Inquiry into Regional Airfares in Western Australia.

Economics and Industry Standing Committee
Legislative Assembly

Submission by Shire of Shark bay
July 2017

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Executive Summary

This paper is submitted on behalf of the Shire of Shark Bay, and refers to the regulated route of Perth to Shark Bay and Carnarvon, currently serviced by Skippers Aviation.

The State Government has signed a deed agreement ("the Deed") with Skippers to provide RPT air services between Perth- Carnarvon/ Shark Bay (Monkey Mia airport) and Perth-Northern Goldfields until 1 July 2018.

Regional West Australia relies solely upon the private, for-profit aviation industry to provide the critical linkages and logistics to our regions. Our businesses, communities, and families are reliant upon these airlines to deliver services that are fairly priced, safe and efficient.

At present, the high cost of airfares and scarce connectivity between regional centres is obstructing economic prosperity and social well-being in regional WA.

The state invests hundreds of millions of dollars every year into the metropolitan transport system – the buses and trains that are essential to underpin critical linkages in and around Perth metropolitan area and outer suburbs. The state regional air transport network is equally important however government policy and regulation has failed to provide the state with a network that is efficient and affordable.

The current airline monopoly and duopoly market services across the state have been left unchecked for too long.

Going forward, State Government approach to regulation must recognise the regional air transport network as an essential service, so important to society's well-being that government must take a tough approach to regulating the services, in a similar way that power, water, and metropolitan bus and train services are regulated. Inequities such as geographic isolation, market size and distance mean that normal commercial criteria have not delivered acceptable results.

In order to move forward positively, the State must develop and apply a regulatory scheme across the state's regional air transport network which will include stringent and transparent regulation of airfares, schedules, regional linkages and service levels. In Shark Bay, this means a Regulated Monopoly will replace the current form of lassiez-faire regulation, which simply does not go far enough to protect consumers from monopolistic behaviour.

The below summarises the issues raised in this paper in response to the evaluation matters A - F listed by the Standing Committee:

Issue 1: Monopoly allows the airline to maximise profits and reduce service levels.
Issue 2: Inadequate transparency and airfare pricing controls results in high air fares.
Issue 3: Ancillary revenue is not counted. True picture of profitability is not known.
Issue 4: Minimum Deed Requirements. Relaxed service criteria in last tender and subsequent Deeds delivered an inferior product.
Issue 5: Failure to address security screening limited the market response during the last tender
Issue 6: Airline industry knowledge within government is to be improved.
Issue 7: Dismantling the Coastal Network resulted in loss of 'network effect'.

Follows are solutions proposed by Shire of Shark Bay:

Solution 1: Build more effective controls and service criteria into the next tender and Deeds – move to a true Regulated Monopoly, including;

- Open book contracting to be used in future tenders and contracts
- Airfare pricing controls to be improved, focus to be shifted to average fares and not maximum fares
- Count Ancillary Revenue in total revenue
- Re-establish historical minimum service levels in the next tender, build these into Deeds

Solution 2: Address airport infrastructure to enable a wider range of aircraft and airlines to service the route in future.
Solution 3: Understand the airline business: re-establish the Aviation Industry Observer position,
Solution 4: Build scale by re-establishing the Coastal Network.

These solutions will deliver affordable, efficient, and safe air services to and between regional centres and capital cities, to cater to all market segments in order to stimulate economic growth and improve the social well-being of our regional community.

At this point, I remain hopeful that this Standing Committee will listen and act and that the future will bring a move toward to building a better regional air network.

Yours sincerely,

Paul Anderson
Chief Executive Officer
Shire of Shark Bay

A, C and D Responses:

A. FACTORS CONTRIBUTING TO THE CURRENT HIGH COST OF REGIONAL AIRFARES;

C. IMPACT OF STATE GOVERNMENT REGULATORY PROCESSES ON THE COST AND EFFICIENCY OF REGIONAL AIR SERVICES;

D. ACTIONS THAT THE STATE AND LOCAL GOVERNMENT AUTHORITIES CAN TAKE TO LIMIT INCREASES TO AIRFARES WITHOUT UNDERMINING THE COMMERCIAL VIABILITY OF RPT SERVICES;

To avoid repetition of information, responses to the questions posed by the Committee at A, C and D have been combined. Seven key issues are identified and expanded upon below.

These issues and solutions are expanded upon in more detail in the following sections:

Issue 1: Monopoly allows the airline to maximise profits and reduce service levels

Aviation providers charge high airfares to Regional areas because they can. The State Government enables this.

On this route, a government protected monopoly is in place, with limited critical oversight and controls by DoT.

There is literally no incentive or reason for the airline to drive down the price of airfares.

Airlines, like any for-profit business, strive to maximise profit.

Airlines practice **Yield Management**. Yield management is a variable approach to pricing airline seats based on understanding, anticipating and influencing consumer behavior in order to maximise **revenue** and profits.

Until and unless Government changes their approach, this situation will remain.

The actions taken at the last State Government tender process created a monopoly and did not build adequate controls into the Deeds.

The outcome of this is unsurprising, and is as would be expected of a monopoly:

> In a monopolistic market, the monopoly has full control of the market. Since it has total market control, a monopoly sets the price and supply of a good or service. This characteristic makes it a *price maker*. A monopoly is a profit *maximizer* because it can change the supply and price of a good or service to generate a profit. It can find the level of output that maximizes its profit by determining the point at which its *marginal revenue* equals its marginal cost. A monopoly generally has one seller that controls the production and distribution of a good or service. This makes it very difficult for other firms to enter the market and creates high barriers to entry, which are obstacles that prevent a firm from entering into a market. Potential entrants are at a disadvantage because a monopoly has *first mover*'s advantage and can set prices lower to thwart a firm's entry. Since there is only one supplier and firms are not able to easily enter or exit, there are no substitutes for the goods or services. A monopoly also has absolute *product differentiation* because there are no other comparable goods or services. (Investopedia.com.)

The impact of the State Governments regulatory approach has delivered that described as above:

- High cost,
- Schedules, capacity and service designed by the airline to prioritise maximising profits over serving the public needs.

Solutions to counter this situation are to make adjustments and place more robust controls around the monopoly. These are suggested in the following sections.

Issue 2: Lack of transparency and controls results in high air fares

Solution: Open book contracting to be used in future tenders and contracts.

There is strong precedent for employing a range of open book tendering and contracting models. Such arrangements can be found commonly within the resources sector and also within the Federal Government air services contracts (see Section F, this document).

Most airlines, certainly those operating in WA, will be familiar with this concept and are likely to already have similarly structured contracts with other clients.

The resources sector and Federal Government are the major bulk buyers of air services in our nation. As such they hold extensive experience in regard to air services contracting. Tapping into their experience may be useful in drafting future Deeds, tenders and EOIs for state sole-operator Deeds.

An example of an open book model for a tender and Deed;

- The airline costs are transparent – accounts are tabled, listing all fixed and operating costs,
- Profit margin is negotiated and agreed between the airline and the customer – the State Government,
- The cost and margin then form the 'peg' for average fare targets,
- Controls are built into the Deed for CPI variations to the agreed fare, or extraordinary variations,
- Transparent reporting parameters are set, while providing profit margin protection for the airline and price gouge protection for customers.

By utilising the methods outlined in this section, monopoly routes are effectively open for competition each time they are tendered. Airlines will bid during tender time stating their proposed average fare price.

While it is of fundamental importance that the community receives value for money, particularly around pricing, it is of equal importance that the contracted airline is in a commercially sustainable situation. Open book contracts are not unusual and would serve both purposes: protect the margin of the airline therefore ensuring it is sustainable, while building controls into contracts to restrain average fare price increases.

Solution: Airfare pricing controls to be improved, focus to be shifted to average fares and not maximum fares.

Setting and controlling maximum fare, as has historically been the case, has little bearing over what the consumer actually pays at the transaction point.

Use of maximum fare as the measure that is monitored in the performance of in the Deed must be replaced by average fare.

The Deed should set a benchmark average fare as outlined above, the result of negotiation with preferred airline tenderers, and this should then be measured and monitored. The average fare set in the Deed can then be varied annually by the operator in line with CPI movements. The different fare levels and advertised fares are largely irrelevant to the actual dollar amount that on average, customers pay to use the service.

In calculating average fare: FOC tickets, industry tickets and any reduced fare staff travel or other non-commercial reduced cost travel tickets must not be included for the purposes of calculating the average fare sale price. Prize-winners travelling on FOC tickets or sponsored tickets are marketing expenses and / or the cost of providing community programs and must not be included in average fare calculations.

These tickets must be excluded when reporting the average sale price under the KPI or Route Performance Report, as they have the effect of unfairly diluting the average fare reported.

Secondly, the average fare paid by the public should be monitored, as distinct from that paid by corporate customers under contractual arrangements with the airline, as these can dilute the representation of the true cost to public of the airfare. The buying power of the resource industry or larger consumers can result in this sector taking the lion's share of the cheapest airfares while the community is left with access to only the higher yielding tickets.

To reiterate, lowest and highest published fare is not an indicator of what general public passengers are actually required to pay when purchasing airlines tickets.

Deeds that permit the Department to review average sales by fare type for 'reasonableness' (as has been in place in the past) are not appropriate. This clause is wide open for interpretation – the measure of 'reasonableness' is unclear, and one persons 'reasonableness' may not align with another's view.

By including an agreed average fare target in the Deed these matters are clear and no longer open for interpretation of the application of the clause or manipulation of fare levels inside maximum and minimums.

Importantly, the average fare target could be the result of a competitive tender and subsequent negotiation with the preferred airline tenderer. This is likely to result in a better deal for users of the services.

Significant changes in passenger numbers (upwards or downwards) will affect the overall total revenue amount achieved. Passenger numbers versus average sale price should be monitored on a continuous basis with the effect of changes to total revenue and the subsequent profit margin impact discussed, understood and addressed if necessary by permitting an increase in average fare or facilitating a reduction in average fare.

For example, a new resource project could bring an influx of new passenger business, which would then provide the opportunity to reduce the average fare while still maintaining profit margin. Conversely, an event that significantly reduces passenger traffic would require new analysis of the average fare, passenger numbers and profit margin equation.

Summary:

- Use open book contracting methods
- Set target average fare targets in the next Deeds and control it ('maximum fare' as used now as a monitoring measure is not an indication of actual fare charged).
- Link a CPI variation mechanism to average fare.

Issue 3: Ancillary revenue must be counted.

The total profit and loss picture for the airlines arising from the operation of the Deed is not accurate without the inclusion of ancillary revenue. This should identify and include revenue gathered by from:

- Car parking,
- change fees (currently $44 for an itinerary change and $66 for a name change, on bookings that will permit changes),
- freight carriage,
- excess baggage charges (currently $7.50 per kilo),
- pet carriage,
- fuel levies, if any,
- sales of merchandise, food and drink,
- credit card fees.

Summary:

Count all revenue streams as part of the profitability assessment.

Issue 4: Re-establish historical minimum service levels.

By relaxing the minimum criteria in the Deeds at the last tender round, the State Government removed access to connections with major airlines and other regional centres, frequent flyer program inclusion, and inclusion in standard airline Global Distribution Systems (GDS).

By waiving the requirement for inclusion in a GDS, State Government enabled Skippers to limit its distribution network and reduce its costs.

Resultant from this, tourism product to the area became largely invisible to travel agents without intimate knowledge of the region. This is obviously not ideal and in direct contradiction to the State Governments 2020 Tourism strategy which aims to enable WA destinations to grow their tourism sectors through industry and government partnerships

The features listed below represent the expectations of stakeholders as minimum requirements for any airline servicing the region under a government awarded license. These requirements are central to the strategy of achieving better air services for the region.

- Inclusion in a Global Distribution System and online booking systems such as wotif and webjet,
- inclusion in a mainstream Frequent Flyer program,
- relationships with domestic and international wholesalers, as well as major corporate travel agencies,
- arrangements with other airlines to facilitate through fares and cooperative activities,
- appropriately located and appointed passenger lounges,
- customer contact centre with extended opening times,
- minimal airline booking change fees that reflect the true cost of making the change,
- ability to establish monthly accounts with the airline as a form of payment,
- a waitlist service,
- a destination marketing plan to achieve route growth, developed and delivered in partnership with other stakeholders,
- commitment to a dedicated destination marketing spend that is quantified,
- employment of tourism / travel industry marketing staff within the airline.

It is worth remembering that all of these features were in place prior to the 2011 tender process undertaken by DoT. Additionally, there was no subsidy requirement at that time.

What is a GDS?

A Global Distribution System (GDS) is a software system used to enable travel agents to access live online airline seat inventory. GDS is the tool of trade that travel agents around the world use to find schedule information and book airline tickets for their customers. An airline that does not participate in GDS is largely invisible to travel agents and therefore that airline's destinations are also invisible to travel agents. CVQ and MJK currently are not in a GDS. Travel agents cannot sell tickets on Skippers Aviation flights in the usual manner. As there are many thousands of travel agents, this is simply not adequate as a replacement for inclusion in a GDS.

The basis for which DoT states GDS is 'not feasible' is unclear. Where does the figure of $1 million come from? There are many options for GDS to suit most budgets. Some airlines choose to piggy-back on larger airlines' GDS systems (such as Alliance and Air North with Qantas).

Airlines are extremely cost sensitive. If it were possible to thrive without a GDS then no airline would be investing in and participating in GDS as it would be a waste of money. Further, until 2011, airlines servicing the region did participate in GDS. There is no justification for DoT to continue providing concessions on this basic requirement.

Other airlines across the country have invested in GDS. This should be a requirement to ensure that the basic distribution infrastructure required to service the market is included in a fresh tender process.

Extract from DoT Position Papers:
The current RPT provider on the Coral Coast route, Skippers, does not use a Global Distribution System (GDS), which is generally accessed by international travel agencies and operators. The cost for implementation of such GDS system is estimated at nearly $1 million which, given the low revenue earned on the route, is not feasible.
Where possible, airlines operating on this route should have a GDS and easy passenger links to other airlines and flights operating elsewhere in Australia and internationally.

Further, DoT has chosen to use the words "*where possible*" when referring to the need for GDS and linkages with other airlines. The use of the term 'where possible' is extremely vague. How would DoT measure the level of possibility? DoT has not acknowledged the criticality to the region of future inclusion in an airline GDS and connectivity beyond Perth.

Issue 5: Failure to address airport security screening.

Airport infrastructure shortfalls in Carnarvon and Monkey Mia need to be addressed. Reluctance to invest in basic airport infrastructure and flawed security legislation must not be permitted to continue to be an eternal limiting factor to the economic prosperity of the region.

> **Extract from DoT Positon Paper:** Larger planes (over 20,000 kg) will only be able to land at Carnarvon and Monkey Mia after both airports are upgraded to accommodate for security screening operations. These works require substantial capital investment for which there is **no current economic justification**.

Further, DoT's claim is not supported by any references or studies outlining the case for rejecting security screening as economically not viable.

As advised to DoT, Gascoyne Development Commission (GDC) DC and Gascoyne Shires had been working to remove this barrier and at the time were confident that the economic case supporting the capital investment in infrastructure has been made. Further, feasible funding sources had been identified.

The State must address security screening and any infrastructure issues to enable a wider range of aircraft to service the route in future.

Issue 6: Limited knowledge of airline industry within government.

In past governments, under Alannah MacTiernan as Minister for Planning and Infrastructure (circa 2002) the State worked very closely with the aviation industry.

There was a position within Government of **Aviation Industry Observer**, reporting to Minister MacTiernan. The Observer built close relationships with airline management. As a result, there existed partnership between government and airlines, and a deep level of aviation industry knowledge and understanding within the Department of Transport. This level of knowledge does not appear to exist today in Government.

As a result, decisions on air services have been made by DoT based upon questionable assumptions.

Examples of this were provided in the document: Shire of Shark Bay Submission to Department of Transport, Reference: Review of RPT Air Routes in WA. Position Paper – for public comment, October 2014.

These are again provided below, for the information of the Standing Committee:

DoT Claim	Comment
There is no economic justification to put in security screening at Carnarvon Monkey Mia.	DoT has not qualified this statement with any economic justification study and there is no supporting analysis of any kind presented in the paper. Lack of security screening limits services to the area and reduces competition.
Airlines have little interest in the Carnarvon Monkey Mia route.	This statement did not align with comments from airlines at the time. Further, both Qantas and Virgin advised at the time that they had not been consulted with regard to the Carnarvon Monkey Mia route.
Airlines desired load factor is at least 75%.	There is no supporting analysis of any kind presented in the paper. Target seat load factor is influenced by many factors. Monopoly routes generally have a much lower break-even point. For example, Qantas recently advised that their target is 60%. See further comments below; Defining Profitability.
Carnarvon Monkey Mia is marginal / unprofitable.	DoT has not qualified this statement with any apparent economic justification study and there is no supporting analysis of any kind presented in the paper. In fact, there is evidence to support the opposite. At the time, Virgin (prev. Skywest) reported that this route was one of their best performing routes before DoT awarded the access to Skippers in 2011.
There is no economic justification for inclusion in Global Distribution System (GDS).	DoT has not qualified this statement with any apparent economic justification study and there is no supporting analysis of any kind presented in the paper. As the vast majority of airlines have invested in GDS, and it was in place prior to DoT's changes of 2011, the evidence suggests that this statement is incorrect.
GDS costs around $1 million to implement.	DoT has not qualified this statement with any references and there is no supporting analysis of any kind presented in the paper. There is a wide range of GDS providers with different options to suit different budgets. The vast majority of airlines have invested in GDS.
GDS should be a requirement 'where possible'.	The use of the term 'where possible' is extremely vague. What does it mean? How would DoT measure the level of 'possibility'?
Overall, travelers to and from Carnarvon and Monkey Mia appear to be satisfied with the quality and schedule of air services.	The survey that DoT refers to was not carried out independently of the service provider. Its results are in sharp contrast to the feedback provided by stakeholders during the December 2013 review carried out by Gascoyne Development Commission.
Industry, tourism and social needs are being met (Carnarvon and Monkey Mia).	As reported via multiple representations to DoT this statement is not supported by regional stakeholders.
Monkey Mia can only work in conjunction with Carnarvon.	There are multiple other options for Deed combinations. The statement as presented has the potential to mislead and may result in a distorted market response.
Lack of screening at Carnarvon and Monkey Mia has reduced the airfares significantly.	DoT has not qualified this statement with any references and there is no supporting analysis of any kind presented in the paper.
Demand for Carnarvon flights is unlikely to grow in the future.	DoT has not qualified this statement with any apparent economic study and there is no supporting analysis of any kind presented in the paper.

It is not difficult to see that using the DoT beliefs listed in the left-hand side of the table would deliver flawed outcomes.

<u>Understanding and Defining Profitability</u>

Importantly, the State must define 'commercial viability' and 'profitability and contain this within the Deed as a 'marker' and a peg to fare pricing. There has long been concerns raised about the marginal nature of the coastal route and its various forms. However, information on what these concerns are based on is not available. The following must be noted and incorporated into the State's thinking:

- **Define profitability.** How is the State measuring profitability and what level of profitability triggers the claim to be made that a service is not profitable or commercially viable?

- **Ancillary revenues** from car parking, excess baggage, cargo, credit card fees, reservation change fees and booking fees must also be considered in the profitability equation.

- **Profitability requirements will vary from airline to airline.** A long-term government contract offers very valuable cash flow and this can be taken to the bank to leverage building of the business in other areas. DoT must understand and appreciate the commercial value of the Deed, estimated at around $40 million over a five-year agreement.

- **Weighing profitability requires a network approach.** Monkey Mia and Carnarvon are not serviced as a stand-alone contract. What is the **net result** from the network combination of all routes awarded under DoT control? . How much overhead cost is applied to these routes, is it reasonable?

- DoT has claimed in the past that 75% seat load factor is required to be profitable. The seat load factor as a measure of profitability varies from airline to airline and from route to route. It is influenced by type, size and value of aircraft, average fare, ancillary revenue, number of passengers, frequency of schedule, portion of fixed cost base allocated to the route and operating costs specific to the route Monopoly routes generally have a much lower break-even point.

The revenue value of a five-year monopoly licence to service Shark Bay and Carnarvon is somewhere in the region of $40 million coming to the airline. This is significant, and the State must recognise the commercial value of this opportunity by shifting the belief and narrative that there is no value or profitability in the Deed.

Issue 7: Dismantling the Coastal Network resulted in loss of 'network effect'

It does not make economic sense to pair two of the state's thinnest routes – Carnarvon and Monkey Mia – together, and then separate them from the rest of the state network.

It makes far greater sense to leverage and use the access rights to stronger routes by pairing them together, and thus bolster airline interest in a total network delivery.

The destinations need not be geographically located close by as the connection is a contractual one only exercised via Deed.

This is the network approach historically proven and necessary to ensure government meets its obligations to provide adequate services to remote and marginal areas of the state.

There are many possibilities of route combinations and past government policy was strongly against allowing airlines to just service the most robust routes ('cherry picking').

In 2002 / 2003, (then) Minister for Planning and Infrastructure Alannah MacTiernan undertook a review of intrastate air services. This review was sparked by the Ansett collapse, which left some regions at risk of losing their air services.

Minister MacTiernan was firm in her assessment that a network approach was essential, and that cherry-picking by airlines of the most attractive routes would create high prices and sub-optimal services.

As a result, the states less robust routes were divided into networks. Shark Bay was included in the Coastal Network, which comprised:

Coastal Network pre-2011: Perth to Albany, Carnarvon, Esperance, Exmouth (Learmonth), Geraldton, Kalbarri and Shark Bay.

This approach was also supported by the experts at the Centre for Asia Pacific Aviation (CAPA), working in conjunction with Tourism Futures Australia, who said in their commissioned report to WA State Government:

> Extract from Report: Airlines typically operate a network of routes. Only some of these routes will be profitable on a fully costed basis. However once these routes have been served it is in the interests of the airline owner to use spare capacity on routes that can at least cover marginal costs. This results in the well-known cross subsidy across routes. It is important to recognise that this type of cross subsidy is commercially sensible. It is not akin to a community service obligation. Cross subsidisation across routes is a common practice amongst airlines including those operating RPT services in WA. Such practices obviously benefit passengers on the subsidised routes. However, they also benefit routes that provide returns to facilitate the subsidy because overall aircraft utilisation is higher, overheads are distributed more widely and the overall profitability and sustainability of airline operations are increased. Reference: Review and Assessment of the Effectiveness of Air Services in Western Australia, Technical Report, For Department for Planning and Infrastructure November 2002.

The change of government invoked a change of philosophy and a move away from this network approach. The Coastal Network was largely dismantled from around 2011 and now operates as it does today, with Skippers, REX and Qantas providing services to parts the original network, and Shark Bay being serviced with Carnarvon by Skippers.

Today, the former Coastal Network comprises:

- Carnarvon and Shark Bay- served by Skippers
- Kalbarri – nil services
- Esperance and Albany – served by REX
- Exmouth – served by Qantas under monopoly
- Geraldton – reduced regional connections, served by Virgin and Qantas from Perth under duopoly.

The network philosophy recognises that economy of scale can deliver benefits to the consumer. It is understood that the philosophy above prioritises the aim to work toward achieving a 'free market'. However, arguably, that approach also results in undermining the so called 'commercial viability' achieved by the network approach.

Solution: leverage and use the access rights to stronger routes by combining them together as a network, and thus bolster airline interest in a total network delivery. There is no reason why this could not include presently un-regulated duopoly routes such as Karratha, Port Hedland, Kalgoorlie and Broome.

B. IMPACTS THAT HIGH-COST REGIONAL AIRFARES HAVE ON REGIONAL CENTRES- FROM A BUSINESS, TOURISM AND SOCIAL PERSPECTIVE;

On the Carnarvon and Shark Bay route, a government backed monopoly is in place and stakeholders report, with minimal exception, that:

- Services are not affordable,
- the needs of the tourism industry and business sector are not being met and this is obstructing economic development,
- due to high cost, social needs are not being met resulting in inability to visit friends and relatives,
- due to scarce regional linkages, needs for school and medical travel are not being met,
- future planning has not been adequately undertaken; in particular the state of the Carnarvon airport is a serious and urgent issue.

The Gascoyne Regional Development Plan (2010-2020) was designed by the four participating Shires to provide a strategic direction for the region up to 2020. This Plan documents 19 Desired Outcomes for the region. The ability to access safe, affordable, efficient, and effective aviation services is fundamental to achieving these desired outcomes. Without one, the other is unlikely to be readily achieved.

There is no question that air services are a driving factor underpinning successful outcomes in (at least) the areas of:

- tourism,
- health,
- education,
- industry,
- community.

Without access to safe, affordable and efficient air services; social and economic outcomes will be less than optimal. The drivers for these are listed below.

Tourism and Business

Business: The high cost of air travel is a deterrent to investing in business growth. The high cost of airline booking change fees does not recognise the nature of business travel. There is also a lack of booking options via corporate travel agents and lack of connectivity with other airlines. These are elements that add to the challenge of carrying out business regionally.

The needs of industry closely mirror many of the needs of the tourism industry. Ideally, air services will offer:

- inclusion in a Global Distribution System and online booking systems such as wotif and webjet,
- inclusion in a mainstream Frequent Flyer program,
- relationships with domestic and international wholesalers, as well as major corporate travel agencies,
- arrangements with other airlines to facilitate through fares and cooperative activities,

- appropriately located and appointed passenger lounges,
- customer contact centre with extended opening times,
- minimal airline booking change fees that reflect the true cost of making the change,
- ability to establish monthly accounts with the airline as a form of payment,
- a waitlist service.

Tourism: Air services must further enhance the international reputation of the Gascoyne region as an attractive tourism destination, enabling the region to achieve tourism growth in line with state-wide expectations.

Additional to the items listed above, the following is required by the airline to support tourism industry development:

- a destination marketing plan to achieve route growth, developed and delivered in partnership with other stakeholders,
- commitment to a dedicated destination marketing spend that is quantified,
- employment of tourism / travel industry marketing staff within the airline.

Health and Schooling

At the time of the last review, the Gascoyne region was serviced by the WA Country Health Service, under the Midwest Gascoyne Region division. Perth and Geraldton provide visiting specialist services throughout the region, while people in need of specialised medical care travel to Geraldton to receive treatment under the PATS scheme.

Also, there were 51 students living in the Gascoyne and attending residential colleges in Geraldton.

The Geraldton link therefore provided an important service to these groups of regular travellers.

Historically, there were up to four flights per week between Shark Bay / Carnarvon and Geraldton. This has been reducing steadily under the Skippers Deed since 2013, and now this important regional connection no longer exists.

During the DoT community consultation in 2013, there was no apparent acknowledgment by DoT of the importance of the links to Geraldton from the Gascoyne as a regional centre, despite representations made by stakeholders.

Community

Travel by air for the purposes of visiting friends and relatives (VFR) in the Gascoyne, and vice versa, is beyond the reach of the budgets of most. This has obvious impact on the desirability of living in regional WA.

E. ACTIONS THAT AIRLINES CAN TAKE TO LIMIT INCREASES TO AIRFARES WITHOUT UNDERMINING THE COMMERCIAL VIABILITY OF RPT SERVICES; AND

The study of economics, experience, and history all tell us that in a monopoly, prices rise. Similarly, while not strictly the scope of this paper (although relevant), a duopoly such as that seen on the Broome route between Virgin and Qantas will produce the same results. There should therefore be no surprise to Government that airfares are high across the state.

Until and unless Government changes their approach to regulation of the state airline network, this situation will remain.

Airlines, like most for-profit businesses, are interested in maximising profitability. Without adequate contract mechanisms to control pricing, it is highly unlikely that this will change.

There is simply no incentive for a monopoly holder such as Skippers to reduce prices. At the same time, there is every reason to monopolise the opportunity to the extent possible.

Please refer to earlier sections of this document to review actions that can be taken by the State Government to limit airfare increases without undermining commercial viability.

F. RECENT ACTIONS TAKEN BY OTHER AUSTRALIAN GOVERNMENTS TO LIMIT REGIONAL RPT AIRFARE INCREASES.

F.1 Christmas, Cocos and Norfolk Islands

Examples to be studied are the air routes between mainland Australia and to Christmas Island, Cocos Island and Norfolk Island. Each of these destinations is remotely located and has a small population, heavily reliant upon their air services to meet business, tourism and community needs.

These routes are managed by the Federal Government Department of Infrastructure and Regional Development. The exact terms of contracts are not available publicly, however, it is understood that a safety net subsidy is provided, such that if the airline does not receive an agreed revenue amount over a period of time, a top up subsidy is paid to the airline in order to ensure ongoing viability. Therefore, books are open, numbers are transparent and margin is agreed between the parties.

Resources Industry

Secondly, the government can look to private sector for examples of contracting air services. Resources industry in particular uses mechanisms that provide transparency and accountability. Companies including Rio Tinto, BHP and Woodside, for example, commonly use open book contracting and fixed price airfare contracting to purchase their air services.

Summary Conclusion

Stated very simply, the current situation of high airfares across regional Western Australia is the obvious result of monopoly and duopoly behaviours, which is enabled by the State's approach to regulation.

Without taking action to control airline behaviour, this situation is highly unlikely to change.

This paper outlines several strategies to deliver a better result for regional Western Australia. All of these are feasible and should not be considered to be outside the realm of possibility.

Going forward, State Government approach to regulation must recognise the regional air transport network as an essential service, so important to society's well-being that government must take a tough approach to regulating the services. This could reflect the way that the state's power, water, and metropolitan bus and train services are regulated. Inequities such as geographic isolation, market size and distance mean that normal commercial criteria will not delivered acceptable results.

On behalf of the community and the Shire of Shark Bay, I remain hopeful that we can work together towards a positive future arrangement for accessibility to our region.

Reference Documents

Department of Transport Position Paper on the Review of Regulated Public Transport Air Routes in Western Australia October 2014,

Shire of Shark Bay Submission to Department of Transport. Reference: Review of Regulated Regular Public Transport Air Routes in Western Australia. Position Paper – for public comment, October 2014

Department Transport Draft Aviation Strategy December 2013

Gascoyne Regional Development Plan 2010 - 2020

Centre for Asia Pacific Aviation; Review and Assessment of the Effectiveness of Air Services in Western Australia, Technical Report, For Department for Planning and Infrastructure November 2002

Shire of Shark Bay
Submission to Department of Transport

Reference: Review of Regulated Regular Public Transport Air Routes in Western Australia. Position Paper – for public comment.

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1. Acronyms, Abbreviations and Notes

DoT	Department of Transport
EOI	Expression of Interest
GDC	Gascoyne Development Commission
GDS	Global Distribution System
IATA	International Air Transport Association
CAPA	Centre for Asia Pacific Aviation
KPI	Key Performance Indicator
RPT	Regular Public Transport
SME	Small Medium Enterprise
TFI	Tourism Futures International
UNESCO	United Nations Education Scientific and Cultural Organisation

Notes

1. Shark Bay is the preferred name for use when referring to the region. Monkey Mia is the IATA name used for the airport that services the Shark Bay region, which incorporates the town of Denham and location of Monkey Mia, however the official name of the airport is Shark Bay.

2. TFI/CAPA Report means the document titled Review and Assessment of the Effectiveness of Air Services in Western Australia **-** Technical Report for Department for Planning and Infrastructure**,** November 2002 prepared by Tourism Futures International and the Centre for Asia Pacific Aviation.

2. Overview

The Shire of Shark Bay supports the two submissions made by the Gascoyne Development Commission (GDC) to the Department of Transport (DoT). These submissions are responses to the DoT Position Paper on the Review of Regulated Public Transport Air Routes in Western Australia October 2014, and the DoT Draft Aviation Strategy December 2013.

This paper supplements the GDC submissions. It has been prepared by the Shark Bay Shire to bring focus to specific issues facing Shark Bay (see Note 1) in particular the criticality of the tourism industry to the region.

The December 2013 GDC submission was prepared following extensive stakeholder consultation across the region, including Shark Bay. It provides an accurate viewpoint of the region. The claim by DoT that services are meeting industry, tourism and community needs is rejected as it is an inaccurate representation of the current situation.

The Skippers Aviation operating model does not adequately address the needs of many market segments of the region. It is reasonable to conclude that this relates to the failure of the previous tender process to adequately ascertain and weight criteria identified by the Shark Bay community as essential. There has been an erosion of service standards and ancillary outputs, including tourism marketing, subsequent to the 2011 change of aviation companies.

In Shark Bay, people are paying much higher service prices than the state average despite the service being under contractual management by the state government.

Stakeholders are in strong agreement that the outcome of the 2011 review, resulting in the replacement of Virgin / Skywest with Skippers Aviation in Carnarvon and Shark Bay, has been detrimental to the economic prosperity of the region. The limitations of the service are not meeting tourism, industry or the social needs of the community.

In sharp contrast to DoT’s claim, Shark Bay stakeholders report consistently that:

- services are not affordable
- the needs of the tourism, industry and business sectors are not being met and this is obstructing economic development
- due to high cost, social / human needs are not being met, this includes inability to visit friends and relatives
- due to scarce regional linkages, student and medical travel requirements are not being met

It is a primary issue for Shark Bay stakeholders that these needs have not been met since the 2011 DoT tender process replacing Skywest with Skippers Aviation. There is an expectation that DoT will address these shortcomings following this review.

3. Significance of the Tourism Industry

There is a widely-held view amongst key Shark Bay stakeholders that at the eleventh hour the needs of the tourism industry were (as put succinctly by one stakeholder) *“completely divorced from the last tender process”.*

The requirements of the tourism industry in Shark Bay must underpin any tender process. Tourism must be recognised by DoT as a critical driver in the selection of an air service provider to Shark Bay. The needs of the tourism industry closely mirror those of small and medium enterprises (SMEs). Many SMEs in the region are indeed in the tourism industry, whether directly or indirectly. The President of the Shark Bay Tourism and Business Association reports that "***100% of businesses in the Shark Bay area are in the tourism industry. Their success or failure is intrinsically linked to tourism dollars".*** Tourism is the largest revenue earner of all industry sectors in the Gascoyne Region, generating an average turnover of around $200 million per annum,
(GDC website http://www.gdc.wa.gov.au).

With the current route access licence Deeds between DoT and airlines due to expire in February 2016 the economic future of the Gascoyne region is now resting in the hands of DoT.

The Australian National Landscapes status and recent World Heritage listing of Ningaloo Coast alongside the listing of the Shark Bay area now means that the Gascoyne has two World Heritage listed areas as well as the world's largest monocline at Mt Augustus and also the Kennedy Range. These substantial world class tourism attractions represent great opportunities for the region to develop and grow tourism markets (see section 4 for more information on World Heritage listing and National Landscapes inclusion).

Tourism generates jobs and wealth and this is especially important in regional areas such as Shark Bay where alternative economic stimulation opportunities are often limited.

The importance of grasping opportunities to develop tourism markets in the region must not be understated. For the Shark Bay Shire, the Skippers decision resulted in reduced promotion and marketing of tourism. This negatively affects current and future growth and prosperity of the local community.

Specific concerns associated with the current contract arrangement are:

- The Skippers terminal being located several kilometres from T2 and T3 at Perth Domestic airport and the additional cost of taxi fares to depart from or arrive at the facility.
- The shuttle bus from the domestic/international terminals does not go to the Skippers terminal, only as far at the long-term car parks which are not within easy walking distance.
- Small aircraft sizes result in limited freight and baggage capacity with restricted air freight being carried.
- Shark Bay has had to negotiate with Skippers to schedule flights for children returning from boarding school in Geraldton to allow them to fly home/return for school holidays.
- Airfares are very expensive at around $1,000 return to Perth from Shark Bay.
- Limited discounted seats are available.
- There is no Frequent Flyer loyalty program available.
- High costs inhibit patronage and have significantly contributed to the decline in passenger numbers since the introduction of Skippers to the route.
- A substantial number of Shark Bay residents are driving to Geraldton and flying to their destinations. (This is also the situation with Carnarvon residents, who drive to Exmouth to fly elsewhere). There is a flow on effect for the Shark Bay economy which is impacted by this practice when shopping and other services are accessed out of town.

- A Global Distribution System is not available with Skippers, therefore international visitors are not aware of flights to Shark Bay, as the airline is not visible to international agents (unless they are aware of Discover West which is unlikely). This is also the case for visitors from the East Coast of Australia who book through a travel agent.
- There are no baggage transfer agreements for on-going flights.
- Skippers Aviation has no marketing/tourism profile, marketing department or budget for tourism.
- There are minimal passenger amenities and services at the terminal, such as food and drinks, etc.
- There is no connectivity between Shark Bay and other tourist destinations in WA. Shark Bay is a stand-alone, isolated destination separated from vital linkages to other tourism ports.

Frustratingly, **all of these service features were in place** prior to the 2011 change made by DoT to install Skippers in place of Skywest.

4. National Landscapes and World Heritage

(See also Appendix- copy of Submission to DoT by Chair of the Ningaloo Shark Bay National Landscapes Committee)

The National Landscapes program is a high profile, federal tourism initiative. The program is the result of a partnership between conservation and tourism interests, being driven by Parks Australia and Tourism Australia. The aim of the program is to:

- promote Australia's world class, high quality visitor experiences
- increase the value of tourism to regional economies
- enhance the role of protected areas in those economies, and
- build support for protecting our natural and cultural assets.

The National Landscape sites are capped at sixteen across Australia. There are strict selection criteria – only destinations that have truly extraordinary attributes and/or a unique point of difference are accepted.

The Gascoyne Region contains one of these iconic Australian National Landscapes sites - Ningaloo to Shark Bay. Shark Bay and Ningaloo Coast are also internationally listed World Heritage areas. The United Nations Educational, Scientific and Cultural Organization's (UNESCO) charter is to *'…encourage the identification, protection and preservation of cultural and natural heritage around the world considered to be of outstanding value to humanity.'* The recognition of Shark Bay and Ningaloo Coast as World Heritage sites places them on an elite list of locations across the world which also includes the wilds of East Africa's Serengeti, the Pyramids of Egypt, the Great Barrier Reef, the Galapagos Islands and the Grand Canyon. http://whc.unesco.org/en/about/

Research conducted by Tourism Australia indicates that at least a third of visitors to Australia prefer to visit natural World Heritage areas to other areas in Australia, and that two out of three people are more likely to visit a national park if it is also World Heritage listed. Parks Australia and Tourism Australia market and promote National Landscapes sites at trade events and in promotional activities including Australian Tourism Exchange, Best of Australia booths, exhibitions, appointments with buyers from key markets around the world and industry, stakeholder engagement, websites, social media, etc.

The formal international and domestic recognition of the significance of these sites represents a considerable opportunity for the Gascoyne to secure a larger share of the international visitation market while also increasing its domestic tourism visitation.

The Ningaloo-Shark Bay National Landscape Committee has recently completed an ‘Experience Development Strategy’. The strategy has identified facilities, services, and infrastructure required to connect with the target market and support the delivery of a world-class visitor experience.

Critical issues for Shark Bay’s strategic plan to leverage the World Heritage and National Landscape status include:

- Ability to package visitation between the two Gascoyne World Heritage areas of Shark Bay and Ningaloo Coast (Exmouth)
- Ability to fly between Shark Bay and Exmouth
- Affordable airfares, tours and package deals with airlines which are accessible by travel agents around Australia and the world via GDS.

Currently, none of these basic features – enablers of success - are in place to support Shark Bay in developing and leveraging its World Heritage and National Landscape status. The absence of these features means that the opportunity is not maximised and tourism businesses miss out. The flow-on effect of this missed opportunity is experienced across the region and is significant.

Additionally, the GDC recently completed the Gascoyne Tourism Strategy. Air access to the Gascoyne Region is listed as a limiting factor to tourism expansion and increasing visitation to the area: ‘*airfares can be prohibitive to promoting leisure travel as airlines strive to maximise yields. Skippers do not have a dedicated wholesale arm as part of its overall operations… Therefore, they do not have a comparable global tourism brand and distribution network/system. This is a critical issue for Carnarvon and Monkey Mia.’*

In summary, the Shire of Shark Bay has an expectation that in moving forward DoT will take action and recognise the importance of addressing the needs of the tourism industry of the region.

5. The 2016 Dirk Hartog Commemorations

Further cementing Shark Bay’s tourism significance is the coming Dirk Hartog Commemorations.

In October 2016 it will be 400 years since Dutch Captain Dirk Hartog arrived at Cape Inscription near Shark Bay. He left an inscripted pewter plate on a post at the Cape to mark his landing, the first recorded European contact with Australia. This internationally significant event is drawing a great deal of interest both in Australia and in the Netherlands. The Dutch Ambassador to Australia has recently visited Shark Bay. The Department of Premier and Cabinet has despatched invitations to Dutch royalty and dignitaries.

Following recommendations from the Premier’s Department, the organising committee is planning a range of commemorative events and activities. This is supported by contracted event managers, Project3 - who are currently organising the high profile Albany ANZAC celebration.

To achieve success with the event, there is a clear need for alignment of tourism service providers with the goals of the organising committee. Tourism focussed airline services that are readily available for sale by travel agents via GDS around the world is a critical factor underpinning the success of the event.

The airline services must offer through fares and connections with other domestic and international airlines, as well as the ability to be packaged with land content at a range of stopover points between Europe and Shark Bay. Currently, the services offered by Skippers do not align with these requirements. Shark Bay Shire has an expectation that DoT will address these matters in the post-2016 tender process.

6. Minimum Service Requirements

The features listed below represent the expectations of stakeholders as **minimum requirements** for any airline servicing the region under a government awarded licence.

- New criteria for Deeds and improved methods of Deed management.
- Flight schedules with frequency, linkages and timing that meet the social and economic needs of the community.
- Aircraft of a typical regional airline standard. (This excludes Metroliner type aircraft.)
- Affordable airfares – benchmarked to state average.
- Participation in an industry standard airline distribution system (GDS).
- Destination marketing program.
- Connectivity with other domestic and international airlines.
- Frequent flyer program.
- Passenger lounges and facilities at main airport.
- Customer contact center with extended operating hours.

DoT is reminded that **all of these features** were in place prior to the 2011 tender process which resulted in DoT replacing Skywest with Skippers. Further, there was no subsidy requirement.

7. Continual Erosion of Services

Shark Bay received a lesser air service as a result of the outcomes of the 2011 tender process and has since suffered economic loss as a result.

Industry experts have used the terms '***downward spiral'*** and '***cancer'*** to describe the impact of the 2011 decision on the Carnarvon and Shark Bay routes.

Stakeholders and industry experts predicted this decline in growth. Strong representations were made to DoT before, during and after the 2011 process which resulted in DoT installing Skippers on the route.

The recent decision by DoT to allow a further downgrade to some of the summer services to Carnarvon by permitting Skippers to use Metroliner aircraft on the route is alarming and will result in a continuation of the 'downward spiral' and spreading of the 'cancer'. Shark Bay Shire is very concerned that this downgrade may herald the start of further entrenched reductions to service levels that will flow on to negatively affect Shark Bay.

DoT is reminded that this experiment has been undertaken previously with disastrous results.

- On 15 January 2004 Skippers took over from Skywest and commenced Shark Bay services using 19 seat Metroliner type aircraft under government awarded Deed.
- On 1 January 2006 the Deed was returned to Skywest.

Anecdotally the results are reported as follows:

- There were no toilets on the Metroliner aircraft, and there were reports of passengers urinating in eskies mid-flight. Note: Apparently most (but not all) of the Metroliners in the Skippers fleet have since had toilets installed. However, the aircraft were not manufactured with toilets installed and a standard retrofit generally results in one seat in the passenger cabin being converted to a toilet and a curtain being hung around it. This offers little privacy and is most inappropriate for a commercial service and is not in accord with the State Government's proposed vision "to establish a world-class aviation network that promotes WA's economic and social development." (DoT Position Paper, page 14). Has DoT inspected the aircraft to be used on the route?

- A 10 kilo bag limit was in place and this was useless for most passengers, particularly international passengers who often arrive with 20 - 30 kilos. At the time that Skippers took over there was a decent flow of Europeans to Shark Bay as Skywest had an office in Italy and invested heavily in destination marketing. This dropped off quickly. Offloaded bags were often sent up by road or on alternative flights.

- No GDS, as is still the case and is still a problem – Shark Bay eventually dropped off the map.

- International tourists arriving Perth on major airlines to transfer to Shark Bay being shocked and frightened at the size of the aircraft and refusing to board the Metroliner.

It was fairly quickly seen that the experiment was not a success, and the route reverted to Skywest at the first opportunity to do so.

The challenge now is to reverse the trend by returning to pre-2011 minimum requirements. These have been described fully in previous submissions to DoT and are again summarised below.

8. DoT Position Paper

In the absence of supporting information and explanatory notes, Shire of Shark Bay has grave concerns that it if taken at face value, the following assertions as included in the Position Paper, have the potential to distort the market response in a competitive tender process. DoT has reported in the Position Paper (Route by Route Analysis, Pages 43 to 49), that:

1. *There is no economic justification to put in security screening at Shark Bay.*
2. *Airlines have little interest in the Coral Coast route.*
3. *Airlines desired load factor is at least 75%. Shark Bay is marginal / unprofitable.*
4. *There is no economic justification for GDS / GDS costs around $1 million to implement. / GDS should be a requirement 'where possible'.*
5. *Overall, travellers to and from the region appear to be satisfied with the quality and schedule of air services. Industry, tourism and social needs are being met.*
6. *Shark Bay can only work in conjunction with Carnarvon.*

7. *Lack of screening has reduced the airfares significantly.*

To again reinforce Shark Bay Shire's view, these proclamations generate serious concern due to their potential to influence decision makers whilst having no strong foundation or basis for making the claim. These issues have every possibility of distorting an approach to the airline market and therefore could have the effect of reducing competition in a tender or EOI process.

DoT has not qualified these statements with any evident study or research. There are no references provided in support of these claims. The concerns with this list of issues identified by Shark Bay Shire are reported more fully below. Please also refer to the October 2014 GDC submission for further information on these serious concerns.

- *<u>There is no economic justification to put in security screening at Shark Bay (DoT Position Paper Page 49)</u>*

Reluctance to invest in basic airport infrastructure, coupled with flawed security legislation (the 20 tonne rule), must not be permitted to continue as an eternal limiting factor to the economic prosperity of the region. The statement posed by DoT is also not supported by any references or studies outlining the case for rejecting security screening as economically unviable.

As advised to DoT, Shire of Shark Bay has been working with GDC to remove this barrier and is confident that the economic case supporting the capital investment in infrastructure has been made.

DoT must not continue to present lack of security screening infrastructure as a closed issue and an immovable barrier to change in parts of the state. This is potentially misleading to any airline that might be considering entry to this route. DoT should work with regional bodies including Shire of Shark Bay and GDC toward removing this barrier.

- *<u>Airlines have little interest in the Coral Coast Route (DoT Position Paper Page 49)</u>*

Shire of Shark Bay understands from the GDC that as recently as mid-September 2014, airlines had not yet been canvassed for their views on servicing this route. All airlines operating in Western Australia, or with the potential to operate in the state, including Qantas, Virgin, Skippers, Air North, Alliance and REX (all airlines with full GDS capability and connectivity to other airlines) must be consulted before a conclusion can be drawn as to their level of interest.

- *<u>Airlines desired load factor is at least 75%. Shark Bay is marginal / unprofitable. (DoT Position Paper Pages 44 and 49)</u>*

DoT has not qualified this assertion with any study, research, reference or report. Regardless, the level of profitability of the route as a stand-alone commercial prospect should not be the key factor of consideration when addressing the future of air services to the area. Of relevance is the fact that Shark Bay can and should form an integral and valuable part of the state's regional aviation network. This concept is explained more fully by the report of the Centre for Asia Pacific Aviation (CAPA), Review and Assessment of the Effectiveness of Air Services in Western Australia - Technical Report for Department for Planning and Infrastructure, November 2002:

'Airlines typically operate a network of routes. Only some of these routes will be profitable on a fully costed basis. However once these routes have been served it is in the interests of the airline owner to use spare capacity on routes that can at least cover marginal costs. This results in the well-known cross subsidy across routes. It is important to recognise that this type of cross subsidy is commercially sensible. It is not akin to a community service obligation. Cross subsidisation across routes is a common practice amongst airlines including those operating RPT services in WA. Such practices obviously benefit passengers on the subsidised routes. However, they also benefit routes that provide returns to facilitate the subsidy because overall aircraft utilisation is higher, overheads are distributed more widely and the overall profitability and sustainability of airline operations are increased.'

In summary, DoT must consider Shark Bay as just one part of a state-wide network that utilises cross-subsidy to ensure that more marginal areas receive adequate air services. The stand-alone level of commercial profitability of the route is not relevant.

- *There is no economic justification for GDS / GDS costs around $1 million to implement. / GDS should be a requirement 'where possible'. (DoT Position Paper Pages 45 and 49)*

Airlines are extremely cost sensitive. If it were possible to thrive without a GDS then no airline would be investing in and participating in GDS as it would be a waste of money. Further, until 2011, airlines servicing the region **did** participate in GDS. There is no justification for DoT to continue providing Skippers with concessions on this basic requirement. This is a particularly critical factor on a tourism route such as Shark Bay.

Other airlines across the country have invested in GDS. Any airline that is unwilling to invest in the basic distribution infrastructure required to service the market should be excluded from a fresh tender process. From the CAPA report:

*'Listing in global computer reservations systems and 'through fares' are important to tourism marketing. If two carriers compete on a route with similar aircraft and fares, the ability of one airline to link to the airline networks of partner feeder airlines, to list their inventory in domestic and international reservations systems and to provide frequent flyer points **will be decisive.'***

DoT has not explained the basis for its claim that GDS is not feasible, or the figure of $1m. Shire of Shark Bay understands that there are many options for GDS to suit most budgets and that some airlines choose to piggy-back on larger airlines' GDS systems (such as Alliance and Air North with Qantas).

Further, DoT has chosen to use the words "*where possible"* when referring to the need for GDS and linkages with other airlines. The use of the term 'where possible' is extremely vague and causes unease. DoT must explain how it would measure the level of 'possibility'. Shark Bay Shire is not satisfied that DoT has acknowledged the criticality to the region of future inclusion in an airline GDS and connectivity beyond Perth.

In summary, the tourism and travel industry do not spend time debating whether or not GDS is important. It is, quite simply, fundamental to properly servicing a tourism market.

DoT should not continue to sponsor Skippers or any other airline to save money on airline distribution costs. Any airline unwilling to invest in the basic distribution infrastructure required to properly service the market should be excluded from a fresh tender process on the basis of non-conformity with tender requirements.

- *Overall, travellers to and from the region appear to be satisfied with the quality and schedule of air services. Industry, tourism and social needs are being met. (DoT Position Paper Page 47)*

This statement is incorrect. To reiterate the point, DoT's claim that the services are meeting industry, tourism and community need is distinctly contradictory to information provided by stakeholders surveyed by GDC, as reported to DoT in December 2013:

- Services are not affordable
- The needs of the tourism industry and business sector are not being met, and this is obstructing economic development
- Due to high cost, social needs are not being met, this includes inability to visit friends and relatives
- Due to scarce regional linkages, needs for school and medical travel are not being met

To again reinforce Shark Bay Shire's view, these proclamations generate serious concern due to their potential to influence decision makers whilst having no strong foundation or basis for making the claim.

- *Shark Bay can only work in conjunction with Carnarvon (DoT Position Paper Page 49)*

This statement has the potential to lead the market to a particular position rather than encouraging the market to consider innovative methods to address the scope of works.

It does not make economic sense to pair two of the states most marginal routes – Carnarvon and Shark Bay – together.

It makes far greater sense to leverage and use the access rights that DoT holds to stronger routes by pairing them with marginal routes and thus bolstering airline interest. This will ensure that smaller regional communities are not marginalised as a result of the state's air regulation policy. The destinations need not be geographically located close by as the connection is a contractual one only exercised via Deed.

This is the network approach historically proven and necessary to ensure government meets its obligations to provide adequate services to remote and marginal areas of the state.

Further, if a subsidy is now required for Shark Bay as a result of the dismantling of the state network and the downward trend triggered by the 2011 tender process, DoT must accept this path may now be necessary.

There are many possibilities of route combinations and DoT is reminded of past government policy that was strongly against allowing airlines to just service the best routes ('cherry picking').

The concept of cross-subsidisation has been explained earlier in this paper, and the quote from the CAPA report is again reported here for emphasis:

Airlines typically operate a network of routes. Only some of these routes will be profitable on a fully costed basis. However once these routes have been served it is in the interests of the airline owner to use spare capacity on routes that can at least cover marginal costs.

This results in the well-known cross subsidy across routes. It is important to recognise that this type of cross subsidy is commercially sensible. It is not akin to a community service obligation. Cross subsidisation across routes is a common practice amongst airlines including those operating RPT services in WA. Such practices obviously benefit passengers on the subsidised routes. However, they also benefit routes that provide returns to facilitate the subsidy because overall aircraft utilisation is higher, overheads are distributed more widely and the overall profitability and sustainability of airline operations are increased.

In summary, DoT must not draw conclusions around network deed and route structure without having tested the market or consulted with airlines. Cherry-picking should be disallowed. DoT must canvass airlines and encourage innovative thinking around route structure while leveraging access to stronger routes to bolster airline interest in marginal routes.

- <u>*Lack of screening has reduced the airfares significantly. (DoT Position Paper Page 49)*</u>

There is no support for the claim that Shark Bay travellers have enjoyed ‘significantly’ lower airfares as a result of the absence of security screening. This does not correlate with the high cost of Skippers airfares to Shark Bay.

How is DoT benchmarking Shark Bay airfares against other routes where screening is in place?

9. Recommendations Summary

Shire of Shark Bay is committed to moving forward constructively with DoT to achieve a satisfactory outcome meeting the expectation of stakeholders. Shire of Shark Bay’s recommendations and expectations are as follows:

1. The Shire of Shark Bay supports DoT’s recommendation of continued regulation of the route.

2. This is on the proviso that DoT runs a fresh tender or EOI process for Shark Bay using a new minimum criterion that delivers a return to pre-2011 service levels. In particular, the process MUST return a focus to recognising tourism as the major industry and economic driver of the area.

3. The fresh tender process, to be run by DoT, must be guided by a Steering Committee that will work alongside DoT. The Steering Committee will comprise members of the public that will represent the interests of small business, tourism and community.

4. DoT must consult with airlines and encourage innovation in their approach. Route structure models and combinations currently in place need not indicate the future structure of the statewide air transport network.

5. The fresh tender process must leverage access to stronger routes under DoT licence control against the service needs of more marginal routes, taking a state-wide approach.

6. Further, if needed, a safety net subsidy should not now be out of the question. This could now be necessary as a result of the degradation of the Shark Bay market post-2011 Deeds.

7. DoT must also work to remove unnecessary barriers to market growth and economic development, specifically around airport infrastructure and security screening requirements.

A successful outcome for Shark Bay for the form of regulation, after completion of the current Deed period in 2016, is for continued regulation with a fresh tender or EOI process incorporating the revised minimum requirements for selection criteria.

The features listed below represent stakeholders' **minimum requirements** for any airline servicing the region under a government awarded licence.

- Improved methods of Deed management via KPIs and control of airfares.
- Flight schedules with frequency, linkages and timing that meet the social, tourism and economic needs of the community.
- Aircraft type of a typical regional commercial airline standard (this excludes Metroliner).
- Affordable airfares – benchmarked to state average.
- Participation in an industry standard airline global distribution system.
- Destination marketing program.
- Connectivity with other domestic and international airlines through fares.
- Frequent flyer program.
- Passenger lounges and facilities at main airport.
- Customer contact center with extended operating hours.

DoT is again reminded that **all of these features** were in place prior to the 2011 tender process which resulted in DoT replacing Skywest with Skippers. Additionally, there was no subsidy requirement at that time.

Shire of Shark Bay looks forward to in future working constructively and closely with DoT to achieve acceptable outcomes for the region.

Appendix – Ningaloo -Shark Bay National Landscape Committee, November 2013

WA Department of Transport's State Aviation Strategy Submission from Ningaloo Shark Bay National Landscape

I understand that the air service to Shark Bay and Carnarvon is under review.

The result of the government's decision to appoint Skippers as the airline service for Shark Bay and Carnarvon has, as detailed below, resulted in a lesser service than was previously provided by Skywest.

This has resulted in inconvenience to local stakeholders, exacerbated the effects of the tourism downturn caused by the GFC and strong Aussie dollar, impeded the growth and development of the region and created economic hardship to both business and community.

Whilst Skippers staff and crew do an excellent job and the company is an efficient FIFO operator, it cannot provide the service and facilities required by RPT domestic/international air travel.

- Loss of access to the Global Distribution System
- The Ningaloo-Shark Bay National Landscape is one of only 16 locations selected by Tourism Australia & Parks Australia to present to international visitors as an iconic destination.
- By appointing Skippers, the Shark Bay and Carnarvon airports of the National Landscape have been isolated from air travellers because they can't be accessed via the GDS. As a result travellers are routinely told by travel agents that it's not possible to fly to Shark Bay.
- Tourism is the life-blood of the Shark Bay World Heritage Area (which contains the internationally renowned Monkey Mia dolphin experience).
- Loss of route connections between Exmouth, Carnarvon and Shark Bay
- Shark Bay Car Hire used to have a solid market for hiring cars to visitors wanting to explore the region to Exmouth. The company would routinely fly to Exmouth to collect cars. When the Shark Bay- Exmouth connection was lost so was a significant portion of their business.
- Visitors are no longer able to fly from Shark Bay to Exmouth to connect with a flight to Broome and other locations and invariably have to back track to Perth to access these connections
-
- Exmouth has lost business from Shark Bay and Carnarvon and vice-a-versa

Fare structure

- Remains consistently high and has no rewards program. It's possible to fly Perth/Brisbane return for close to the same airfare as one-way Perth/Shark Bay

Marketing & Packaging

- Skippers does no tourism marketing or packaging of its own.

Schedule & connection with domestic flights

- It is not possible to book through connections as with other domestic carriers.

Baggage check through

- It is not possible to check baggage through to/from as with other domestic carriers.

Skippers Terminal issues

- The Skippers terminal is located well away from the domestic terminal.
- It is poorly signed if endeavoring to find it within the precinct of terminals.
- The connecting courtesy bus service to the domestic terminal is unreliable.
- It is not possible to obtain or leave a hire car at the terminal.
- Taxis are reluctant to take a hire between domestic terminals.
- Travellers arriving in the early morning to take a flight have found the terminal closed.
- Food and drink machines are often empty.

The future of the Ningaloo – Shark Bay National Landscape is very reliant on a good quality of air services with linkages between Shark Bay and Exmouth. It is essential that an airline be appointed that is as accessible and convenient to consumers and the travel industry as other iconic destinations.

The Ningaloo – Shark Bay National Landscape Committee is about to undertake an Experience Development Strategy that will set the framework and direction for the future of the landscape. With the current aviation structure it will not be possible to develop an optimum structure that would include product development dependent on a better quality of air services.

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