West, Skywest, Aeropelican, Hazelton and Kendell were successfully sold and are continuing to operate routes in regional Australia. The Government's interventions in supporting operations during administration and its involvement in the sale processes were designed to achieve a managed outcome that avoided any sudden or widespread loss of services in regional Australia.

The regional aviation sector is confronted by a number of very significant challenges. These include:

- a long-term downward shift in demand as a result of demographic and economic changes in the regions;
- increased competition from other transport modes, especially roads;
- technological change as the generation of aircraft that stimulated a boom in regional aviation in the 1960's approach the end of their economic life; and
- cost pressures arising from the operation of ageing aircraft, increasing fees, charges and levies imposed by government bodies and increasing insurance costs.

While poor commercial decisions have played a part in the difficulties experienced by some regional airlines, the long-term pressures on regional aviation are beyond the control of any one regional operator. Small regional operators do not have the depth or market power to absorb large unexpected changes in their cost base. The industry is fragmented and it is only recently that the industry's peak body, the Regional Aviation Association of Australia has broadened its scope to include the long-term sustainability of the industry as a major area of focus.

It is unlikely that the regional aviation sector will return in the near future to the state that prevailed in 2001. Access to regional air services was artificially maintained prior to September 2001 by unsustainable subsidies from within Air New Zealand for the Ansett Group and by aggressive price discounting. Those conditions were not efficient or sustainable as a means of providing long-term access to regional air services.

In coming to a view about the appropriate response to this situation, the Government has considered its role and objectives and its broad goals or aims in a deregulated

market. The broad goals for the Government's aviation policies can be expressed in terms of:

- a safe, secure and sustainable aviation sector;
- price and service competition for consumers; and
- reasonable access to services for regional communities.

The regional aviation sector will continue to adjust. In particular, the Department believes that we can expect to see a gradual withdrawal of Regular Public Transport (RPT) operators from thinner routes servicing outlying communities and the consolidation of regional aviation services at a smaller number of hubs providing direct services to major population centres. Charter operators and part time 'aerial taxis' may take a greater share of traffic between outlying centres. At the same time, major operators will replace their services on thin regional routes with affiliates that fly smaller aircraft that better match demand. Access to the major airlines booking and other support systems are expected to be a significant component of these commercial alliances.

These adjustments are likely to take some time, certainly a number of years, but some form of consolidation along these lines is essential in order to secure sustainable air services in regional areas. Difficult decisions will need to be made by local communities to rationalise airports in order to allow the development of hub and spoke operations.

The Commonwealth Government is not in a position to make this happen, and it would in any case be inappropriate to attempt to direct industry or local communities about the choices they may need to make. However, there is scope for the Commonwealth to take a leadership role and provide support of various kinds as the market adjusts. For example, there could be a role for the Commonwealth in removing unnecessary barriers to adjustment and possibly in supporting communities to ease the short-term and transitional disruption that may otherwise occur.

The Minister's plan to reform land transport planning – Auslink - could create opportunities for the Commonwealth to support this process by encouraging local communities to make more strategic investment choices in transport infrastructure – for example, downgrading some airports in return for improved feeder roads to the local hub airport.

The issues confronting regional aviation are of a long-term nature. Solutions will involve concerted action over a long period by airline operators, airport owners and regional communities. There is no single, simple intervention for Government that will speed up the adjustment process. There is however a number of practical steps that can be taken to assist in the industry to achieve long term commercially sustainable services.

The Bureau of Transport and Regional Economics (BTRE) is undertaking, at the request of the Minister, a long-term study of regional public transport. This will identify the nature of the demand for regional transport services, examine governments' subsidy and regulatory arrangements to ensure that they do not discriminate against the providers of long distance passenger transport services and

assess options in developing a policy framework covering public transport services to regional areas. At the August 2002 Australian Transport Council (ATC) meeting in Auckland, New Zealand, Premiers, Chief Ministers and the Commonwealth agreed to cooperate and provide the BTRE with information necessary to support the study. The ATC will consider the first stage of the analysis at its November 2002 meeting and further analysis at its 2003 meetings. The study will provide a basis for informed decision-making on regional transport.

The Department is actively involved in assisting the development of the Government's 10 Year Plan for Tourism. Regional aviation is only one element of an overall tourism infrastructure and the Government has been keen to see the plan address the wider issues that impact on regional tourism, including the barriers to regional investment, regional tourism growth, regional transport infrastructure and training for the regional tourism sector. The Minister convened a regional tourism Round-table at Parliament House on 12 August 2002. It brought together representatives Chairs from Area Consultative Committees and significant players in regional tourism. The Round-table provided a focus for discussion to inform the development of the Green paper on the 10 year plan about opportunities and impediments to development and growth in the regions and innovative and practical solutions. The Round-table provided an important regional perspective on the issues facing regional Australia.

Area Consultative Committees (ACCs) also provide an important regional perspective on the issues facing regional Australia. The network of 56 ACCs are non-profit, community-based organisations, largely comprising business people, professionals and local representatives funded by the Commonwealth Government. The national network across Australia serves all regions. ACCs provide an important link between the Commonwealth Government and rural and metropolitan Australia. As volunteer community based organisations, ACCs are uniquely placed to respond to issues in their regions and provide a vital conduit to Government on local, social and economic conditions.

The Government has responded to the Manning Task Force report on regional aviation and agreed a number of measures, including the removal of restrictions on access to regional cities by international carriers. The Department is renegotiating international air service agreements to give effect to this measure.

In addition, there are a number of residual State, local and Commonwealth policies that may be hampering the regional aviation adjustment process. As one example, some State Governments have until very recently seen regional airline licensing as a revenue raising measure rather than as a means of recovering the costs of administration. The concept of cost recovery is supported where this helps achieve improved economic efficiency. However, the Department does not believe that charges should be applied to regional aviation where they can not be clearly demonstrated to match the actual cost of delivering services.

The Department considers that there is merit in reviewing a number of existing policies and programmes with a view to removing unnecessary burdens and barriers to adjustment for regional operators. Issues that may be examined include:

- the level and basis of regulatory fees and non-commercial charges imposed on regional operators by State, local and Commonwealth Governments to ensure that they are closely related to the actual cost of services provided, and hence contribute to improved economic efficiency;
- the compliance burden of CASA safety obligations;
- the operation of the Airport Local Ownership Programme.

While responsibility for some of these issues rests with the Commonwealth, many of them involve State and local governments. The issues are complex and in some cases there are conflicting policy objectives that are not easily resolved. The ATC provides a forum to take the issues forward. The topics may be developed by individual jurisdictions, consulting with other Governments as necessary, prior to bringing specific proposals to the ATC.

Government Support for Regional Air Services

Experience has shown that policy interventions to support particular service levels are not effective over time, and harm more efficient providers. In the long run, they delay or prevent the industry from adjusting to a more sustainable equilibrium.

State and Territory Governments are responsible for intra-state trade that covers most regional air services. They support the delivery of regional air services to a varying extent through direct subsidies, competitive regulatory regimes, business development and employment support incentives, relief from taxes, fees and charges.

After the collapse of Ansett the Government established the *Rapid Route Recovery Scheme* to provide assistance to domestic carriers to enable the restoration and maintenance of air services to regional communities affected by the collapse. That programme assisted communities to have access to services that would not otherwise be available. The programme was designed as a short term, transitional response to the sudden impact of the Ansett collapse and the programme has since expired after benefiting about 18 operators.

The Federal Government provides a range of measures designed to support the delivery of regional air services in a way that does not advantage one operator over another. These valuable measures include:

- subsidised control tower services at general aviation and regional airports;
- funding to expand aircraft maintenance engineer training in regional Australia;
- exempting regional aircraft with fewer than 16 seats from the Air Passenger Ticket Levy;
- reduced aviation fuel excise;
- quarantined regional slots at Sydney airport; and
- exempting small regional airlines and aeromedical operators from enroute navigation charges.

Assistance is provided at the community level for very remote communities that are at times isolated from essential services and supplies through the *Remote Air Services*

Subsidy Scheme (RASS). During the wet season, many of these communities are isolated from population centres and must rely totally on regular air services.

Air services subsidised under RASS reach a population of around 10,000 people in 250 remote communities. The scheme enables operators to provide a passenger service in addition to carrying mail and cargo.

The second area of assistance is perhaps less recognised but it is by far the most extensive, pervasive and more fundamental. This is the area that sets the right business environment, through such things as lower business tax rates, a dynamic economy with low interest rates and low unemployment rates. In addition, there are a raft of business and community support programs and services that are administered by Commonwealth agencies other than the Department of Transport and Regional Services that indirectly assist businesses to provide services where they are needed.

TRANSPORT LINKS TO MAJOR ISLANDS

The Commonwealth offers two schemes to assist the movement of vehicles and non-bulk freight across Bass Strait: The Bass Strait Passenger Vehicle Equalisation Scheme and the Tasmanian Freight Equalisation Scheme. Funding for these programmes is demand driven and uncapped.

Further detailed information on transport links to the major island territories is provided at Attachment A and B.

INDIAN OCEAN TERRITORIES

The Commonwealth has underwritten domestic airtservices to the IOTs since Ansett withdrew from providing a regular commercial air service in October 1997. The current agreement provides for Regular Passenger Air Services between Perth and the IOTs and involves a twice-weekly service to both Territories, with an additional service provided to Christmas Island.

An unsubsidised weekly service is currently operated between Jakarta and Christmas Island under charter by a Christmas Island businessman. Additional charter flights operate to Asia in the busier times of year (typically December to February and Chinese New Year), on an as-needed basis. A number of companies have shown an interest in providing charter services during these busier periods.

Air services to the Indian Ocean Territories are not subsidised under the Remote Air Services Subsidy (RASS) scheme since their nature and scale is different to those of mainland communities and the level of isolation and access is one step further removed. The IOTs receive irregular sea freight services from Fremantle and Singapore, but these services are effected by weather and do not cater for passengers. Air services provide the only regular passenger services to the Christmas and Cocos (Keeling) Islands communities and are important for the provision of perishable and urgent freight services.

The special Commonwealth support arrangements for the IOTs are justified by the isolation, lack of alternative reliable transport services and absence of a State government, making the Commonwealth responsible for the provision of transport services to the IOTs. While the Commonwealth seeks to minimise the level of subsidy to the operations, it retains an obligation to provide access between the islands and the mainland.

The Commonwealth also owns the Christmas Island and Cocos (Keeling) Islands Airports. A commercial operator manages these under a short-term contract. The long term management arrangements are currently being reviewed.

NORFOLK ISLAND

Both air and shipping services to Norfolk Island are provided on a commercial basis and other than its regulatory role for both aircraft and shipping the Department of Transport and Regional Services has no role in the provision of these services to Norfolk Island.

The Norfolk Island economy is largely dependent on tourism. The Commonwealth Grants Commission in its 1997 Report on Norfolk Island conservatively estimated that tourists contributed at least \$23.0 million in 1995/96 (the next biggest sector, tobacco re-exports, contributed \$2.2 million). As such any disruption to airline services (and hence tourism) has a significant impact on the Island's economy. The effects of the June 2001 demise of Flight West, which provided a regular service between the Australian mainland and Norfolk Island, were significant and while Norfolk Jet Express has increased its capacity in response to Flight West's withdrawal tourist numbers have not fully recovered.

Decreases in capacity also have an effect on the amount of airfreight, especially to the island. Mail and essential supplies, such as medicines, can be effected adversely.

Norfolk Jet Express (NJE), a locally (Norfolk Island) owned airline, provides the only regular air service between the Australian mainland and Norfolk Island. NJE provides its services using an Air Nauru 737-400 aircraft that it 'wet' leases from Air Nauru. NJE code shares its flights with Qantas. Qantas is also NJE's booking agent.

A second airline, Alliance Airlines, is due commence a regular service from 7 September 2002. Alliance Airlines has stated that it will be using Fokker 100 aircraft on the Norfolk Island route.

NJE provides 6 return services per week between the mainland and Norfolk Island. Alliance Airlines proposes to have 4 return services per week – 2 return services on Saturday and Sunday each week.

Air New Zealand provides 2 return services per week between New Zealand and Norfolk Island.

The bulk of goods to and from Norfolk Island come by ship and there are regular shipping services to Norfolk Island. Few if any tourists arrive by ship.