

21st January 2009

Mr. Cathal Guiomard
Commissioner for Aviation Regulation
Commission for Aviation Regulation
3rd Floor
Alexandra House
Earlsfort Terrace
Dublin 2

Dear Cathal,

Detailed below is Cityjet's response to CP1/2009.

The Consultation on the Decisions of the 2008 Aviation Appeal Panel

1. Although the DACC's Appeal to the Panel, which included Cityjet's views was not upheld, Cityjet welcomes the decision of the Appeal Panel to refer matters back to the CAR based on the Appeal by Ryanair. This response draws on Ryanair's Appeal and highlights those matters supported by Cityjet.
2. First and foremost, Cityjet welcomes and agrees with the view expressed by the Panel that *"permitting what may be a greatly oversized Terminal 2 does not facilitate the efficient and economic development of Dublin Airport and might give rise to a risk to the financial viability of DAA, contrary to Section 33(1) (a) and (c) of the 2001 Act."*¹ Cityjet considers that this gives a clear signal to the CAR that the cost of T2 is excessive and that it has a duty to reduce the proportion of the costs allowed to enter the RAB if it is to comply with its statutory objectives.

¹ Ryanair Appeal Decision, paragraph 8.18.

3. Cityjet considers that there are other key messages that emerge from the decisions of the Panel, namely that the CAR can no longer engage in “*passive regulation*”². It is with considerable concern, therefore, that the CAR refused to meet with the DACC on the 16th January, as requested by letter of 12th January, to discuss the important issues arising from the decisions of the Appeal Panel and other important matters relating to the regulation of Dublin Airport. Each of the matters are referred to in turn below.

Assessment of capacity at Terminal 1 at Dublin airport

4. The Panel made clear that it considered that the CAR erred in its 2007 Determination because it had “*considered the size of T2 in isolation without properly considering the scale of the economic and efficient next increment of capacity at Dublin Airport to meet user needs within the limits set by (a) the Local Area Plan, including the provision therein for the further development of the airport on the western campus, and (b) runway constraint.*”³ In other words, the CAR should have first established the capacity offered by the existing infrastructure (T1 and the runway) before determining what the requirement was for additional capacity by taking Dublin airport as a whole and having regard to the scale of a cost effective increment to meet the needs of all users in aggregate.
5. It is clear that the Panel also considered the cap of 30 mppa under the Fingal Local Plan to be material to the determination of the overall scale of development, which could be approved to enter the RAB.
6. The Panel stated that “*in order to properly assess the proper size of Terminal 2 (and accordingly the appropriate parameter for Box 2) the Commission must first establish and clearly identify the capacity of Terminal 1*”⁴ and that “*Only having identified the capacity of Terminal 1 can a view be taken as to the appropriate size of Terminal 2 by reference to the needs of the airport and airport users.*”⁵ In other words, the CAR is required to consider the capacity of Terminal 1 as augmented by T1X, Pier D and Area 14, all of which were known to the Commission in July 2007.

² Ibid, paragraph 8.12.

³ Ryanair Appeal Decision, paragraph 8.3.

⁴ Ibid, paragraph 8.4.

⁵ Ibid, paragraph 8.5.

7. The CAR's assessment of T1 capacity at 18.5 mppa in CP5/2007⁶ is not supported by evidence and lacks the transparency that the Panel said the CAR needed to adopt in relation to its full reasoning as to the costs which are allowed into the RAB. Cityjet notes that the 2001 Determination of airport charges at Dublin Airport was based on a RAB designed to deliver 19.7 mppa in T1 by 2006. Is it axiomatic, therefore, that additional projects completed since 2006 must have served to increase capacity materially above that level.
8. Cityjet considers that the CAR erred in setting the capacity of T1 at 20 mppa as its basis for considering the capacity required in T2 in its 2007 Determination. We share the view expressed by Ryanair that, having regard to the capital works completed or underway, the capacity of T1 will be of the order of 25-26 mppa in 2009, particularly once airline efficiency improvements such as the use of kiosks and internet check-in are taken fully into account and, as should have been apparent to the CAR, as reflecting industry trends at the time of the 2007 Determination. We note that the Panel expressed support for Ryanair's view as it had not been challenged, *"In those circumstances the Panel tends to the view that Ryanair's calculation may well be correct. If that is so the capacity of Terminal 1 could well be up to 26 million passengers per annum."*⁷

Consequential assessment of the required capacity for a second terminal

9. Cityjet agrees with the Panel's statement that the CAR should not reach a view on the scale of T2 development required to meet the needs of all users of Dublin airport, without first having assessed and taken full account of the capacity of T1. The Panel also made it clear that *"The delay in the provision of a second runway"* was a material consideration as well as the 30 mppa planning cap under the Local Area Plan.⁸
10. In other words, it is clear that the Panel took the view in reaching its decisions that the required capacity of T2 should be the difference between the capacity of T1 and the ceiling of 30 mppa. The costs relating to this increment of capacity, and no more, is all that should have been allowed into the RAB. On balance, we tend to support the view expressed by Ryanair that this should have been of the order of 5 mppa's worth of capacity overall or no more than 45% of the cost of T2 overall. We support the view expressed by the Panel that any development of T2 beyond this scale should have been at DAA's risk⁹.

⁶ CP5/2007, page 107

⁷ Ryanair Appeal Decision, paragraph 8.10.

⁸ Ryanair Appeal Decision, paragraph 8.6.

⁹ Ibid, paragraph 8.12.

11. Of particular concern to us is the timing when T2 enters the RAB. Runway constraints at Dublin Airport presently prevent any growth in peak hour traffic, particularly in the morning, with the departure capacity of 31 movements per hour acting as a binding constraint. It would appear to us that the CAR was advised that making effective use of T2 would require runway capacity of 36 to 38 departing aircraft movements in the busy hour to be available in the first year of opening¹⁰. We do not understand how the CAR could have approved expenditure to enter the RAB in 2010 when its own consultants advised that:

“As the runway capacity ultimately determines the capacity of the airport we are concerned that without delivery of additional runway capacity by 2009 the proposed terminal capacity at Dublin Airport will far exceed runway capacity resulting in the inefficient use of capital investment.”¹¹

and

“Given the possibility of a delay to the delivery of a new parallel runway at DUB, the magnitude of additional terminal capacity being provided by the DAA could result in both T1 and T2 being substantially underutilised as a result of runway capacity constraints.”¹²

12. The situation has further deteriorated by DAA’s announcement that the construction of the new runway will be delayed beyond the planned date of 2012¹³. We believe that there is no case for the costs associated with that development to enter the RAB until additional runway capacity is provided. We accepts this may not be a matter for this review but for the next Determination later in 2009.

Correct sizing of the Terminal 2 that DAA proposed to build:

13. We support the view expressed by Ryanair that, based on its evidence, the size of T2 required is 45% of the size being constructed by DAA, having regard to the capacity of T1, the planning cap of 30 mppa and any loss of effective efficiency as a consequence of splitting demand across two terminals.

¹⁰ RR&V Report No 4: Review of DAA Terminal Sizing, page 23.

¹¹ Ibid.

¹² RR&V Phase II Report and Responses, July 2007, page 12.

¹³ Press Statement of 18th December 2009.

Consideration of the appropriate T2 associated projects capital expenditure which should be included in Box 1 or Box 2;

14. The Panel made clear that consequent upon a detailed assessment of the capacity required to be provided in T2, having regard to the capacity of T1 and the Local Plan capacity ceiling of 30 mppa, the CAR should then determine what proportion of DAA's expenditure on T2 should be included in Box 1 and what included in Box 2.¹⁴ We support Ryanair's assessment that €171 million of the CAR's adjusted costs for the T2 terminal building are eligible to be included in Box 1. The remaining terminal building costs of €208 million should be placed in Box 2 to remain at DAA's risk. The Appeal Panel referred back issues relating to Pier E, apron and other costs under a separate heading, dealt with below. Any costs entering the RAB at the time of the next Determination should be subject to the caveat that it must be demonstrated that the costs have been efficiently incurred.

Decision to exclude €25 million in respect of contingency costs in reaching its determination;

15. Cityjet notes that the Panel referred back the CAR's decision to substitute DAA's contingency costs relating to T2 with those of its own¹⁵. Such a decision could be material to the level of charges within the current Determination period as it relates to the projected amounts of T2 expenditure upon which DAA is allowed to earn a return within the current regulatory period to the end of 2009. However, in the context that the Panel made clear that it did not expect the results of its referral back of certain matters to result in change as to the current level of the cap on airport charges¹⁶, merely to what capital expenditure would be allowed into the RAB and the conditions relating to Box 1 and Box 2, this is not material. By the time the opening RAB for 2010 is set, it will be clear the extent to which DAA has been required to use such contingency allowances in the course of constructing T2. If such contingency allowances have been spent, they fall eligible to enter the RAB, subject to the Box 1/Box 2 conditions and provided the costs have been efficiently incurred. If the contingency allowances have not been required, they cannot enter the RAB at that point.

Decision to exclude certain airfield projects costs in the determination under appeal;

16. In relation to whether the CAR was right of not to reduce the cost of some airfield projects by €4 million in its 2007 Determination, the same considerations apply as note above in relation to the €25 million contingency costs in respect of T2. By the time of the next review, the actual costs will be known and the RAB set on that basis, subject to the test of efficient procurement.

¹⁴ Ryanair Appeal Decision, paragraph 8.15.

¹⁵ DAA Appeal Decision, paragraph 8.8.

¹⁶ The Panel stated that it did not consider that the cap on airport charges should have been either reduced or increased in the Interim Review – Ryanair Appeal Decision, paragraph 8.23

Consequential appropriation of capital expenditure into Box 1 and Box 2, particularly the treatment of Pier E as either part of Box 1 or 2;

17. We understand that the CAR relied on DAA's response to the consultation on CP5/2007 to justify the exclusion of the costs of Pier E and various T2 ancillary developments from the two box approach. However, these facilities are, like the terminal itself, sized to handle particular hourly flows of demand and not related to some overall annual passenger throughput. Therefore, to the extent that the main terminal block is oversized, the vast majority of these facilities will suffer from the same over-specification.
18. The Panel made clear that it agreed with Ryanair that the CAR erred in the 2007 Determination in effectively allowing all such costs into Box 1 on the basis that DAA's argument was "*persuasive*"¹⁷. DAA merely noted that the size of these facilities is related to peak hour demands, of which the CAR was itself critical, and cited a gating analysis¹⁸, which was based on the same overly peaked aircraft schedule which had been used to generate the excessive terminal busy hour demand. It also merely asserts that other facilities cannot be reduced in scale if a lower design hour throughput was adopted.
19. RR&V considered the requirement for Pier E in its Phase II Report of July 2007. They noted that full consideration of the scale of pier requirement was outside the scope of their study but made a pertinent comment that "*Reducing the level of demand, in line with alternative busy hours could result in a reduction in the size of Pier E.*" We agree with this view.
20. The logical consequence of the adopting a significantly lower design hour passenger flow as the basis for sizing the terminal building for inclusion with Box 1 applies equally to the pier, apron and associated works, with any risks associated with DAA building too large a pier and any phasing implications being placed in Box 2.
21. The Panel expressed a clear view that the approach adopted by the CAR in CP5/2007 was the correct one and "*should be reinstated*". This means that the costs of T2 associated projects should be subdivided into Box 1 and Box 2 roughly in proportion to the division of terminal related costs.

¹⁷ Ryanair Appeal Decision, paragraph 8.16.

¹⁸ DAA Response to CP5/2007, page 53.

Remuneration of Box 2.

22. The Panel made clear that it is not appropriate to allow any remuneration of the costs eventually placed in Box 2 until the trigger of 33 mppa is reached¹⁹. This means that the CAR erred in the 2007 Determination in allowing DAA to earn its cost of capital (a return on the costs) on the full cost of T2 from when it has been incurred. To the extent that DAA has been doing so as a consequence of leaving the airport charges cap unaltered for the period to 2010, the excess income, which DAA has received, will need to be clawed back in the next Determination for the period 2010-2014. The Panel made clear the *“risk of oversizing is one which should be borne by the DAA, not be current or prospective users.”*²⁰ The Panel made clear that allowing a return on such costs was clearly contrary to the 2001 Act.
23. Cityjet also welcomes the clarification by the Panel that, in assessing whether the trigger for the costs of Box 2 to enter the RAB, for the purpose of both earning a return of and a return on capital, would be related to the throughout of the Eastern Campus only, i.e. taking no account of any additional passengers permitted to be handled on a Western Campus by the construction of a competitive third terminal²¹. The Panel stated that to do otherwise would be contrary to Section 33(1) (b) of the 2001 Act as it would allow DAA to benefit from having built an oversized T2 at the expense of users.
24. The 2007 Determination allowed DAA to earn a return on the full cost of its investment in T2, which the Panel has clearly stated to be in contravention of the 2001 Act. Furthermore, pursuant to its obligation to have regard to the financial viability of DAA, the CAR gave a commitment to accelerate depreciation in the event of any financial shortfall for DAA. As a consequence, given that DAA has already incurred the excessive costs of development, the effect of the CAR’s decisions will be that users will effectively be required to pay for such facilities even though they cannot ever be used given the planning cap on the passenger throughput on the Eastern Campus. This is unacceptable.

¹⁹ Ryanair Appeal Decision, paragraph 8.19.

²⁰ Ibid, paragraph 8.20.

²¹ Ryanair Appeal Decision, paragraph 8.22.

25. Essentially, therefore, the CAR wrongly indemnified DAA as against any exposure it may have due to its building an oversized T2 Phase 1 in the event that it does not or cannot reach the Box 2 trigger of 33mppa. Such indemnity, if it arises, would be paid for by airport users by way of even higher airport charges. The Panel made clear that such risks associated with the over-sizing of T2 should be borne in their entirety by DAA. Cityjet calls upon the CAR to reverse its decision in the treatment of such costs and to ensure that any excess revenues collected by DAA as a result of its 2007 Determination are returned to users in the next review.

Issues for the Next Review

26. We consider that there are other matters, relating to the 2009 Determination, upon which the Panel expressed a clear view, in particular:
- (a) the treatment of the T2 depreciation costs within a unitised framework;
 - (b) the timing when T2 is deemed to be operational.
27. We consider that this re-consideration should also extend to the status of Pier C.
28. A particularly important consideration for us is the implementation and form of unitised depreciation, an approach which the Panel endorsed²². We are particularly concerned that a further dramatic increase in the cost of using Dublin Airport, consequent upon the full costs of T2 entering the RAB, would be catastrophic in terms of the impact on traffic growth in the current economic climate. In response to the Appeal by Aer Lingus, the Panel made clear that the definition of when T2 becomes operational, and hence when depreciation costs fall to be recovered from users, *“will be considered in the 2010/2014 Determination and any matters to be considered can be considered within that consultative process.”*²³ Given the constraint imposed by the capacity of the current runway system at Dublin Airport until at least 2013 (or later), we believe that this will be a very significant matter for consideration at the next review in the context also of projected levels of growth in demand relative to current terminal capacity.

²² DAA Appeal Decision, paragraph 8.7.

²³ Aer Lingus Appeal Decision, paragraph 9.1.2.

Yours sincerely,

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