

SUBMISSION TO THE COMMISSION FOR AVIATION REGULATION
ON THE DETERMINATION OF AIRPORT CHARGES

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Confidential Annex (Separate Document) - WITHHELD

1. INTRODUCTION

This paper sets out Ryanair's submissions on the determination of airport charges by the Commission for Aviation Regulation (the "Commission") by reference to the Commission's paper entitled "Economic Regulation of Airport Charges in Ireland" (the "Consultation Paper").

The welcome appointment of the Commission comes at a critical juncture in the development of the air transport industry in Ireland when costs at the Irish airports controlled by Aer Rianta cpt ("Aer Rianta" or the "Airport Operator") have been escalating, whereas the level of service provided is unacceptably low. This has had a markedly negative effect on traffic volumes over the past year, particularly as regards travel from the United Kingdom, Ireland's largest market, which has stagnated at a time when Sterling has never been stronger. This stagnation in traffic and the absence of airlines willing to develop new routes in the current environment have wider implications than just the profitability of the Airport Operator or the airport users ("Users"). More importantly, this situation affects the strength and development of the Irish economy as a whole given the vital nature of air access for a peripheral island nation.

Given the recent shocks to the Irish economy, including the downturn in the US economy and the outbreak of foot and mouth disease, the development of air transport is a crucial factor in sustaining the strength of the Irish economy. The foot and mouth crisis also points to the danger of over reliance on the UK market for air transport services. Currently, 57% of Irish air traffic is between Ireland and the UK.

The situation at the Irish airports is in stark contrast to the rapid growth of air transport services elsewhere in Europe and particularly to the development of low fares air services out of the UK. The low fares sector is now the fastest growing sector of the European aviation industry. Minetel's February 1999 'Low-Frills/Low-Cost Report' predicted that the sector will grow from 5.4 million passengers in 1998 to 15 million by 2003. This is probably a conservative estimate given that Ryanair's traffic alone will increase to approximately 9 million in 2001.

Ryanair was largely responsible for lowering air fares, which created the boom in air travel between Ireland and the UK in the 1980's and early 1990's following deregulation between those markets and is now having the same effect offering low fares services from the UK to the European Continent. Indeed, the UK has seen much more growth in the low fares airline sector than any other European country to date. The UK has also benefited from having been one of the first countries to introduce a more commercial approach to airport management. This has helped to ensure that UK airports meet the needs of their users while keeping their costs low. The result is that many of the heaviest air passenger flows in Europe are between London and other major European cities.

High and rising costs and inefficient facilities in Ireland are hampering the ability of Ryanair and others to offer similar low fare services from Ireland to the Continent and increasing capacity from Ireland to UK destinations. Stagnation of traffic on existing routes and the absence of any significant new route development are likely to continue unless the Commission is successful in introducing a regulatory environment that simulates competition, i.e., increases efficiency and reduces costs. Such an environment would inevitably lead to lower fares, new route development, increased passenger volumes and higher levels of service.

Importantly, the Department of Public Enterprise (the "Department") has already recognised the importance of these objectives in its Statement of Strategy for the three State Airports, which requires Aer Rianta to:

- Provide the necessary infrastructure and services at the lowest possible cost, consistent with safe commercial operations;
- Provide a financial return to the shareholder which is consistent with the foregoing requirements;
- Develop traffic at the three State airports; and
- Exploit new business opportunities, provided they are organically linked to the core business and do not detract from the core responsibilities.

It is clear to Ryanair that Aer Rianta has failed to fulfil the Department's mandate of providing the necessary infrastructure at the lowest possible cost. Moreover, Aer Rianta's escalating costs and charges are leading to stagnating traffic growth, which is contrary to the Department's mandate of "developing traffic". However, Aer Rianta certainly has been very successful at providing monopoly level financial returns to its one shareholder, i.e., the State, and in fact is one of the most profitable airport operators in the world (indeed, in 1998 it was the second profitable airport operator in Europe and fourth in the world on a profit per passenger basis - see report from Airline Business Magazine from December 1998, attached as Annex 1).

However, Ryanair submits that this is not and should not be the primary objective of the Airport Operator, especially in the case of Ireland where air access is vital to the development of the economy as a whole. Finally, Aer Rianta has also exploited new business opportunities all over the globe but Ryanair submits that these business opportunities are in no way "organically linked" to Aer Rianta's

core business, i.e., the management of the three State airports. Moreover, these other business opportunities have seriously detracted from Aer Rianta's core responsibility of developing traffic and new routes at the three Irish airports.

Ryanair welcomes the opportunity to submit its comments as part of this consultation process for the Commission's determination of the airport charges to be applied at the three regulated airports, Dublin, Cork and Shannon (the "Regulated Airports"). It is vital to Ireland's future that the Commission will be successful in achieving the objective set forth in the Aviation Regulation Act, 2001 ("the Act"), i.e., "to facilitate the development and operation of cost-effective airports which meet the requirements of users". The Commission will note the deliberate and singular emphasis on the part of the Oireachtas that the "requirements of users" and not the Airport Operator are met. The Commission's determination should therefore accurately reflect the differing requirements and operational practices of the different users at the Regulated Airports.

To this end, the regulatory framework must be structured in order to force Aer Rianta to increase its efficiency and reduce its costs. Increased efficiency and reduced costs will lead to increased traffic and new route growth. However, there must also be an effective mechanism that ensures consultation and consensus between the Airport Operator and the users. Finally, the regulatory framework should facilitate the introduction of competition wherever possible in the provision of services and facilities at the Regulated Airports.

Ryanair would welcome an opportunity to expand on its submission at a meeting with the Commission.

2. BACKGROUND ON RYANAIR

A brief history of Ryanair is set out below in order to provide a background to its submissions.

Ryanair is Europe's largest low fares airline and is headquartered in Ireland. It is a publicly quoted company whose shares are traded on the Dublin, London and New York (Nasdaq) stock exchanges. It is committed to low-cost air-fares and introducing competition to flag carriers and the growing alliances in the European air transport market. Its ability to offer the lowest fares in the industry to passengers is dependent, to a very large extent, on low-cost and efficient airports.

Ryanair, began operations in 1985 with the launch of a daily flight on a 15-seater turbo prop aircraft between Waterford Airport and London Gatwick. The company began with a commitment to providing low fare air travel to the Irish public in contrast to the oligopoly pricing being offered at the time by Aer Lingus and British Airways. Ryanair was the first European airline specifically set up to offer low fares and competition on short-haul intra-European routes. In the company's first year, its 57 employees carried just over 5,000 passengers on this original route.

In 1986, Ryanair entered the Dublin-London route, which was then shared by two state-owned airlines namely, Aer Lingus and British Airways. The Dublin-London route had been stagnating at about 1 million passengers per annum between 1975 and 1985, and was then characterised by some of the highest air fares per kilometre in Europe. Prior to Ryanair's entry onto the route, the normal airfare between Dublin and London in 1985 was £209 return. Ryanair began services on the 23rd May 1986, with an introductory launch fare of £94.99 return. In its second full year of operation, Ryanair's 120 employees carried just over 82,000 passengers on two routes.

Over the next three years (1987 to 1989), Ryanair expanded rapidly opening many new routes between Ireland and the UK and increasing its fleet. However, while customers continued to flock to Ryanair for the low airfares, costs were not controlled, and the company racked up significant losses. By 1990, the company employed 350 people, operated 14 aircraft (four different types), was carrying 600,000 passengers a year, but had managed to lose £20 million in just four years. These losses were largely due to over expansion and the inability to tightly control costs in the newly deregulated market where such cost control was essential to the ability to offer low fares services profitably.

Under a new management team, a major overhaul of the airline was undertaken in 1990/91, with Ryanair relaunched as the first in a new breed of "low fares/no frills" airlines adapting, in a European environment, the formula so successfully pioneered by Southwest Airlines in the U.S. It is clear from the Southwest model in the US that a low cost base in terms of airport costs and efficient facilities is critical, (given the relative constancy of other costs such as fuel and aircraft) for developing a low-fares airline.

Non-profitable routes were eliminated, the network was cut back from 19 to just 5 routes, the turbo prop aircraft were disposed of, and airfares across the remaining network were substantially reduced with 70% of all seats offered at the two lowest fares. On Dublin-London, for example, a new promotional fare of just £69 return was launched which stimulated a whole new era of growth for Ryanair, Irish tourism and travel between Ireland and the UK. By 1991, Ryanair was operating an all jet fleet of 6 BAC 1-11 aircraft, employing 350 people, carrying 700,000 passengers on just five routes, and it had recorded its first ever profit, despite the damage done to the airline industry by the Gulf War in 1991.

Over the next couple of years, schedules on the key Dublin-London route were increased, average air fares were lowered, new routes were launched from Dublin to Birmingham, Glasgow, Manchester, and Gatwick, while traffic continued to grow strongly due to Ryanair's commitment to increasing capacity and continuously lowering fares. By 1994, Ryanair was employing over 500 people, carrying over 1.5 million passengers per annum, offering the lowest air fares in Europe, starting at just £49 return on the Dublin-London route, and had recorded its fourth consecutive year of profitability.

1994 also saw the acquisition of Ryanair's first Boeing 737 aircraft with an order for six second-hand 737-200 series aircraft (130 seats) being purchased direct from Boeing. Over the following three years a further fifteen 737-200 aircraft were purchased bringing the fleet to twenty-one 737-200's. To coincide with this expansion of the fleet, many more new routes were opened by Ryanair between Ireland the UK, increased frequencies were offered on all routes, and air fares were lowered even further. As a result in 1995, the airline's 10th anniversary, Ryanair had become the largest carrier on the Dublin-London route and on each of the routes on which it operated (in terms of traffic on those routes), with total passengers of 2.25 million per annum and the work force now exceeded 600 people.

Following full EU air transport deregulation in 1997, the airline was free for the first time to open up new routes to Continental Europe. Services were launched from London Stansted to efficient secondary airports in Stockholm and Oslo, as well as from Dublin to efficient secondary airports in Paris and Brussels. Again, Ryanair entering these markets offered air fares which were up to more than 80% lower than the cheapest mid-week fares then provided by the flag carrier airlines. Passengers responded enthusiastically and in great numbers to the arrival of low fares for the first time in these European markets. Ryanair was the first low fares airline to offer scheduled services from the UK to Continental Europe and vice versa. 1997 also saw Ryanair Holdings plc float on the Dublin and New

York (Nasdaq) Stock Exchanges. At the time, the airline was capitalised at a market value of IR£300 million, and was carrying over 3 million passengers per annum on its network of 18 routes.

Despite this success, Ryanair remained committed to driving down airfares, increasing frequencies and maximising the number of low fare seats available to both business and leisure passengers. Ryanair was competing head to head with many of Europe's largest airlines including British Airways, SAS, Alitalia, Lufthansa, Sabena, Air France, and Aer Lingus, but by offering an unbeatable package of low fares, on-time flights, high frequencies, and friendly in-flight service, Ryanair was continuing to succeed and win increasing public and customer support.

In 1999, Ryanair announced its next major investment programme with a US\$2 billion order for up to 45 new Boeing 737-800 series aircraft. These are the latest and most modern aircraft manufactured by Boeing. The first five aircraft were delivered to Ryanair in 1999, and five more scheduled for delivery each year thereafter. Ryanair was now offering Europe's lowest airfares, on Europe's newest and most modern aircraft. In 1999 Ryanair announced another set of record results, operating 35 routes to 11 countries, and carrying almost 6 million passengers. Ryanair's customers enjoyed over £300 million worth of savings over the competing high fares being charged by Europe's flag carrier airlines. The company was then employing over 1,200 people.

In early 2000 Ryanair launched Europe's largest travel website at www.ryanair.com, which within three months of its launch was taking over 50,000 bookings per week, by offering low airfares which started from as little as STG£1 return plus taxes on Glasgow-London and STG£9 return plus taxes on the Dublin-London routes. In February 2000, Ryanair announced the launch of 10 new European routes for Summer 2000, with services from London (Stansted) to Malmo in Sweden; Hamburg (Lübeck) in Germany; Verona (Brescia), Sardinia (Alghero) and Lamezia in Italy; Provence (Nimes) and Perpignan in France; and Shannon in Ireland. The airline also launched 2 new low fare services from Frankfurt (Hahn) last Summer to Shannon in Ireland and to Glasgow (Prestwick) in Scotland.

To date in 2001, Ryanair has launched 7 additional routes out of the UK and has increased capacity on a number of existing routes. In February, Ryanair announced the opening of its first Continental European base in Brussels Charleroi, from which it will initially offer services on seven routes. Ryanair would have established this base at an Irish airport had the cost base/facilities at the Regulated Airports been more competitive and cost-oriented. This year, Ryanair, will operate with a fleet to 36 Boeing 737's and will carry some 9 million passengers. Unfortunately, however, only some 18% of this traffic will originate in Ireland due to the uncompetitive cost base and inefficient facilities at the Regulated Airports.

It will be clear from this submission that Ryanair's rapid growth of routes and traffic will continue to be centred upon low cost and efficient airports so as to minimise airport costs and ensure rapid turn-around times and maximum efficiency of aircraft. This is a major factor in Ryanair's ability to guarantee the lowest fares in Europe.

3. BACKGROUND ON AER RIANTA'S CHARGING POLICY

Aer Rianta is the State-owned company that operates the three Regulated Airports in the Republic of Ireland. As such, it has a near total monopoly in the provision of air transport services to and from Ireland, with 97% of total traffic, and has a complete monopoly in the provision of services to and from Dublin as there are no other airports offering any competition within 100 miles of Dublin Airport. It is common knowledge that Ryanair has been staging a long-term campaign against Aer Rianta for what Ryanair perceives as an abuse of Aer Rianta's dominant position to maintain high costs and low service standards at the airports it controls.

This campaign has gained considerable momentum since 1998 when Aer Rianta indicated that it was going to do away with a scheme of discounts that had applied to its published tariff over the past 15 years. Throughout the late 1980's and 1990's, Aer Rianta, at the behest of successive Irish governments, maintained a policy of reducing airport charges, which were levied on airlines through a series of highly complex schemes based on the published tariff set in 1987. These discounts involved rebates on landing and passenger fees based on stimulating incremental growth, development of new routes and the use of inferior low cost facilities, i.e., Pier A. These schemes were initially agreed directly between the individual airlines and the management of Aer Rianta, but were subsequently formalised and approved by successive Government Ministers from about 1991 onwards.

The success of these schemes was such that costs to airlines were significantly reduced, fares to the consumers were dramatically lowered and traffic through Aer Rianta airports (and Dublin in particular) exploded. The most notable effect of this policy was to transform the stagnant Dublin/London route from 1 million passengers annually to over 4 million. The graph at Annex 2 demonstrates the so-called "Ryanair Effect" (i.e., reducing airfares, stimulating rapid traffic growth) on this route, a phenomenon that has been repeated on all of the routes on which Ryanair operates. It demonstrates that demand for air travel is highly elastic and that as fares go down, passenger numbers rise. The current stagnation on the Dublin-London route corresponds with the removal of the discount schemes. These schemes were in fact self-financing as the resulting additional traffic more than compensated for the lower passenger and landing charges, as the following table indicates:

DUBLIN AIRPORT

1987 1.8 m. departing passengers (3.6 m. total) @ £9.50 = £17 m. in airline fees
 1999 6.4 m. departing passengers (12.8 m. total) @ £6.00 = £38 m. in airline fees

Source: Aer Rianta annual reports.

In 1998, Aer Rianta commissioned PriceWaterhouseCoopers to undertake a report on its charges. The report concluded that Aer Rianta's published charges were not excessive when compared with the published tariffs of other European airports and in the context of its proposed £200 million development plans. However, Ryanair publicly attacked this report on a number of bases, but particularly on the ground that published tariffs are irrelevant, airlines and passengers are only concerned by the actual prices they are charged and not the published tariff. Ryanair also questioned Aer Rianta's proposed £200 million development, on which it and the other airport users had not been adequately consulted.

The report also recommended the unwinding of the various discount schemes as a result of the impending loss of duty free in 1999, due to the European Commission's abolition of duty free sales for passengers travelling between EC Member States. Ryanair noted that the airlines were also losing revenues from the loss of duty free but were not increasing their prices because of the intense competition for passengers. Ryanair also pointed out that Aer Rianta had eight years to prepare for the loss of duty free but made no attempt to reduce its costs. Instead, Aer Rianta built a multi-million pound duty free shopping complex in Pier C, the year before duty free was abolished. This complex has since been scaled back and is relatively under utilised.

In response to the PriceWaterhouseCoopers study, Ryanair commissioned a study by KPMG and the University of Westminster based on the actual charges then paid by Ryanair at all of the airports to which it operates. This study proves that Dublin Airport is the most expensive airport that Ryanair operates into, including such major airports as Gatwick, Manchester, Luton, Stansted. A non-confidential version of the study is attached hereto as Annex 3. This study indicates that Dublin Airport is over twice as expensive as the average costs across Ryanair's network. Indeed, this gap has increased following the completion of this report given the further increases in Aer Rianta's charges in 2001.

The effect of Aer Rianta withdrawing its discount schemes has been to approximately double the level of charges payable by Ryanair and other airlines to Aer Rianta. Ryanair submits in its Confidential Annex figures for the years 1998 to 2000, based on Aer Rianta's numbers, that indicate the average charge per passenger has doubled. Figures for 2001 are based on estimates as the amount of discounts for 2001 are not yet available. Also provided in the Confidential Annex is a table prepared by DKM Consultants in a report prepared for Ryanair in 1999. This table illustrates the effect on Ryanair's charges brought about by the unwinding of the discounts.

The DKM report concluded the following impacts of the increased charges:

- a. Increased ticket prices. For a price sensitive sector of the industry, this will lead to volumes being lower than they would otherwise have been. This will affect passengers originating at both ends of the route.
- b. The impact will be felt on both existing routes and on new routes that may come on stream.
- c. Where the overall viability of a route is marginal, or in the case of a new route uncertain, the cost increase may tip the balance and cause the route to be abandoned or scaled down. This may cause a much bigger impact than the level of cost increase may suggest.
- d. Dublin is no longer the only low-cost (tourist) destination from airports in the UK. The low-fares sector is expanding rapidly into Europe and very competitive fares to many destinations are now available ex-London. These are being provided by Ryanair and other low fares operators. This threatens the existing business to Dublin from the UK, especially London.
- e. It is likely that Dublin/UK will not continue to deliver growth at the level experienced over the last number of years. This market has reached a level of maturity and alternative low fares destinations are increasingly available ex-UK. Therefore, most new growth will have to be generated through other, new, destinations. To generate such business, competitive fares will be needed and this will require competitive airport charges.

Furthermore, Aer Rianta's development plan for 2020 is based on continued strong growth in passenger numbers. The "consultation process" currently taking place with regard to this proposed development is discussed in response to Question 39 below. However, Aer Rianta's proposed development is based on traffic growth projections that are not based in reality, or recent experience, and these growth projections have been attacked by several airlines, including Ryanair and Aer Lingus. The one proven way to achieve traffic growth is to maintain a competitive cost base that enables airlines to offer low airfares. This is where the majority of passenger growth at the Regulated Airports has come from in the past decade.

Aer Rianta has also been able to effectively prevent efforts to introduce competition at the airport. Aer Rianta rejected a proposal by Ryanair in 1998 to fund the construction of Pier D in exchange for a lower cost base. This low cost facility would have introduced 12 efficient pier served stands (at a cost of less than £1 million per stand) and alleviated the current shortage of such stands. Aer Rianta instead chose to spend £50 million on a three-story pier that only provides 5 pier served stands (i.e., at a cost of £10 million per stand) and is only used by two airlines. Aer Rianta has also prevented the construction of competing car parking facilities while at the same time has increased prices at its own monopoly car parks by 72%. Aer Rianta also prevented the Forte Crest Hotel from building a multi-story hotel extension, thus limiting the capacity of that hotel, while it built a multi-story hotel directly across from it, i.e., the Great Southern Hotel.

Furthermore, Aer Rianta has introduced and increased charges in other areas. In 1995, it introduced a fuel levy at Dublin Airport and recently attempted to introduce a similar levy at Cork. There was no additional service provided that would justify this fee. Although the British Aviation Authority ("BAA") in the UK operated a similar levy at Heathrow, Gatwick and Stansted, that levy was for the purpose of paying for new fuel hydrant systems that the BAA installed, thereby eliminating the cost of storage and tankering for its airline customers. However, at Dublin Airport, the airlines must still meet the cost of airfield storage and tankering.

More recently, Aer Rianta took advantage of the "regulatory vacuum" that was created during the period between the Commission's original appointment in 1999 and recent empowerment. Ryanair submits that during this period, the Department failed to control Aer Rianta's capex and allowed Aer Rianta to abolish the discount schemes, thus doubling the level of charges to Ryanair and other Users. In this respect, Aer Rianta increased capital expenditure by £350 million between 1999 and 2003, a 67% increase over the period between 1994 and 1998. Aer Rianta has also increased charges in other areas, including check-in desk fees; the introduction of an administration fee for groundhandlers; a fee for fixed ground power usage; fees on cargo handling, increased parking fees, etc.

Based on the foregoing, it is crucial that the Commission adopt the pre-1999 situation as a starting base for its determination. Otherwise, Aer Rianta would be permitted to circumvent the effectiveness of any economic regulation as it has been able to effectively "pad" itself against impending regulation during the "regulatory vacuum". That is, regardless of the formula applied by the Commission, Aer Rianta would still retain the majority of the increases it imposed over the past 18 months. Similarly, by basing itself on the current capital employed, the Commission's determination will be distorted as Aer Rianta's 67% increase in capital spending that also occurred during the period of regulatory absence.

4. KEY ISSUES

Ryanair has identified the following key areas of concern relating to the regulation of airport charges:

- (1) the need to recognise the essential nature of low cost air access to and from Ireland, a peripheral, island nation, and the risks of uniquely high (over) dependency of the Irish economy on low cost air access from the UK;
- (2) the need to develop new traffic and new routes as mandated in the Department of Public Enterprise's Statement of Strategy;
- (3) the need to significantly lower costs and increase the cost-effectiveness of the Airport Operator;
- (4) the need develop efficient facilities at the lowest possible cost (including competing low cost terminals);

- (5) the need to base the initial determination on the situation existing pre-1999 when the in order to discount the effect of the "padding" that has occurred during the "regulatory vacuum";
- (6) the need to fund capex in the short-term by selling non-core activities and to introduce cost-efficient financing of development (i.e., limit borrowing, promote public/private partnerships; co-funding by users, etc.);
- (7) the need for airport charges to accurately reflect the level of services and facilities provided;
- (8) the need for charges to reflect the benefits of increased passenger levels and the consequential increase in revenues to the Airport Operator; and
- (9) the need to promote effective competition in terms of services and facilities provided at the Regulated Airports;
- (10) the need to ensure effective consultation and consensus between the Airport Operator and its Users; and
- (11) the need for benchmarking to reflect the importance of low cost access to Ireland and therefore to be based on low cost access at comparable airports.

5. COMMENTS ON THE STATUTORY BACKGROUND

Introduction to Section 33

Ryanair notes that Section 33 of the Act requires that the Commission "shall have due regard to various factors". It is submitted that although the Commission must have due (i.e., reasonable) regard to the various factors, the Commission is not obliged to give equal weight (or indeed any weight in certain circumstances) to each and every factor. The Commission may therefore ultimately choose to ignore a factor that it regards as not meriting consideration in setting the airport charges. Furthermore, although the Act does not specifically allude to the development of traffic at the Regulated Airports, it is clear that this is an important and perhaps over-riding criterion that is featured in the Department's Strategy Mandate and should therefore be given significant weight in the Commission's determination.

Ryanair submits that the factors outlined in Section 33 must be taken into account in "making a determination" with the "aim to facilitate the development and operation of cost-effective airports which meets the requirements of users". It is imperative that the Commission bear in mind at all times that this objective refers to "users" as opposed to airport operators. It would be ultra vires the Commission's powers to do otherwise. Although the Act does not provide a definition of "user", Statutory Instrument No. 505 of 1998 on the Access to the Groundhandling Market at Community Airports (S.I. 505) defines "airport user" as "any person responsible for the carriage of passengers, mail or freight by air from or to an airport", i.e., airlines or freight operators. Thus, the Act recognises the importance of such development for the airlines and freight carriers that use the Regulated Airports. Ryanair submits that the Commission may also legitimately take into account the needs of users in terms of passengers.

Section 33(a)

Section 33(a) refers to "the level of investment in airport facilities at an airport to which the determination relates, in line with safety requirements and commercial operations in order to meet current and prospective needs of those on whom the airport charges may be levied".

It is submitted that in having due regard to investment, the Commission should include the facilities at the airport in question that relate to activities to be included in the single till (discussed further below). However, the Commission should also have due regard to the investments that have been made in Aer Rianta's non-core activities, Aer Rianta International, the Great Southern Hotels, and overseas airports, as these activities have affected the situation at the Regulated Airports due to the cross-subsidisation that occurs between these activities.

The level of investment considered by the Commission should relate to current and prospective needs that meet the requirements of Users. This certainly has not been the case in the past or currently and Aer Rianta has made investment and development decisions with no regard to the needs of users. As a result, investments have been made that add to the inefficiency of the Regulated Airports and the users are paying for this inefficiency in the form of inflated charges.

Section 33(b)

Section 33(b) refers to "a reasonable rate of return on capital employed in that investment, in the context of the sustainable and profitable operation of the airport".

Ryanair submits that the amount of capital employed must first be established and, as discussed above, should be that existing pre-1999, i.e., before the Commission was appointed. It is further submitted that sustainability of airport operation should be considered as the primary criterion over profitability given the essential nature of the airport infrastructure for access to Ireland.

Section 33(c)

Section 33(c) provides that one criterion is the "efficient and effective use of all resources by the airport authority".

Ryanair submits that the criterion of efficiency and effectiveness should be measured against the ability of the Airport Operator to develop traffic and new routes at the Regulated Airports. This can only be achieved through the efficient and effective use of all resources available to the Airport Operator. This would include actual and potential resources either under its own ownership or control as well as those resources which may be available to the Airport Operator. Thus, if a third party (e.g., an airline or other party) is willing to provide (or part finance) resources to the Airport Operator then those resources ought to be taken into account as being available to the Airport Operator for the purposes of resource utilisation by the Airport Operator.

Section 33(d)

Section 33(d) refers to the "contribution of the airport to the region in which it is located".

This is an important criterion for which serious consideration should be given. In the context of the Irish air transport sector, being a peripheral island nation makes access to air transport a crucial factor in the development of business and tourism in the regions surrounding a particular airport. The Irish Government has recognised the importance of the tourist industry in Ireland, which is driven by low cost access. The relevance of an airport's contribution to the region in which it is located is therefore the level of traffic and new

routes delivered to the region.

Section 33(e)

Section 33(e) refers to the Commission having "due regard" to "the level of income of the airport authority from airport charges at the airport and other revenue earned by the authority at the regulated airports or elsewhere".

This criterion clearly relates to the concept of the 'single till', an established basis for determining the level of airport charges. The rationale behind the single till principle is that airport charges should be kept as low as possible in order to increase passenger numbers. Increased passenger numbers, delivered by the airlines, lead to increased commercial revenues for the airport operator that are used in part to maintain low aeronautical charges.

Section 33(f)

Section 33(f) refers to the need for the Commission to have due regard to "operating and other costs incurred by the airport authority at the airport".

Ryanair submits that section 33(f) must be interpreted as reasonable costs incurred by the airport authority at the Regulated Airports only. The Airport Operator must not be allowed to take into account the costs of services within the airports that are used in Aer Rianta's non-core activities, e.g., consulting and architectural services used in the various duty free projects that Aer Rianta is involved in.

Section 33(g)

Section 33(g) refers to the need for the Commission to have due regard to "the level and quality of services offered at the airport by the airport authority and the reasonable interests of the users of these services".

Ryanair submits that this is an important criterion and should be given significant weighting by the Commission. The cost and quality of services and facilities must be reflected in the charges paid by a User. The current 'one-size-fits-all' approach clearly does not meet the requirements of individual Users.

Section 33(h)

Section 33(h) refers to the need for the Commission to have due regard to "the cost competitiveness and operational efficiency of airport services at the airport with respect to international practice".

Ryanair submits that this is an important criterion and should be afforded considerable weight. However, the Commission is again urged to have regard for the critical importance for low cost air access to Ireland and any comparators considered should reflect this. Therefore, comparators should be chosen not only with regard to international "best practice", but should also reflect the critical need to promote low cost access to the Regulated Airports.

Section 33(i)

Section 33(i) provides that the Commission shall have due regard to the need to impose "the minimum restrictions on the airport authority consistent with the functions of the Commission".

Ryanair submits that given the current chronic lack of competition, high costs, inefficient use of resources, and lack of adequate consultation at the Regulated Airports controlled by Aer Rianta, the maximum restrictions allowable under the Act should be applied. If, at some time in the future, the regulatory measures succeed in increasing Aer Rianta's efficiency, etc., and an effective degree of competition is introduced at these airports, the Commission may wish to re-evaluate the imposition of such restrictions.

Section 33(j)

Section 33(j) provides that the Commission shall have due regard to "such national and international obligations as are relevant to its functions."

Of particular relevance in this context, are the Commission's obligations under Articles 10 and 82 of the EC Treaty to ensure that the Commission does not adopt any measure that would enable the Airport Operator to abuse its dominant position. For example, a determination that enabled the Airport Operator to impose the same level of charges for different levels of services could potentially infringe Articles 10 and 82 of the EC Treaty.

In terms of national obligations, Ryanair submits that the Department of Public Enterprise's Shareholder Mandate to Aer Rianta, and in particular its reference to the lowest possible cost and development of traffic, are relevant to the Commission's functions.

6. QUESTIONS RAISED IN THE CONSULTATION PAPER

Question 1: Are there other types of framework that should be considered by the Commission in the regulation of airport charges?

The form of economic regulation adopted by the Commission must force the Airport Operator to reduce its costs and become more efficient. Ryanair submits that the Airport Operator is currently highly inefficient due in large part to its monopoly position, which provides it with no incentive to be efficient. Competition forces companies to reduce costs and increase efficiency. Below are observations on the possible approaches for the economic regulation of the Regulated Airports.

Rate of return regulation

If the regulatory framework aims at "emulating the market outcome" then the profitability of the Airport Operator should not be the determining criterion in the regulatory framework. As noted above sustainability of the Regulated Airports should be the focus of the regulatory framework as it more accurately "emulates the market outcome". The rate of return method also incentivises so-called

"gold-plating". Examples of gold-plating abound at the Regulated Airports in terms of the facilities and ancillary activities.

It is therefore submitted that rate of return regulation would not be an appropriate framework for the regulation of the Regulated Airports given Aer Rianta's tendency to develop costly and inefficient facilities, such as Pier C the 6-bay terminal extension, etc.

Incentive Regulation

As the Consultation Paper recognises at Section 2.2.2, incentive regulation attempts to incentivise a regulated company to reduce its costs and become more efficient. The inflation-based approach to economic regulation of airports has been in use at various airports for over a decade and the overall experience has been positive in terms of incentivising airports to improve their efficiency and lower their costs. This in turn has led to increased traffic growth and increased revenues from commercial activities.

The key focus of the regulatory scheme should be to incentivise traffic growth and route development at the Regulated Airports. This will be achieved where the Airport Operator is forced to reduce costs, increase efficiency and develop low cost, efficient facilities. However, Users should also be incentivised to increase traffic and develop new routes through lower charges which reflect the lower marginal costs of the Airport Operator in terms of increased "efficiencies".

There are, however, various problems associated with this approach. One is that the regulated entity will initially have a high cost base and charges due to the lack of competition. In Aer Rianta's case, its cost base and charges have increased substantially during the "regulatory vacuum". Ryanair therefore submits that the regulatory determination should be based upon the cost base that existed pre-1999.

A further problem identified in the Consultation Paper with this form of regulation is that it also incentivises a regulated company to reduce the level of its services in order to cut costs and maximise profits. This would be a significant problem at the Regulated Airports and particularly Dublin Airport where service levels are already quite low. This problem would need to be addressed by monitoring the level of services provided at the Regulated Airports (based on benchmarking of best practices at comparable airports) and the imposition of penalties where service levels are not maintained.

A problem, which is of major concern to a low fares airline such as Ryanair, is that a simple maximum price cap under the incentive approach would inevitably also become a price floor in that an airport operator would be loath to reduce charges for a user, even where a lesser quality of services and/or facilities was being provided to that user. This is already the case at the Regulated Airports where the Airport Operator has pursued a 'one-price-fits-all' policy under the guise of 'non-discrimination'. That is, Ryanair and other airlines operating out of the low cost Pier A facility and the old terminal are paying the same charges as those airlines operating out of superior facilities in Piers B and C and the new terminal extension, which were vastly more expensive to build and maintain and provide a premium level of service. Ryanair and other airlines are thus subsidising airlines using these higher cost, higher quality facilities.

In order to be effective, the regulatory framework should also include measures to monitor costs, revenues, profits and price cap compliance as well as quality of service. This should be complemented by transparency, which will provide both the Commission and the airport users with adequate information on the costs and other factors underlying the charges (e.g. benchmarking exercises published at regular intervals and available to interested parties).

Introduction of Competition

Ryanair submits that any regulatory framework must ensure the promotion of effective competition wherever possible. Even in the UK, where incentive regulation has been somewhat successful, there is a recognition in the current regulatory review that the introduction of competition at airports, in terms of competing terminals or gates, the provision of ancillary services, etc., is a crucial complement to economic regulation. As competition in the provision of airport facilities and ancillary services develops, regulation could be lightened. In this regard, the regulatory framework should aim to create a structure that simulates competitive behaviour in the short term but that provides for the introduction of competition wherever possible.

The Regulated Airport facilities are currently suffering artificial capacity constraints in certain areas as they are not being operated efficiently. A competitive environment would force the Airport Operator to become more efficient or risk losing market share to a competitor.

Question 2: What regulatory framework do you advocate for the economic regulation of airport charges?

As discussed in the response to Question 1 above, Ryanair advocates an incentive based regulatory framework that introduces a series of price caps based on a CPI - X formula. However, as noted above, Ryanair submits that the regulatory asset and cost bases to be considered in the Commission's determination should be those that preceded the Commission's appointment in 1999. That is, capex and increases in charges made during the period between the original appointment and the empowerment of the Commission should not be considered. Otherwise, the determination would be distorted due to the effective absence of regulation during that period.

For example, if a CPI - 10 formula is determined and one assumes that inflation is 0, then charges will be reduced by just 10% having previously (over past 18 months) been increased by ART by over 100%. In effect Aer Rianta will be allowed to retain 80% of the price increases they have imposed during the past 18 months and a high cost base will therefore be copper fastened at the Regulated Airports. It is imperative that the Commission carry out a root and branch review of Aer Rianta's costs in order to establish the true costs of the relevant facilities (e.g., the low cost A Pier or the old terminal excluding the new 6-Bay extension), before applying the CPI-X formula.

Question 3: What structure of pricing would be most effective in achieving allocative efficiency at Ireland's regulated airports?

Section 2.3 of the Consultation Paper refers to the structure of charges under the regulatory regime. The Commission refers to allocative efficiency, which requires that charges reflect the quality and cost of the facilities and services provided.

Differentiated Charges for Differentiated Services and Facilities

In the CAA's recent consultation paper regarding Pricing Structures in Economic Regulation (March 2001), the CAA discusses the

desirability of price differentiation at airports. The CAA notes that "airport charges cover a wide range of services and facilities with a corresponding range of incremental costs associated with them. A basic principle of efficiency is that prices should reflect these incremental costs.

This concept is very apt in relation to use of facilities at the Regulated Airports, where there is considerable differentiation between the quality and costs of facilities and services. However, despite this differentiation, Aer Rianta has applied a single charge. Ryanair submits that it is the cost and quality of the facility being used that should determine the charge for using such facility. For example, in Ryanair's case, it operates out of Pier A, the oldest and lowest quality of the three piers. The cost of Pier A facility is substantially less than that of the more modern and expensive Piers B and C. Similarly, Ryanair is operating out of the old terminal (i.e., excluding the 6-bay extension) and uses the old baggage hall as opposed to the new, underground facility and yet is paying the same charge as users of the new facilities.

The inferior quality and low cost nature of Pier A compared to Piers B and C is manifested in a number of ways, in addition to the sheer age of the facility: (i) a longer walk to and from the terminal for passengers; (ii) absence of air bridges, i.e., passengers are subjected to the elements when embarking and disembarking the aircraft; (iii) no air conditioning in the pier; (iv) excessive congestion in the pier - Pier A accounts for 50% of the throughput of Dublin Airport compared to 32% for Pier B and only 18% for Pier C; (v) no fixed electrical power available; and (vi) concession facilities are significantly inferior to those of Piers B and C.

In addition, Pier A cost approximately £5 million to build and refurbish whereas Pier C cost approximately £50 million to build. This clearly supports a differentiated pricing structure for the use of these facilities that takes into account the quality and cost of these facilities. Indeed, Aer Rianta partially recognised the inferior nature of Pier A through a £1.50 discount per departing passenger for airlines operating out of that pier. However, Aer Rianta removed this discount, along with other discount schemes in operation arguing variously that these discounts were being removed to compensate for Aer Rianta's loss of duty free revenues and/or that the European Commission forced them to remove these discounts. It should be noted that regulatory regimes in other jurisdictions reflect the relative cost and quality of facilities. For example, the airports operated by the British Airports Authority (BAA plc) offer discounts or rebates for the use of certain inferior facilities.

Therefore, the structure of pricing must reflect the quality and cost of the facilities provided in order to achieve the statutory objective of the operation of "cost-effective airports which meet the requirements of users".

Peak Pricing

Section 2.3 of the Consultation Paper suggests peak pricing as a possible structure for a charging mechanism. However, peak pricing would only be appropriate in a situation where the existence of peaks resulted in congestion to the point that demand exceeded supply. This is clearly not the case at Dublin Airport. Indeed, this notion of peak pricing is precisely the reason why Aer Rianta was pushing the Department of Public Enterprise to fully co-ordinate the airport after the terminal congestion problems of last summer. Clearly, a system of fixed slots would enable Aer Rianta to argue for higher prices in the peak, which would increase its profitability and make it more attractive to potential investors. However, as was explained by the airport users at great length to both Aer Rianta and the Department, in order for full co-ordination to be necessary it must be justified by congestion that cannot be solved in the short term by other means. This is not the case at Dublin Airport.

Indeed, the draft independent report commissioned by the Department of Public Enterprise for the purpose of determining whether Dublin Airport needs to be fully co-ordinated confirms that the congestion problems encountered at the airport during the summer of last year were largely due to the delayed construction works in the new terminal and that there was also evidence of mismanagement by the Airport Operator. The report concluded that there is no basis for introducing full co-ordination at this time. Indeed, the draft report confirms that the terminal has extensive over capacity (i.e., a capacity of over 20 million passengers per annum with a current throughput of only 14 million) due to the expansion of the terminal and that the runway capacity could be increased by at least 10% with better management. In addition, the current draft of the report does not take account of the existing parallel runway that could be used more extensively to remove some of the non-commercial and smaller commercial traffic from the main runway. This issue is discussed further in response to Question 23 below.

Thus, there is clearly no issue of congestion at Dublin Airport and therefore no justification for introducing peak pricing. Indeed, the introduction of peak pricing at an uncongested airport would have an adverse effect on the growth in traffic numbers as higher prices in the peak would not be reflective of demand. Prices overall must be lowered in order to reflect the considerable over capacity at the airport.

Incentivised Pricing

Any pricing structure should include a mechanism for incentivising the efficient use of airport facilities. Greater efficiency of use leads to increased capacity and lower cost. Greater efficiency in the use of facilities also reduces the need for investing in additional facilities and therefore capex costs. These reduced costs should be passed on to efficient Users in the form of lower charges.

In respect to Users with rapid turnarounds, these Users should not be subjected to the same charges as airlines with slower turnaround times. For example, Ryanair operates 25 minute turnarounds of its aircraft whereas most other airlines have turnaround times of approximately twice that. Faster turnarounds mean greater use of stands. Evidence of this is the fact that Pier A processes approximately 50% of the airport throughput, whereas Piers B and C combined process the remaining 50%. A pricing regime that incentivises this efficiency would lead to more efficient use of existing facilities and therefore lower costs and less pressure to build additional capacity.

In a similar vein, Ryanair contends that airlines who overnight aircraft here at Dublin because they are based there should not be obliged to pay overnight parking for occupying facilities that would otherwise go unused. There is no justification for overnight parking charges for passenger aircraft when there is little or no passenger traffic at Dublin Airport from 11.00 p.m. to 7.00 a.m.

In the United States, airlines lease or rent such facilities as passenger gates from the airport. Those airlines that use them intensively thereby reduce their per passenger cost. This is not evident in Ireland at the Regulated Airports. The termination of growth discounts by Aer Rianta and the flat fees discourage efficient use of facilities and discriminate against those carriers that use facilities more intensively.

Incentives should also be provided to Users for increases in incremental growth on existing routes and the establishment of new routes. Increased traffic leads to lower incremental costs for the Airport Operator, which should be reflected in terms of lower charges.

Question 4: In the context of any knowledge or experience that you may have in terms of the successes or failures of economic regulation of airports abroad, are there lessons to be applied in Ireland drawing on such international experience?

The Consultation Paper addresses a number of examples of economic regulation from various countries and the degrees of success or failure of those regimes. The bulk of Ryanair's experience with economic regulation of airports stems from the situation in Ireland, pre-Aviation Commission, and in the UK.

Ireland

With respect to the regulation of charges in Ireland pre-Commission, it was noted above that the Irish Government was charged with setting the level of airport charges under the Air Navigation and Transport Acts ("Air Navigation Acts"). This was last done in 1987, before the deregulation of the air transport sector in Europe. At that time, airfares were at oligopoly levels and airport charges were a relatively minor portion of those fares.

However, following deregulation, the Irish Government introduced a range of discounts that had the effect of drastically reducing the published charge and the results, as discussed above, were rapid expansion of traffic numbers and the introduction of many new routes. This approach was rather piecemeal at first until the Government formalised these schemes. The removal of these schemes by Aer Rianta, in the absence of effective regulation, has led to massive increases in the charges to operate at the Regulated Airports and has had a negative effect on the levels of traffic and the availability of services, particularly to Continental Europe.

The lesson from the former approach to regulation of charges in Ireland is that growth and new route incentives achieve the overriding goal of regulation, i.e., lower fares, increased traffic and new routes. Unfortunately, the former regime was unable to control Aer Rianta's monopolistic tendency towards inefficiency and high cost development. This was particularly apparent in the past 18 months (i.e., the "regulatory vacuum" period) during which prices to the airlines have been doubled, and high levels of capex have been committed to by Aer Rianta. This inefficiency and the massive capital costs Aer Rianta has incurred, against the express requirements of its users, has led to the current situation where Aer Rianta is arguing for even higher charges to cover their inflated capital costs. Ryanair submits that Aer Rianta must be tightly regulated in order to force it to be more efficient in terms of the use of existing facilities and to reduce its costs, both opex and capex.

Effective consultation was another issue not addressed under the former regime. There are numerous examples where Aer Rianta has either failed to consult with Users or where the consultation was meaningless as Users were not given adequate information or where the views of Users were not taken into account in reaching a decision. The issue of consultation is dealt with in the response to Question 39 below.

The UK

Under the Airports Act of 1986, the CAA has pursued an incentive based approach to the regulated airports in London (i.e., Heathrow, Gatwick and Stansted) and Manchester Airport. Before the CAA can set a price cap it must make a reference to the Competition Commission. The reference asks the Competition Commission to report on what the maximum limit on airport charges for the following period of five years should be, and whether, since the date of the previous reference, the airport has pursued a course of conduct contrary to the public interest. The CAA has to impose conditions on the airports if the Commission finds that an airport has been acting against the public interest.

There is no similar mechanism provided for in the Act to be applied in the Irish context. The challenge for the Commission will be to control activities of the Airport Operator that are contrary to the public interest, such as the failure to consult with Users, the development of unnecessary, costly and inefficient facilities, and the diversion of scarce capital into non-core hotel, overseas airports and duty free investments.

In the context of consultation, the Monopolies and Mergers Commission ("MMC") concluded in its Review in June 1996 that:

"In our view, consultation with airlines on a capital programme is essential, to enable the costs and benefits both of the overall strategy and of individual projects to be evaluated adequately and to assess whether airline requirements are being met."

In its current review of airport charges at the UK regulated airports, the CAA is also addressing the issue of introducing competition within airports in order to achieve the kinds of efficiencies that economic regulation has failed to do. In its Consultation Paper of February 2001 regarding the Competitive Provision of Infrastructure and Services Within Airports, the CAA reached some useful conclusions regarding the regulation of airport charges. The CAA does not have an express statutory duty to promote competition. Its obligation is to impose minimum restrictions and encourage commercial solutions generated by industry participants rather than imposing defined regulatory rules. In the introduction to its paper the CAA states that :

"It is widely accepted that economic regulation should not be implemented unless it is clear that a serious loss of economic efficiency would exist without regulation and where other solutions are not available. Therefore the CAA believes that it may be beneficial to investigate the potential for increasing the level of competition in the provision of facilities and services within airports with a view to reducing the degree of necessary regulation."

The Commission should introduce mechanisms into its initial regulatory framework to ensure that the Airport Operator does not continue to erect barriers to entry for companies wishing to introduce competition at the Regulated Airports, whether they are airlines or other service providers.

Question 5: What set of services provided by an airport operator should be considered to be financed from the five airport charges specified in the Act?

There are five specific "airport charges" identified in Section 2 of the Air Navigation Acts: (i) landing; (ii) taking off; (iii) parking of aircraft at an airport; (iv) passenger arrival or departure; and (v) cargo transportation at an airport.

Ryanair submits that all of the aeronautical services provided by the Airport Operator to its Users should be financed from these five charges. These should also include fees for check-in desks, an indispensable component of processing the departure of passengers, and therefore covered by the charges referred to under Section 2(b)(iv) of the Air Navigation Act. Other charges, such as the fuel levy, CUTE (although Ryanair will not use this service), Hold Baggage Screening (HBS), etc., must also be scrutinised by the Commission and form part of the determination on charges.

However, within these five categories, it is clear that there are numerous services that are used in common with all airlines, e.g., runway provision and maintenance, and other services that may or may not be used by certain airlines, e.g., air bridges, CUTE HBS, etc. Still others may depend on the facilities they pertain to, e.g., the number of security desks available, the availability of certain amenities, e.g., air conditioning, fixed electrical power, etc.

Thus, within those 5 categories, the charges imposed by the Airport Operator need to be clearly and transparently identified so that a bundle of services is not provided for a single charge. For example, Ryanair does not use, the new 6-bay extension, Pier C, CUTE or HBS, and these facilities/services should not be charged to Ryanair as part of a single, bundled charge.

Question 6: How should the costs of other airport services be paid for?

The possibility of the "user pays" principle should be considered for certain services in addition to those services normally provided by the Airport Operator, e.g., business lounges, fast track services, etc. These kinds of premium services should be paid for by the airlines using them.

Question 7: What are the advantages and disadvantages of regulating a number of airports on an aggregate basis?

Ryanair recognises that this issue may be politically sensitive in that it deals with the viability of Cork and Shannon airports. Regulating these airports in the aggregate or separately from Dublin Airport may affect this viability. However, it is submitted that if a strict economic approach is to be taken, each airport should be regulated separately as they have very different needs and characteristics and no rebalancing should be permitted between the airports. Although Ryanair cannot make an informed judgement on this issue due to a lack of adequate information on costs at these airports, it is likely that separate regulation of these airports would inevitably lead to a reduction in the charges at each airport but with a larger reduction occurring at Dublin Airport because of greater traffic volumes and resulting "efficiencies".

Perhaps the major difficulty with regulating Cork and Shannon separately, is that Aer Rianta has over-invested at these airports and the level of capex is therefore seriously inflated. For example, in 1999 alone, Aer Rianta invested approximately £95 million at Shannon, during a year when traffic at Shannon was negatively impacted by the successive withdrawals of AB Airlines, Pakistan International, and later Virgin Express. The imminent establishment of an Open Skies regime between the EU and US will further impact negatively on traffic volumes and this airport. Nevertheless, an individual price cap for these airports would force Aer Rianta to make these airports independently efficient leading to lower costs, thereby attracting increased traffic volumes, increased revenues, etc. Furthermore, no rebalancing should be permitted between the Regulated Airports.

In the event that the Regulated Airports are regulated in the aggregate, a mechanism for ensuring that Cork and Shannon are developed as efficient, low-cost facilities, would have to be introduced in order to ensure growth of traffic and new routes out of these airports.

Question 8: Should Dublin, Cork and Shannon airports be regulated separately or on an aggregate basis?

As discussed in response to question 7, the Regulated Airports should be regulated separately.

Question 9: Should the maximum charges set by the Commission apply to individual charges, to a basket of charges or to the total of charges?

As noted above in the response to Question 5, there are certain services that are common to all users and that could therefore have a common cap. This cap would need to be based on benchmarked charges for providing similar services at an efficient airport or airports. Other services would need to be capped individually because they are not used by all airlines and therefore cannot be bundled into a single category of charges, e.g., air bridges, CUTE, HBS, etc.

Finally, charges for a further category of services should be linked to the facility to which they relate. For example, charges for the use of a particular pier and the related services at that pier should be capped in accordance with the cost and quality of that pier. Thus, the charge for operating out of Pier A or an eventual low cost facility (in the form of Pier D or otherwise) should accurately reflect the cost and quality of that facility.

Question 10: If more than one limit, on which categories of charges?

See response to Question 9 above.

Question 11: How should the determination on maximum airport charges be expressed having regard to the options contained in Section 32(6) of the Act.

Section 32(6) of the Act provides various alternatives for the expression of the price cap mechanism to be used in the Commission determination. Consistent with Ryanair's proposals set forth in response to Questions 5 and 9 above, Ryanair submits that the Commission's determination should provide for a combination of limits on airport charges based on whether those charges are common charges, individual charges, or charges linked to the facilities used. The charging mechanism should also provide incentives for efficient users and growth of traffic and new routes.

Costs at the Regulated Airports should be benchmarked against efficient comparators to ensure that the starting point for the determination is the lowest actual cost. The cap in each case should be based on a CPI - X formula, with the X component being sufficiently high to achieve the necessary level of cost efficiency.

Question 12: Are there any alternative ways by which the contribution of each of the factors specified in Section 33 to the achievement

of the statutory objective may be assessed?

Please see the observations made on the statutory background set out at Section 3 above.

The Commission has identified the two elements in Section 33 of the Act, i.e., to facilitate the development and operation of cost-effective airports which meet the requirements of users. Ryanair submits that the statutory objective could be achieved by:

- 1) promoting transparency of airport costs and the development of facilities; and
- 2) identifying and fulfilling the requirements of users through effective consultation and consensus;
- 3) Promoting traffic and new route growth at the Regulated Airports.

Question 13: How should an airport operator relate capex decisions to current and perspective user needs? How should the Commission assess the degree to which the operator is doing so successfully?

Section 4.5.1 of the Consultation Paper rightly recognises that economic regulation must seek to avoid excessive or excessively early investments that have to be paid for through airport charges. Ryanair submits that all capex decisions must be subject to consultation and consensus between the Airport Operator and the Users, whether they relate to current or perspective needs.

Ryanair is aware that the interests of airport operators and users may differ in terms of the relative horizon of decisions on capital investments. Airport operators have a longer term outlook as new facilities, particularly runways and terminals, have long lead times. Airlines, on the other hand, would prefer to defer the cost of new facilities for as long as possible. However, it is necessary, through an effective consultation process, for an airport operator and its users to achieve a consensus on the necessity, timing and cost of capex. It is not acceptable for a monopoly airport operator to dictate the need and cost of capex, when these decisions directly affect the users and the costs are ultimately borne by those users.

There is an urgent need for regulatory oversight at the present time given the current status of the 20-year development plan. Section 4.5.1 of the Consultation Paper recognises the importance of carefully scrutinising a regulated firm's investment plans as to their timing and efficiency. Ryanair is of the view that the Airport Operator has made certain important decisions with respect to major developments without due regard to the Users' current or prospective needs. At a recent meeting with (one of) Aer Rianta's consultants, PB Aviation, Ryanair and other Users questioned the accuracy of the Aer Rianta's growth forecasts and other Users noted that Airport Operator had not consulted the Users on their future traffic plans. These forecasts are crucial for determining whether and at what time capex is necessary and yet the Airport Operator did not properly consult with the Users in preparing these forecasts.

The Commission should scrutinise the degree to which the Airport Operator is successfully relating capex decisions to current and perspective User needs by the degree to which consensus has been achieved between the Airport Operator and the Users.

Question 14: How should capex be funded? Should one of the five regulated charges be ear-marked for investment spending or, instead should the revenue from charges be pooled (perhaps along with other incomes allowed from under the Act) to fund both opex (operating expenditure) and capex?

Ryanair submits that, in the short-term capex and debt repayments should be funded through the disposal of Aer Rianta's significant non-core assets/interests (i.e., Aer Rianta International, Great Southern Hotels, and other airports outside of Ireland). The disposal of such assets would be sufficient to fund substantially all of the necessary current and prospective capex requirements.

Ongoing capex and opex requirements, agreed between the Airport Operator and the Users, should be funded from a pool of the five regulated charges, along with the revenues from the other activities included in the single till (discussed further in the response to Question 27 below). Capex should also be financed through the sale or lease of property for the construction of competing facilities. Other alternatives are public/private partnerships and third party financing of facilities.

Question 15: When should investments be included in the assets on which a reasonable return is applied in the calculation of airport charges - before construction of the new facility commences, once the investment is in progress, or only once it is in use.

Having due regard to Section 33(b) of the Act, it is submitted that the rate of return on capital must be reasonable in the light of the anticipated lifetime of assets, therefore one would anticipate that, on an annual basis, there should be a relatively low rate of return.

Any investments should only be included in the regulated asset base ("RAB") on which a reasonable rate of return is applied in the calculation of airport charges only once such asset is in use. This would avoid a "Terminal 5 situation" occurring, whereby users are pre-funding a capital cost that never occurs or is interminably delayed, as at Heathrow Airport.

Question 16: What assets should be included in the regulatory base?

Ryanair submits that all assets necessary for providing aeronautical services at the Regulated Airports and also those necessary for achieving the commercial revenues included in the single till (see response to Question 27) should be included in the RAB. A separate RAB should be calculated for each of the Regulated Airports. These assets should be valued at net book value (i.e., historical cost less accumulated depreciation).

Question 17: On what basis should those airport assets that are used to provide airport services and other services at Irish airports be valued?

See response to Question 16 above.

Question 18: How should the rate of return of the airport operator be defined and measured?

As noted at Section 4.5.2 of the Consultation Paper, the rate of return earned on capital investment is, effectively, an element of the cost of operating an airport. Therefore, the higher the rate of return permitted, the higher will be the airport charges. The Consultation Paper also recognises that over the medium term, unless the rate of return matches the cost of capital, the Airport Operator would be unable to replace its stock of assets, thereby jeopardising the sustainability of future operations.

Ryanair submits that the Commission should base its determination on the sustainability of the Regulated Airports as opposed to their profitability and the Airport Operator's rate of return should therefore be equal to its cost of capital. This reflects the criterion in Section 33(b) of sustainability and the principle that the Regulated Airports constitute essential infrastructure for air access to Ireland.

Question 19: How should the cost of capital of the airport operator be calculated?

See response to Question 20 below.

Question 20: Has the capital asset pricing model a role to play in estimating the cost of capital given that the equity of the company is not publicly traded? What firms or industries in Ireland or elsewhere have similar risk profiles to the airport operator and could therefore be used as benchmarks to determine the value of beta in the CAPM?

Yes. The Capital Asset Pricing Model is used to calculate to the level of risk - and required rate of return - of an investment versus a "risk free" investment (certain government bonds). The risk premium on the market utilised in the CAPM is the expected difference in returns between the risk free rate and other equity investments. The potential risk (or the Beta) of an investment is measured by the effect that a change in the aggregate value of all assets in the economy (or market) can have on the value of the investment.

Because the same risk analysis is required on both public and private equity investments (as they are both affected by changes in the stock markets and aggregate economy), the CAPM applies to both public and private cost of capital analyses. The CAPM is generally used to estimate the cost of equity and the required/anticipated rate of return on public and private investments.

The best comparables are companies with similar operations and risk profiles. The most appropriate comparables to Aer Rianta are other international airport operators. Ryanair has examined several comparables to estimate the appropriate cost of equity for Aer Rianta. The cost of debt used to estimate Aer Rianta's Weighted Average Cost of Capital is simply Aer Rianta's current (not historical) cost of debt (i.e., the rate that they would currently have to pay on borrowed capital).

Please see Annex 4 for a Cost of Capital Analysis prepared for Ryanair by Morgan Stanley Dean Witter. The weighted average cost of capital for other comparable airports is approximately 6.4%. However, this rate of recovery should only be applied to the net book value (historical cost less accumulated depreciation) of the assets, and should specifically exclude the recent profligate capex that occurred during the "regulatory vacuum". This latter capex should be financed entirely through the sale of Aer Rianta's non-core investments in Great Southern Hotels, overseas airports and duty free activities, all of which were originally funded by the diversion of scarce capital generated at the Regulated Airports.

Question 21: What rate of return should the airport company be allowed to earn relative to its cost of capital?

The true purpose of calculating the cost of capital is to establish the expected rate of return (this is also why it is used to discount cash flows when valuing a business). For government entities, (i) the rate of return should be high enough so that the business is self-sufficient and sustainable; and (ii) it is generally accepted that the rate of return should not exceed the cost of capital.

Therefore, Ryanair submits that the Commission should use a rate of return equal to the cost of capital in its determination.

Question 22: How should the efficiency and effectiveness of resource use by the airport authority be assessed?

Having regard to the language in Section 33(h) of the Act, the assessment of efficiency and effectiveness of resource use by the airport authority should be assessed with respect to international (best) practice. At its heart, the efficiency and effectiveness of any airport can best be determined by the extent to which it stimulates traffic and new route growth, because this would be the inevitable by-product of a truly competitive regime, were one to exist at the Regulated Airports. As noted above, the Airport Operator's efficiency and effectiveness are severely lacking due of the lack of competitive forces to discipline them. Market forces tend to increase the efficiency and effectiveness of companies, thus reducing costs.

Ryanair submits that Aer Rianta is inefficient and ineffective in its use of resources in two broad areas, (i) in its development and management of its fixed assets and costs; and (ii) in its management of its variable assets and costs.

Fixed Assets and Costs

With regard to its fixed assets and costs, the Airport Operator, because of the lack of consultation with its users, tends to develop inefficient, over-specified and costly facilities and manages them ineffectively. Examples of this include the recent 6-bay terminal extension, and Pier C, where Ryanair understands that there were significant cost overruns, although Aer Rianta has not provided Users with details of such overruns. It is noteworthy that both Aer Lingus and Ryanair, the two principal users of Dublin Airport have both refused to move into or use any of the facilities of the new 6-bay extension. The extension was also seriously delayed and caused severe congestion in the terminal last summer. Once Users began to move into the extension, there were significant problems with the CUTE System and the new baggage hall, which Aer Rianta was slow to address.

These kinds of inefficiency and ineffectiveness could be partially addressed by a severe price cap mechanism. The Airport Operator should also be forced to sell off those non-core, fixed assets that are not achieving a sufficient rate of return and are therefore draining resources from the core activities. However, Ryanair submits that the only effective way to address these problems is to force the Airport Operator to consult properly with its Users and to require a consensus on each development. The Airport Operator should also be required to outsource these kinds of development projects to minimise the risk of cost and time overruns and to ensure that these developments are undertaken on a competitive basis and that any problems arising during or after the completion of such projects are properly dealt with in a timely manner.

Variable Assets and Costs

Ryanair submits that Aer Rianta is an inefficient and ineffective provider of a number of ancillary services, such as car parking, security, cleaning, catering and other services that could be feasibly outsourced to private operators. In essence, these services constitute "little monopolies within the greater monopoly", as they are not exposed to competition, and therefore entail all of the inefficiencies associated with a monopoly provider. For example, Aer Rianta has constructed a "multi-story" car park that is just two stories high. Furthermore, Aer Rianta is substantially overstaffed in all of the areas where it provides ancillary services. In this respect,

it would be interesting for the Commission to query Aer Rianta on the number of staff cuts resulting from the loss of duty free. Indeed, Ryanair has questioned Aer Rianta on the cost saving measures that it has undertaken as a result of the loss of this substantial revenue source. Aer Rianta has been unable to produce any concrete cost savings that have resulted from its so-called "Compact Scheme".

Furthermore, Aer Rianta is highly inefficient in its use of consultants. As a recent example, Aer Rianta hired the consulting firm, PB Aviation, to "consult" with Users on the 20-year development plan for the airport, despite the fact that Aer Rianta has its own team of developers and architects. This leads to expensive duplication for which the Users ultimately pay. It also points to Aer Rianta's inability to consult directly with its Users.

Ryanair submits that a severe price cap mechanism would force Aer Rianta to outsource many of the ancillary activities it is currently engaged in order to introduce efficiency and effectiveness in the use of resources and to substantially reduce costs.

Question 23: At the overall level, relative to comparable airports or businesses, is there evidence of either ineffective use of resources by the Irish airport operator?

Yes. As noted in the response to Question 22 above, there is clear evidence of both inefficient and ineffective use of resources by Aer Rianta relative to comparable airports. Indeed, the recent SH&E draft report confirms that runway utilisation on the main runway at Dublin (10/28) is at least 10% below capacity (i.e., could be increased from 40 movements per hour to 44 movements per hour). Proper management, provision of additional rapid exit taxiways ('RETs') and movement of smaller aircraft onto the short parallel runway 11/29 would further increase the utilisation of the main runway. London Gatwick, for example, has only one main runway and achieves a capacity of 48 movements per hour, handling 30 million passengers per annum. Dublin Airport, on the other hand, has a current declared capacity of only 40 movements per hour and handles only 14 million passengers per annum.

Moreover, Stansted Airport is currently consulting on the next development phase for that airport, i.e., taking the airport from 15 million passengers per annum to 25 million per annum. However, instead of planning to build another runway, Stansted has devised plans to develop its existing runway to achieve 50 movements per hour. The BAA has indicated that it does not intend to develop outside the existing airport boundary and is not proposing any additional runway provision. (See attached slides from a BAA consultation presentation at Annex 5). Again, it should be emphasised that neither Gatwick nor Stansted have an existing short parallel runway that could be used to divert non-commercial and small commercial traffic away from the main runway, thereby further enhancing runway capacity.

The SH&E draft report also noted a lack of efficient organisation by the Airport Operator in the summer of 2000, which meant that passengers had to endure a poor quality of product in the airport. The draft report noted "consistent anecdotal evidence of insufficient staff on security and passport control, ineffective or misleading flight information displays and access to the airside being closed to early morning charter departures."

In addition, Piers B and C at Dublin Airport are clearly underutilised given that both piers combined only account for 50% of the airport throughput with the other 50% being handled by Pier A.

Question 24: In the event that Irish airport charges change, does efficiency and effectiveness and the use of all of the airport operator's resources require that change to be phased in over the period of the control or implemented in full at the beginning of that period?

Ryanair submits that a severe price cap mechanism must be imposed on the Airport Operator as soon as permissible under the Act. Section 32(5)(b) of the Act states that "the determination shall come into operation not later than 30 days after the making of such determination."

By imposing a severe price cap mechanism, the Commission will ensure that Airport Operator is forced to re-evaluate its inefficient and ineffective practices. This re-evaluation should include, (i) the disposal of all non-core activities, particularly those activities that are not achieving an adequate rate of return and are therefore acting as a drag on the core activities, e.g., the Great Southern Hotels; (ii) initiating a proper consultation process between the Airport Operator and its Users in order to reach a consensus on the appropriate development of the Regulated Airports; (iii) negotiate with users interested in entering into financing arrangements for the construction of cost efficient facilities that would facilitate the needs of the Users and would lessen the risk of such development for the Airport Operator; and (iv) immediately put out for tender all ancillary services at the Regulated Airports.

Otherwise, the Commission will not be successful in achieving its objective of "facilitating the development of cost-effective airports which meet the requirements of users."

Question 25: How should the contribution of the airports to the regions in which they are located be assessed?

The contribution of the airports to the regions in which they are located should be assessed in terms of the traffic and new route growth delivered each year at those airports. It is accepted that the multiplier effect exerted by the growth in air transport services is both immediate and significant in the immediate region of an airport. The air transport industry exerts a strong multiplier effect on the Irish economy as a whole and particularly the tourist industry.

The importance of the Irish tourist industry as a driver of national economic growth is recognised in the Government's Development Plan for 2000-2006. In recent years, the industry has demonstrated a significant contribution to wealth creation, sustainable employment and regional development. In 1998, total spending by tourists was just over £3 billion and contributed between 5 and 6% to the total national output of the economy. This spending has contributed both directly and indirectly to the growth of a range of sectors right across the economy, from the food and drinks sectors to the construction sector through the investment in new hotels and other tourism facilities.

Low cost access by air to Ireland from the UK and Europe has been the single most important factor behind the growth in tourism and therefore the level of tourism spend over the last 15 years. The Bord Failte Tourism facts brochure for 1997 states that the average spend per head for a visitor to Ireland was £420 (now probably significantly higher). For every £1 spent by out-of-state visitors, £0.57 accrued to the exchequer, and every additional million of expenditure by visitors supported an additional 51 jobs.

In 1999 and again in 2000, Ryanair submitted proposals to the Minister for Public Enterprise and Aer Rianta for the development of low fare services from Dublin and Shannon Airports that would have directly created over 250 jobs, opened 10 new routes direct from Dublin and Shannon to the UK and Continental Europe, delivering approximately 2 million passengers additional passengers per annum to/from Dublin and Shannon within three years of the commencement of these services. This proposal would have required an investment of £250 million by Ryanair in the Irish tourism industry and in particular in the Mid-West economy. The proposal was contingent upon a low cost deal at both Dublin and Shannon airports and has been rejected on both occasions. This traffic growth has therefore been lost by Ireland and went instead to the UK (primarily in the form of new routes from Stansted and Prestwick to Europe) and more recently to Brussels, Charleroi, where Ryanair has established its first Continental base.

Ryanair submits that low fares access to Ireland has been a major contributing factor to the economic boom experienced in Ireland in the past ten years. Low fares lead to high traffic volumes which in turn lead to higher tourism growth, feeding the multiplier effect and sustaining countless businesses and economic activity in the regions and the Irish economy as a whole.

Question 26: What is the contribution of the airports to the regions in which they are located?

The primary contribution of the airports to the regions in which they are located should be growth in passengers and new routes and all of the associated benefits described in response to Question 25 above.

Question 27: Should airport users obtain any financial benefit from other income that the airport company derives from airport activities? In other words, should airport regulation be based on a single or a dual till principle?

As noted above in the Section on the Regulatory Background, the 'single till' approach has been widespread custom in international airport regulation. The distinct characteristic of the approach is that it takes account of the costs and revenues of both aeronautical and commercial activities of an airport when determining the price cap for the airport charges. Lower airport charges lead to increased passenger numbers and any shortfall in revenues to the Airport Operator from aeronautical charges would be recouped from increased commercial revenues. Part of the rationale behind this approach is that an airport only receives the benefit from the commercial side of their business because airline passengers are using the facilities, and it is therefore reasonable that profits made on the commercial side be used to reduce aeronautical charges. It is a symbiotic relationship through which both the airport operator and the users benefit.

This was, loosely, the method of regulation in Ireland prior to the empowerment of the Commission. The revenues from Aer Rianta's commercial activities, particularly its duty and tax free sales, were used to "reduce" airport charges through various discounts that dramatically increased passenger growth and increased Aer Rianta's revenues from aeronautical income and commercial activities. In 1998, with the impending loss of duty free sales, Aer Rianta argued to the Minister that these discounts should be removed due to the loss of revenues from such sales. Aer Rianta argued that it would lose approximately £30 million in duty free revenues (although no evidence of any such losses has ever been provided despite repeated requests by Users) and that these "losses" had to be compensated by removing the discount schemes.

However, a number of points should be noted here, (i) Aer Rianta had eight years notice that duty would be abolished and yet made no contingency plans or took any cost-cutting measures in preparation for this loss; (ii) the airlines also lost substantial revenues from the loss of duty free sales on board and yet did not pass on these losses to their customers; (iii) as noted above in reference to other ancillary services, Aer Rianta should not be involved in such commercial activities and should, in common with other airports, be sub-contracting these activities to commercial companies who would better develop the commercial side of the airport, whilst remitting rent/concession fees to Aer Rianta. Aer Rianta should only provide suitable space for such activities. In this vein, it should be noted that Aer Rianta has yet to open the substantial commercial space available in the 6-bay extension and is thus failing to utilise this important space.

If Aer Rianta was forced to sub-contract its commercial activities to competitive operators, the rents and concession fees from those activities due to Aer Rianta would substantially increase. Increases in passenger numbers would again boost these revenues, which would justify decreasing the airport charges further.

The single till concept has recently come under some debate in the CAA's price review in the UK when applied to congested airports where passenger numbers cannot be increased and no further benefit from reducing the aeronautical charges can be gained. However, this is clearly not a factor for the Commission's determination as none of the Regulated Airports is capacity constrained.

Ryanair submits that the Commission should therefore apply the single till approach to determining the airport charges.

Question 28: If a single till principle is to be used, what other revenue should be included in it and how should the airport charges relate to them?

A single till approach should include all revenues from any activity at the relevant Regulated Airport, both aeronautical and commercial. This would include revenues that Aer Rianta derives from both aeronautical charges; its own commercial activities at the Airports; revenues from leased premises to commercial operators; concession fees from such commercial operators; parking fees, etc.

Question 29: How should the cost effectiveness of Irish airports be assessed?

Having regard to the language of Section 33(h) of the Act, cost effectiveness must be assessed by benchmarking Aer Rianta's practices against the best practices of comparable international airports, that have a similar emphasis on low cost access. This would include many of the UK airports, which have recognised the importance of offering low cost access in order to develop traffic and new routes.

In any event, as discussed above in response to Question 22 above, it is clear on its face that Aer Rianta is not cost efficient, either in respect of their fixed or variable costs. This is due to the chronic lack of competition or effective regulation that is necessary to force an undertaking to be cost effective.

A further measure of the cost effectiveness of an airport is its ability to attract airlines to operate at that airport and to stimulate passenger and route growth. This has increasingly not been the case at the Regulated Airports in the past three years following Aer Rianta's removal of the discount schemes. Passenger numbers on traditionally the strongest routes between Ireland and the UK have begun to stagnate, particularly last year, at a time when Sterling was at an all time high and one would have expected strong inward

traffic as a result. Indeed, if one excludes the strong continuing growth in outbound holiday traffic from Ireland (which figures account for almost all of the Continental European traffic growth in recent years) it is apparent that the significant cost increases imposed by Aer Rianta over the last two years has led to the stagnation of inbound traffic and tourism at the Regulated Airports.

In order to be effective, a regulatory framework must force the Airport Operator to become more cost efficient by controlling its fixed costs through efficient development and planning, following consultation and consensus with its Users, and by outsourcing ancillary services to reduce its variable costs.

Question 30: What costs of operating an airport are joint costs? How should such joint costs be allocated among users?

This Question has been addressed in the response to Question 3 above on the structure of pricing. Ryanair has identified certain costs for services that are common to all users and could therefore be treated under a common cap. This cap should be set with reference to benchmarked costs at comparable, efficient airports.

Question 31: Should some of the costs of operating an airport be recovered directly from passengers?

Ryanair submits that none of the costs associated with operating an airport should be recovered directly from passengers. It is clear that when a passenger contracts with an airline for passage, the expectation is that the fare covers all of the services involved in getting the passenger from door-to-door within the originating and destination airports.

Question 32: How should the Commission seek to prevent a price maximum being evaded by a lessening of service quality? What incentives could an airport operator be given to provide appropriate service quality?

Having regard to Section 33(g) of the Act, it is submitted that the Commission has jurisdiction to introduce a measure for service quality monitoring. This should involve a process of continuous monitoring, and consultation with the Users. Ryanair also believes that the Commission should play an active role the preparation and publication of ongoing service standard surveys at the Regulated Airports.

A recent example of where the Airport Operator failed to provide an adequate quality of service was its handling of the snow conditions on 27 February 2001 and the following days. Although the weather conditions were relatively severe, Aer Rianta failed to take adequate steps to ensure that the airport remained opened the day of the snow. All users had to cancel all of their flights as the airport remained closed throughout the day. Moreover, flights were seriously disrupted the following day as Aer Rianta failed to take adequate measures to remove snow and ice from the aprons and taxiways. Because there is no penalty against Aer Rianta for such incidents, there is no guarantee that the same situation will not occur in the future.

Therefore, the regulatory regime should provide for some form of penalty or reduction in charges to compensate Users when the Airport Operator fails to maintain the required level of service. This would also provide a mechanism for preventing Aer Rianta from circumventing the effect of the price cap by diminishing service levels.

Question 33: How should the international cost competitiveness of Irish airports be assessed?

Low fare airlines have a requirement for fewer facilities than full service carriers and the trade-off is lower costs. Such an environment does not currently exist at the Regulated Airports. The low fare traffic (and other competing traffic) is stagnating, airfares are rising and no other low fare operator has begun offering services at Dublin Airport.

This is in stark contrast with many of the UK airports, including Stansted, Liverpool, Luton and Prestwick, where more competitive cost regimes have been fostered and emphasis on providing facilities that promote the development of traffic and new route growth, particularly by low fares airlines. Low fares traffic is growing by 25% > 30% per annum at these UK airports, whereas such traffic at the Regulated Airports is stagnant due to high costs and inefficient facilities. Three of the four low fare carriers are now operating from Stansted. Similar double-digit growth in low fares traffic is also occurring at other UK airports. This clearly indicates that the Regulated Airports are not cost competitive and lack the kinds of efficient facilities necessary to sustain low fare traffic growth. The incumbent and only low fare carrier at Dublin (Ryanair) has transferred all of its growth since 1997 to other airports (Prestwick, Luton, Brussels, Stansted), which are cost competitive. It is against this backdrop of stagnating growth particularly in the fastest growing but most cost sensitive sector of the airline market that the cost competitiveness of the Irish airports should be assessed.

Question 34: Does bench-marking have a role to play in evaluating the efficiency of Irish airports? If so, against which entities should Irish airport efficiency be bench-marked?

Bench-marking is a useful tool that can be used to evaluate the efficiency of a regulated airport. It can be difficult for a regulator to set maximum prices based on that regulated firm's accounting costs because the regulator may not have reliable information on the ability of the firm to make cost efficiencies or to make efficient investment decisions. Such information may come from the users of that firm's services, in this case the airlines. Based on responses to previous questions, there is clear evidence of inefficiency at the Regulated Airports that could be evaluated by reference to international comparators.

However, it is clear that such benchmarking should use comparators that adequately reflect the importance of low cost access. Thus, while it is true that Ryanair primarily operates to secondary airports, it also operates to Gatwick, Manchester, Liverpool, and Stansted airports, among others, that cater to both low fares carriers and flag carriers and would therefore be useful comparators to Regulated Airports. Equally, some of the secondary airports at which Ryanair operates, such as Prestwick, Charleroi, Hahn, Beauvais, could also be used as valid comparators for the Regulated Airports.

Best practice at such airports should be used to benchmark efficiency at the Regulated Airports. For example, runway usage at Gatwick and Stansted should be the benchmark for efficient runway utilisation at Dublin. Terminal efficiency at these airports should also be examined as possible benchmarks. Some of the smaller Continental airports, such as Beauvais and Charleroi, have operating efficiencies whereby airport staff are trained and used for a number of operational purposes, which increases efficiencies and minimises costs.

The BAA airports have also been very successful in recovering from the loss of duty free. These airports outsourced their commercial activities (and many of their ancillary activities) and have been very successful in attracting brand names to retail at their airports.

This could be used to benchmark Aer Rianta's commercial and ancillary activities.

Question 35: Are there any difficulties associated with reliance on international comparisons?

Undoubtedly there are difficulties associated with reliance on international comparisons. The process can be somewhat time and data intensive. This is why benchmarking should be used as a tool for the Commission to examine practices at other comparable airports while recognising the complexity of airport operations. A broad view of a variety of airports that have certain similar characteristics to the Regulated Airports will provide a reasonable indication of whether the Regulated Airports are efficient and what steps need to be taken in order to achieve greater efficiency. The comparison should also take into consideration the current and future profile of the passenger and user mix at both the Regulated Airport in question and the comparison airport.

Question 36: Is it appropriate to minimise regulatory restrictions according to the extent of competition faced by an airport operator or airport service provider?

Regulation should simulate and wherever possible introduce competition at the Regulated Airports. As competition develops, a light-handed approach to regulation may be more appropriate. However, it is clear that there is a critical lack of competition at the Regulated Airports, particularly Dublin Airport where there is no competition in the form of regional or secondary airports. Cork and Shannon airports may experience limited competition from Kerry and Galway/Knock airports, respectively.

Ryanair submits that the initial regulatory approach should be very tight to reflect the current inefficiencies and lack of competition at the Regulated Airports, and the 100% price increases which were imposed at the Regulated Airports over the past 18 months. If the Airport Operator is successful in reorganising its operations to achieve efficiencies and introduce competition in the provision of facilities and services, then the Commission may wish to review this issue in a subsequent five-year determination. Equally, even if this initial regulatory approach proves to be overly tough on the Airport Operator, the benefits will nevertheless flow to Users, consumers, tourism and the surrounding regions, which is a preferable short-term outcome.

Question 37: Which airport services, if any, of the regulated airports are exposed to competition? Are there services for which airports possess market power? Are there services for the degree of competition faced by suppliers might be increased?

The following airport services are exposed to some form of competition:

- ground handling services have been liberalised by the EC Directive on Access to the Groundhandling Market. Groundhandling fees were found to be three to four times higher in Europe when compared to the US. This prompted the European Commission to take steps to liberalise this important market. However, Aer Rianta has used the introduction of groundhandling liberalisation to introduce new and increased fees. Thus, competition in this area has been hampered and rendered ineffective by the Airport Operator's imposition of these additional and unjustifiable fees.
- Catering and fuelling services are open to a degree of competition at Shannon Airport. Catering services are offered by Aer Rianta and Aer Lingus and fuelling services by Aer Rianta in competition with Esso. However, in both cases Aer Rianta imposes levies on the provision of such services and competitors have complained that this gives Aer Rianta an unfair competitive advantage. Therefore, the degree of competition in these areas has been rendered ineffective by the imposition of these levies.

As discussed in previous responses, Aer Rianta is a monopoly provider of most of the other services associated with the operation of the Regulated Airports. Because these services are not subject to any competition, the Airport Operator therefore possesses market power for the provision of all of these services. Ryanair submits that these services should be opened up to competition in order to increase efficiency and reduce costs.

Competition should also be introduced in the provision of terminal services, eventually in the form of a competing terminal. In the short-term, the provision of facilities should be done on a competitive basis and users should be allowed to fund and construct facilities such as piers and aprons that meet their operational and cost needs.

Question 38: Are current airport services and the associated prices satisfactory to airport users? Is the present combination of services and prices such as to warrant some form of performance measurement as a condition of a determination of airport charges?

Current airport facilities/services and the associated prices are clearly not satisfactory, particularly to a low fares operator such as Ryanair. Despite the fact that Ryanair is the original European low fares airline and began its operations out of Dublin Airport over 15 years ago and is currently the second largest user at Dublin Airport, Aer Rianta has consistently failed to meet Ryanair's requirements for low cost, efficient facilities with the result that all of Ryanair's growth since 1997 has been away from the Regulated Airports. Equally, Aer Rianta's failure to provide satisfactory prices and services has resulted in the withdrawal of AB Airlines, Virgin Express and CityJet, among others, during this period, and accounts for Aer Rianta's failure to attract any other low fares airlines to the Regulated Airports.

It is clear that Aer Rianta is aware of the needs of low fares operators but refuses to acknowledge the crucial importance of this sector for ensuring low cost access to Ireland. Indeed, at a recent conference on the Low Fares Sector held in Amsterdam, Tom Haughey, Aer Rianta's Director of Marketing Development & Strategy, gave a presentation entitled "A New Age For Europe: The Impact of Low Cost Airlines on European Airport Operations" and spoke of "Bridging the Gap Between High Cost Airports and Low Fares Airlines". Mr. Haughey concisely described the needs of low fares airlines in his presentation (see the slide entitled "Airport Facilities" of the attached presentation at Annex 6).

Only through tight regulation and the gradual introduction of competition will the services and facilities provided by the Airport Operator adequately reflect the level of airport charges.

Question 39: Is the current extent of industry consultation about airport services, prices and related matters satisfactory? In particular, are the arrangements for consultations and negotiations such as to suggest that in some areas agreement could be reached by those involved without recourse to regulation?

Ryanair submits that the current extent of industry consultation about airport services, prices and related matters is far from

satisfactory. Consultation is a crucial element to ensuring successful regulation. Many of the problems with inadequate and inefficient services and facilities addressed in this submission relate directly to the chronic lack of real consultation and consensus between the Airport Operator and the Users. This was evidenced by a unanimous vote of no confidence by the Users in the Airport Operator with regard to consultation on the introduction of CUTE (discussed below).

It is unlikely that even the tightest of price cap mechanisms would be successful in achieving the regulatory objective in the absence of a mechanism to ensure consultation and consensus. Indeed, such consultation and consensus would be of direct benefit to the Airport Operator also as it would reduce the risk involved in developments. This lack of consensus was recently highlighted by the refusal of both Aer Lingus and Ryanair to move into the new 6-bay terminal extension or Pier C. In addition, the development of Pier C has led to a facility that is completely inefficient and only caters to less than 18% of the airport's throughput, despite its extremely high cost. On the other hand, Aer Rianta is refusing to build Pier D, which was initially planned and designed by them and has received planning permission. As is discussed further below, consultation on this issue has been ineffective and reflects the disequilibrium of bargaining power.

The following is a non-exhaustive list of examples of Aer Rianta's failure to properly consult with Users and demonstrates the critical need for a regulatory mechanism to ensure effective consultation and consensus on development and other issues effecting the users:

1. Introduction of the Fuel Levy

As noted above, Aer Rianta introduced a fuel levy at Dublin Airport in 1995 and attempted to do so last year in Cork. Users were not consulted at all concerning this levy, despite the fact that Aer Rianta was fully aware that this levy was passed directly on to the airlines. As explained, this levy was not accompanied by any form of investment by Aer Rianta in the fuelling infrastructure, as was the case when the BAA introduced its fuel levy at the London airports. There was therefore no cost justification for the introduction of this levy.

2. Introduction of CUTE

As mentioned above, Aer Rianta failed to properly consult with users on the introduction of this system on the check-in desks at Dublin Airport. Indeed, it was discovered during an Airport Operators Committee meeting that Aer Rianta had been representing to users that all of the users had agreed to the introduction of this system. When it was revealed that this was in fact not the case and that the two major users of the airport had specifically stated that they would not be using the system, the AOC members unanimously passed a vote of no confidence in Aer Rianta's handling of this issue.

In addition, Aer Rianta has bundled a charge for CUTE into the increased fees for use of check-in desks.

3. Interim Arrangements during Terminal Extension

When it came to the interim arrangements necessary for the construction of the 6-bay terminal extension and the new baggage hall, Aer Rianta imposed interim arrangements without adequate consultation. Aer Rianta's plans did not take into account spare capacity of certain operators and the fact that Ryanair was operating at peak capacity. Ryanair was forced to get an injunction in order to force Aer Rianta to take its operational needs during the construction into consideration.

4. Introduction of the "Interim Pricing Structure"

In December 2000, Aer Rianta introduced its interim pricing structure citing the Groundhandling Legislation (S.I. 505) and its requirement to apply "relevant, objective, transparent and non-discriminatory criteria." Again, Aer Rianta's definition of non-discriminatory appears to be that all users must be charged the same price, even where their situations are vastly different. It is also noted that Aer Rianta increased all of these "interim charges" and introduced new charges, despite the fact that the objective of the Groundhandling Directive was to reduce the operating costs of airlines.

The "consultation" for this important change consisted of a presentation by Aer Rianta on 7 December 2000 informing the users that these pricing changes would be implemented on 1 January 2001. Aer Rianta provided no objective reasons for these increases and when pressed stated that they had consulted with other airports concerning the level of check-in desk fees.

Ryanair was forced to apply for judicial review of the introduction of these fees arguing that access fees under Section 14(3) of S.I. 505 require prior approval of the Minister, or, following its empowerment, by the Commission. Furthermore, Aer Rianta ignored a request by the Minister of Public Enterprise to postpone any price increases until after the Commission was empowered.

5. Introduction of New Rules of Conduct

Aer Rianta also introduced new "Rules of Conduct" that were to apply as of 16 December 2000. There is no legal significance of this deadline, which Aer Rianta was touting as the date by which they had to introduce these measures and yet Aer Rianta did not forward a final draft of the rules to the users until December 12. Despite the fact that these rules of conduct went beyond the current practice at Dublin Airport in a number of important respects, there was no adequate consultation on these rules and they were eventually imposed on the users. The original form of the rules was an agreement that included payment terms. However, it was pointed out to Aer Rianta that it could not tie payment terms to rules of conduct as these are treated separately in S.I. 505. It was also made clear at an earlier meeting that access charges had to be approved by the Minister or the Commission.

As part of the judicial review case mentioned above, Ryanair has also challenged the legality of the new rules of conduct and the process by which Aer Rianta introduced them.

6. Current Development Plan

Aer Rianta is currently "consulting" users with regard to the 20-year development plan for Dublin Airport. This consists of hiring a consultant, PB Aviation, who are conducting a series of three meetings, two of which have already taken place and users have still not received any indication of Aer Rianta's plans for developing the airport. The Users have been led to believe that there are no firm plans yet for the development of the Airport.

However, this is in stark contrast to what senior level officials from Aer Rianta informed Ryanair in September of last year when Ryanair met with Aer Rianta regarding expansion of its engineering facilities airside. There had been an agreement on this expansion dating from 1996 and 1998 and only the financing details remained to be finalised. However, during the meeting, Aer Rianta refused to discuss the agreement stating that it was now off the table as the 20-year development had been completed and in fact Ryanair's facilities would have to be moved to the other side of the airport.

Also, despite the very limited information that users have been provided, it is clear that Aer Rianta is pressing ahead with plans to build a second runway despite, as explained above, that the current main runway is being under utilised and the existing parallel runway is also being under-utilised and could be used to relieve the main runway and thereby further increase runway capacity at the airport. Indeed, Ryanair is aware that Aer Rianta has been informing residents groups in the area of the airport that it is planning to build a second runway.

Under normal circumstances, and Ryanair has most recently witnessed this at Stansted, where the airport is in the initial stages of a major development, i.e., from 15 million passengers per annum to 25 million passengers per annum, the Airport Operator would be required to provide not only airlines but also other users of the airport, including passengers, and interested parties very detailed information concerning the need for development and the various options and costs involved. Users would then have direct input into formulating and deciding upon the proposed options. This is clearly not the case at the Regulated Airports, where Aer Rianta's complete failure to effectively consult with users has led to unnecessary, inefficient and costly development, which in turn has been used by Aer Rianta to justify higher charges.

The attached correspondence between Michael O'Leary and Noel Hanlon of Aer Rianta, which resulted from a meeting between executives of the two companies, graphically illustrates the point. Aer Rianta ostensibly met with Ryanair to determine what its needs are in the next 5 to 10 years. Michael O'Leary explained that Ryanair's plans are directly related to whether Aer Rianta intends to provide low-cost, efficient facilities and a cost base to reflect the use of these facilities. If so, Ryanair could conceivably double its current passenger numbers in the next 5 years and increase them by 50% in the following 5-years.

However, Mr. Hanlon indicated that Pier D "would not be built" and that there would be no special deals for Ryanair and that all airport users would have to pay the same charges. Indeed, Mr. Hanlon stated that there would be no price reductions. Mr. O'Leary corrected Mr. Hanlon stating that Ryanair did not expect a special deal and that any other users in similar circumstances should also be entitled to a similar deal. He also pointed out that it was not for Aer Rianta to decide on what users would be paying at the Regulated Airports and whether prices would be reduced, as this was now a matter for the Commission to decide. Mr. Hanlon replied that it was only his opinion that prices would not be reduced. Correspondence between Messrs. Hanlon and O'Leary on this issue are attached as Annex 7.

Question 40: with a view to minimising regulatory restrictions, which services should form part of the regulatory regime? In what areas might regulation be unnecessary or ineffective even in the absence of market competition?

See response to Question 39 above.

Question 41: What national and international obligations are relevant to the regulation of airport charges?

International obligations which are relevant to the regulation of airport charges include Articles 10, 12, 81, 82, 86 and 87 of the EC Treaty.

National obligations which are relevant to the regulation of airport charges include the Competition Acts 1991-1996. The Department of Public Enterprise's Strategy Statement, mentioned above, should also be considered a national obligation relevant to the regulation of airport charges.



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2nd March, 2001

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 Dublin Airport
 Co Dublin

Dear Noel,

May I thank you, your team and Gerald Fitzgerald of PB Aviation Inc. for taking the time to meet with us this morning as part of the consultation process with one of your principal customers.

In this spirit of consultation (and in order that PB Aviation Inc. can take account of the huge potential opportunity which exists here at Dublin Airport) may I confirm Ryanair's position as follows;

1. Ryanair's operational requirements were perfectly summarised by Tom Haughey in his presentation to the Marcus Evans conference last week (copy enclosed) and I can confirm that what Ryanair want at Dublin is;
 - low charges,
 - fast turnarounds,
 - contact stands,
 - efficient ground handling operations,
 - simple inexpensive facilities,
 - lounges/airbridges/CUTE not necessary,
 - no congestion
2. Since the issue of costs is clearly now a matter of the Aviation Regulator, our consultation must focus on facilities.
3. Ryanair requires low cost efficient facilities along the lines of the D Pier as originally designed by Aer Rianta, or alternatively a second terminal which can clearly be constructed at minimal costs adjacent to the existing facilities here at Dublin or in a green field site at a cost of no more than £20m.

4. What neither we nor any of this airports other customers want is further profligate, inefficient facilities such as Pier C which despite the cost of £50m. wholly fails to address the need for contact served stands at Dublin Airport.

Subject to the development of these facilities and an acceptable cost base being determined by the Regulator in compliance with all competition and regulatory rules, Ryanair believes that we can stimulate substantial additional traffic and tourism growth at Dublin (and the other Aer Rianta airports) by launching a wide series of new low fare scheduled services from Dublin, Cork and Shannon to destinations in the UK, Scandinavia, Germany, Austria, Spain, Italy, France and Benelux countries.

We estimate that Ryanair could over a five year period double our existing traffic numbers of 3 million to 6 million at Dublin, and increase these again by 50% to 9 million passengers over the subsequent five year period. **In essence we believe that we can treble our existing traffic numbers over the coming 10 years if suitable facilities and a competitive cost base emerges at Dublin (and to a lesser extent Cork and Shannon airports).**

These opportunities are being lost by Aer Rianta, Dublin, and indeed Ireland in recent times because of the current policy of Aer Rianta which is to develop expensive, inefficient facilities which don't address the specific needs of your airline customers. Obviously Pier C has been the latest and most profligate example of this failure and your continuing failure to commence construction of Pier D which would provide a further twelve contact served stands at a minimum cost remains all the more inexplicable.

Whilst clearly it will not form part of an Aer Rianta commissioned consultation report, we firmly believe that the break up of the Aer Rianta monopoly would be the most efficient and expeditious manner of improving facilities and lowering costs at Dublin Airport, not just in terms of the provision of facilities to airlines but also to other airport users and the travelling public. Last year's 70% increase in the daily rate of short-term carparking from £7 to £12 was clearly an abuse of Aer Rianta's monopoly position here at Dublin and an increase that would not have taken place had there been some competition to your monopoly.

I will be taking the opportunity of writing directly to Gerald Fitzgerald seeking a meeting directly with PB Aviation Inc. so that we may explore in some greater detail the requirements of your second largest customer here at Dublin and more importantly the potential dramatic growth in routes, frequencies and traffic and tourism which will be yielded as a result.

Thank you again for facilitating this morning's consultative meeting, I thought it was a very positive and useful exchange between our respective companies.

Yours sincerely



Michael O'Leary
Chief Executive

Noel Hanlon
Chairman

AerRianta

Ref: NH/MOB

*Aer Rianta c/o - Airport Managers - Duty Free
Managers - Hotel Managers - International Consultants.*

Mr. Michael O'Leary,
Chief Executive,
Ryanair,
Dublin Airport,
County Dublin.

7 March 2001

Dear Michael,

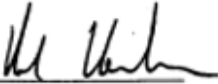
Thank you for your letter of 2nd March, in connection with the meeting that took place as part of the consultant process with P.B. Aviation and our senior executives.

As was set out to you at our meeting, we in Aer Rianta build our facilities here at Dublin Airport to international standards which would allow any airline to operate them to the standards required internationally. As you are very well aware - airlines come and airlines go - but airports stay forever and as I pointed out to you at our meeting, it is the Board of Aer Rianta's position that any facilities provided at the airport will be to international standards.

I find it extremely difficult to actually ascertain the requirements of Ryanair in the years ahead. We are anxious to be in a position to make available to you the necessary operational facilities, including contact stands but I am sure you will appreciate that all charges at Dublin Airport have to be determined in accordance with relevant, objective, transparent and non-discriminatory criteria and that there can be no special deals for any individual company or airline operating at the airport. Perhaps your forthcoming meeting with P.B. Aviation might clarify some of the issues.

I found John McManus's editorial in the Irish Times very informative. I am enclosing a copy for your information in case you have missed it.

Yours sincerely,



Noel Hanlon
Chairman

C.C. John Burke
G. Fitzgerald, P.B. Aviation
Bob Hilliard D.A.P.

Directors

*Noel Hanlon - Chairman, Noel Fox, Dermot O'Leary, Pat Fitzgerald, Peter Dunne,
Tony Smurfit, Tadhg O'Donoghue, Rita Bergin, John Burke - Chief Executive*

Registered Office: Aer Rianta, Dublin Airport, Registered No. 9401 Ireland

*Aer Rianta c/o. Head Office, Dublin Airport, Ireland
Direct: Telephone: (353) (1) 8444620
Direct Telefax: (353) (1) 8446220*

Low-Cost Carriers –
An Airport Perspective
Amsterdam
27th February 2001



Tom Haughey
Director-Market Development and Strategy

AerRianta

Timing is Everything

Prior to liberalisation:

- State control of airlines
 - National policy influencing route development strategy
 - Frequently uneconomic long-haul routes
 - Fleet composition influenced politically
- Highly restrictive labour agreements
- Increasingly elaborate product composition
 - Every scheduled carrier offered a similar type of product

AerRianta

Timing is Everything

- Deregulation in the US in 1980s
- Deregulation in Europe:
 - 1987 First package:
 - first application of EC law to air transport
 - 1990 Second package
 - 1993 Third package:
 - 1997 Cabotage restrictions lifted

AerRianta

Liberalisation:

- Challenged governments to privatise airlines
 - State-owned companies less dynamic, more bureaucratic
- Many states slow to adapt to these changes
- Period of transition as market slowly responded to the changing environment

The New Marketplace

- New opportunities for existing operators to enter or leave routes
- Reduced barriers to entry for new operators
- Openings for non-national carriers
- Fare restrictions lifted
 - Incumbents not very responsive to changes in fare regulations

Liberalisation and Deregulation

- The requirements of the new marketplace should not have come as a surprise
- US deregulation preceded full liberalisation in Europe by more than a decade
- In the US, a new carrier type emerged promising consistent and profitable growth

SW Model V Full Fare	
Southwest (original model)	Full Fare Carriers
High aircraft utilization	Mixed utilization
Fast turnarounds	Longly turnarounds
No inflight meals or drinks	Competition on service levels and meals
No slotting	Expensive slotting and associated technology and costs
No through ticketing	Complex systems driving high staff costs and low productivity
No Seat Pre-selection	Seat Pre-selection a key feature
Use of secondary airports	Use of highly congested major airports
Low cost distribution	Distribution mainly through Travel Agents

No Frills Carrier Product Offers

- Benefits to consumers through lower fares and new routes
- Benefits to shareholders, employees and local communities
- Potential Benefits to suppliers
 - Including airports

Airport Facilities

Low cost airlines want:

- Low charges
- Fast turnarounds
 - Contact stands
 - Efficient ground handling operation
- Simple inexpensive facilities
 - lounges/airbridges not necessary
- No Congestion

European Low Cost V Full Fare	
Low Cost Carriers	Full Fare Carriers
Simple Brand - e.g. Ryanair = low fare Easyjet more complex - virtual company	Complex Brand = Service + Image ++
Online and direct bookings: PK 65% online bookings, only 35% with travel agents; Easyjet, Go 100% direct	Mainly travel agents -although commissions being reduced
Proactive in use of website portal for purchase of other services e.g. hotels, hotels etc	Coordinated website products under development
Simple ticket price structures & tickless check-in	Complex fare structures
Use of secondary low charging airports -Virgin Express use of Bournemouth	Focus on primary airports
High aircraft utilisation-quick turnaround	Lower utilisation on short-haul

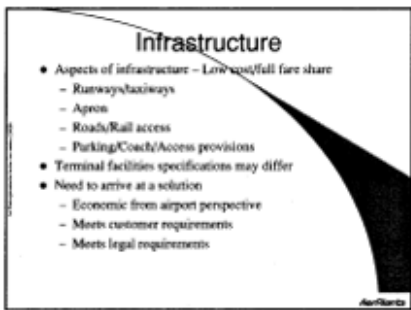
European Low Cost V Full Fare	
Low Cost Carriers	Full Fare Carriers
Do not interline/oline* -Q&A -but Virgin Express does	Focus on interline/oline facility hubs
Simple products- all additional facilities charged for e.g. credit card bookings Late check-in	Complex integrated service products) -faster facilities -Business lounges -Frequent flyer programs
Focus on ancillary revenue generation -advertising, on-board retailing	Focus on primary product
Mainly short-haul focus -although Southwest shifting position on this	Short and long-haul
Constant fleet type acquired at very good rates	Mixed fleet

Interesting Fact

- Diversity of low cost carriers emerging
- Aggressive low cost
- Low cost brand
- Full fare subsidiary
- Mixed structure- charter and scheduled
- Not all will be equally successful

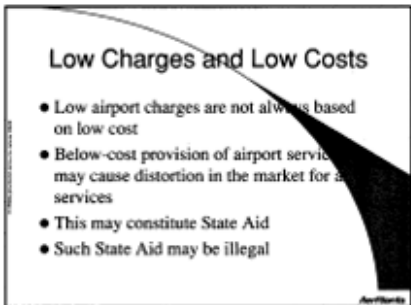
Infrastructure

- Aspects of infrastructure – Low cost/full fare share
 - Runways/taxiways
 - Apron
 - Roads/Rail access
 - Parking/Coach/Access provisions
- Terminal facilities specifications may differ
- Need to arrive at a solution
 - Economic from airport perspective
 - Meets customer requirements
 - Meets legal requirements



Low Charges and Low Costs

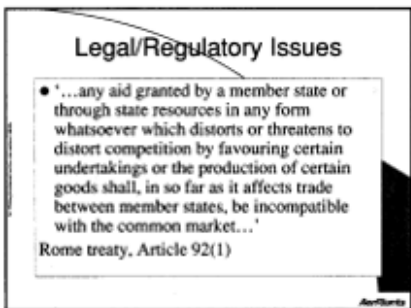
- Low airport charges are not always based on low cost
- Below-cost provision of airport services may cause distortion in the market for airport services
- This may constitute State Aid
- Such State Aid may be illegal



Legal/Regulatory Issues

• '...any aid granted by a member state or through state resources in any form whatsoever which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods shall, in so far as it affects trade between member states, be incompatible with the common market...'

Rome treaty, Article 92(1)



Legal/Regulatory Issues

- Competition Law – Non discrimination
- Pressure to treat all customers in same manner
- Aer Rianta under new Regulatory environment
- Serious issues for airports
- Serious issues for airlines

Airports

Aggressive pricing of under-utilised facilities may make sense- subject to:

- Agreement by the Commission
- Non-discrimination
- No distortion of the airport market

i.e. Where State aid for capex and/or operational approved

Otherwise – no free lunch!
Someone must pay:

Shareholder/taxpayer subsidy	Other users discrimination
---------------------------------	-------------------------------

Low cost carriers and Airports

- There are different kinds of low cost carriers
- There are also different kinds of airports

Airports

- In the airport life cycle the marginal cost will change over time:
 - Large scale infrastructure projects
 - Large chunks of capacity added
 - Long term perspective necessary
 - Long lead time for delivery
 - Levels of non-aeronautical revenues
 - Single till subsidy
 - Access to funding from other bodies
- Airport perspective different from airline

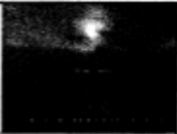
Partnership

- Airport and low cost carriers need to work together:
 - Adequate definition of facilities required
 - Capex consultation process
 - Effective communication
 - Efficient use of available resources
 - Optimise capex spend
- All parties win
 - Essence of successful sustainable business

Summary

- Adversarial attitude on part of low cost carriers ignores market realities of airports
 - Infrastructure is expensive
 - Lead times are significant
- Airlines challenging airports on capex plans be welcomed
- Airlines and Airports are both in business to do business
- Neither can succeed without the other

Low-Cost Carriers –
An Airport Perspective
Amsterdam
27th February 2001



Tom Haughey
Director-Market Development and Strategy
AerRianta

Runway Growth

- Currently runway movements 44 per hour maximum.
- Nature of traffic means demand likely to continue at peak.
- Growth to 50 movements per hour possible in the coming years.

Our Approach

- As part of this process we will not :
 - Seek any relaxation to the current DETR night flight restriction
 - Develop outside of the existing airport boundary
 - Be proposing any additional provisions

Aer Rianta

Cost of Capital Analysis

March 23, 2001

MORGAN STANLEY DEAN WITTER

This paper does not provide the level of detail on airport charging structures to be found in the 1996 study and that report continues to be a useful reference on some of the more complex charging issues.

AIRPORT CHARGES: COMPARISON OF 2000 AGAINST 1995

The airports used in this analysis are those included in the November 1996 study (based on 1995 data): Dublin, Stansted, Gatwick, Luton, Birmingham, Manchester, Liverpool and Prestwick plus those airports in the UK and Europe where Ryanair has started service since 1995. Other airports in Ireland (e.g. Cork, Knock) were not included in the previous study and hence have been omitted from this paper also.

The 1995 airport charges are derived from a study of the contracts, rates and route traffic statistics for Dublin and the UK airports served by Ryanair, undertaken by the University of Westminster as part of the 1996 report. The 2000 analysis of airport charges is based on a report produced in September 2000 by KPMG Chartered Accountants of Ryanair's actual airport passenger and landing costs for the period Jan 1st-July 31st 2000 and its budgeted airport passenger and landing costs for the period Aug 1st-December 31st 2000 at all the airports in its scheduled service network. The KPMG results have been combined to produce estimated figures for the whole year 2000, in order to avoid distortions due to seasonal variations in charges at certain airports. Only in the cases of Bournemouth, Leeds Bradford and Manchester does the budgeted rate per passenger for the last five months of 2000 differ from the actual over the first seven months by more than 20%. There is unlikely to be much variation from the budgeted total charge per passenger in the final out-turn as in most cases it is only the load factor and hence the landing charge per passenger that cannot be calculated exactly for the budget period.

The costs identified for each airport include landing, passenger and aircraft parking charges, net of any rebates. It does not include separate charges for terminal navigation services (such as those levied at the London airports, or by the IAA at Dublin). Security charges and handling charges are similarly excluded, except where they are incorporated within the passenger charge. The various charges are then aggregated and divided by the total number of departing passengers to obtain a charge per departing passenger (even though some of the charges may be actually incurred on arrival).

In order to neutralise as far as possible the changes in exchange rates that have taken place over the last five years and provide a consistent basis for comparison, the same average exchange rate has been applied to both the 1995 and 2000 charges in local currency to translate them to Irish Pounds. The conversion rates used are the average exchange rates for the period January 1995 to September 2000 (Source: Bloomberg/Ulster Bank).

The airport charges incurred by Ryanair at the airports studied for the year of 1995 are shown in Table 1. Navigation charges have been removed from this assessment for consistency with the KPMG review. The charge per passenger is indexed to an average of 100(=IR£).

TABLE 1

Average airport charges incurred by Ryanair in 1995

Dublin and UK airports

Airport	Average charge per departing Passenger (IR£)	Index Average = 100
Dublin		143
Gatwick		*
Birmingham		*
Stansted		*
Manchester		*
Luton		*
Liverpool		*
Prestwick		*
AVERAGE		100

* Less than 100.

Table 2 shows the airport charges incurred by Ryanair for the current year 2000. As explained above, this is based on the KPMG report of the actual charges for the months of January-July and the budget charges for the months of August-December. The charge per passenger is indexed to an average of 100(=IR£).

TABLE 2

Average airport charges incurred by Ryanair in 2000

Dublin, UK and European airports

Airport	Average charge per departing Passenger (IR£)	Index Average = 100
Dublin		204
Gatwick		179
Birmingham		155
Manchester		122
Luton		119

Stansted		102
Others in UK and Europe		Less than 100
AVERAGE		100

The average charge paid by Ryanair has risen by only 16% from IR£ to IR£ per departing passenger over this time period. The charge at Dublin, which was already the most expensive airport in the 1995 study, has gone up much faster from IR£ to IR£ per departing passenger, an increase of 64%. Whereas Dublin was 43% above Ryanair's airport average charge in 1995, this differential has escalated to 104% in 2000. Charges have also risen substantially at Gatwick and Birmingham but remain below the level at Dublin. The launch incentives for new routes have unwound at Dublin for most of Ryanair's services, except those inaugurated in 1997. Although Aer Rianta's published tariff remains lower than that of many other airports, Ryanair has succeeded in negotiating discounts at almost all the other airports listed in Table 2. Most airports remain anxious to expand their business, except for Gatwick which is effectively full for most of the operating day. Comparisons between the published and actual rates at different airports are made in the University of Westminster report to Ryanair of November 1996.

TOTAL COSTS AND TRAFFIC BY AIRPORT

Table 3 compares the share of costs and traffic in Ryanair's operation for each of the airports in Table 2 above.

TABLE 3

Share of total costs and total traffic for airports analysed in Table 2

Airport	Share of Ryanair's costs (%)	Share of Ryanair's traffic (%)
Dublin	50	24
Stansted	33	33
Gatwick	4	2
Birmingham	3	2
Manchester	3	2
Luton	3	2
Others in Table 2	5	35

N.B. Figures do not add to 100 because of rounding

It can be seen that Dublin accounts for half Ryanair's total airport charge bill despite representing less than a quarter of Ryanair's passengers. Stansted accounts for a third of traffic and a third of charges. The smaller airports provide a higher share of passengers than their share of airport charges.

TRAFFIC GROWTH AT DIFFERENT AIRPORTS

A number of airports have adopted a low-charge strategy to try and attract new services, especially by the 'low-fares' scheduled airlines such as Ryanair and easyJet. This has been reflected in very high growth rates, much in excess of 10% per annum. Table 4 compares traffic development over the last five years at Dublin and the four UK airports that are the focus of 'low-fares' airline activity (Stansted, Luton, Liverpool and Prestwick).

TABLE 4

Annual growth in scheduled passengers 1995-2000

Dublin and selected UK airports

Between years	Growth in scheduled passengers (%)					
	Dublin	Dublin (UK only)	Stansted	Luton	Liverpool	Prestwick
1995-96	15	15	23	116	12	118
1996-97	15	13	11	66	18	11
1997-98	11	9	33	37	29	-6
1998-99	9	4	52	42	72	25
1999-2000*	5	0	37	28	107	21

* based on Jan-June 2000 compared to Jan-June 1999

It can be seen that Dublin enjoyed high growth rates of 15% per annum in the mid 1990s but this growth rate has declined by two-thirds to merely 5% per annum at the current time. If only UK routes from Dublin are considered, traffic is actually falling: 4 633 fewer passengers were carried during the first six months of 2000 compared to the equivalent period in 1999. This is surprising given the strength of the Irish economy and the weakness of the euro, which one would have expected to lead to a large increase in inbound tourism from the UK. In contrast, the other airports in Table 4 have enjoyed double digit growth in every year, with the sole exception of 1997-98 at Prestwick. In most cases the greatest expansion has taken place in 1999-2000, the inverse of the picture at Dublin.

Even within Ireland, there has been very rapid growth in European traffic at Shannon Airport where there are low charges for services to Continental Europe. This has led to new routes being launched by both Ryanair and Virgin Express. Traffic between Shannon and Continental Europe grew by 130% in the first eight months of 2000 compared to 1999.

RYANAIR SHARE OF TRAFFIC

Table 5 shows Ryanair's market share of scheduled passengers at the UK airports and Dublin in Jan-June 2000 (Compiled from CAA UK Airport Monthly Statistics, Aer Rianta Traffic Report and Ryanair route traffic data).

TABLE 5

Ryanair charge levels and market share

Dublin and UK airports

Airport	Charge index [^]	Ryanair market share (of scheduled passengers)#
Dublin	204	27%
Gatwick	179	1%
Birmingham	155	6%
Manchester	122	3%
Luton	119	5%
Stansted	102	38%
Leeds Bradford	*	15%
Cardiff Wales	*	19%
Bournemouth	*	84%
Liverpool	*	9%
Bristol	*	18%
Prestwick	*	99%
Teesside	*	16%
Londonderry	*	81%

* less than 100

[^] as per Table 2 above

Jan-June 2000

It is apparent that there is little correlation between Ryanair's market share and the level of airport charges Ryanair pays. The airports where Ryanair accounts for 6% or less of total scheduled passengers incur above average charges. However, when Ryanair accounts for greater than 6% of total scheduled passengers, airport charges fall close to or below average on the charge index, with the exception of Dublin where Ryanair pays the highest charge of all. Although locations such as Prestwick and Bournemouth have low total traffic, this is certainly not the case at Stansted where Ryanair accounts for 38% of the 4.56 million scheduled passengers in January-June 2000. At Dublin, Ryanair has 27% of the 5.58 million scheduled passengers but the charges are double the level of those at Stansted.

COMPETITION BETWEEN AIRPORTS

Another influence on the level of charges Ryanair is able to negotiate at an airport may be the existence of competition with other airport(s) nearby. If one airport is unable to offer competitive charges, the airline - and its passengers - may be able to switch to a different airport offering access to the same hinterland. This can also lead to all airports in a region offering attractive rates to ensure they do not miss out on their share of the traffic.

Table 6 below shows the number of alternative commercial airports available within a 60 mile (100 km) radius at each location Ryanair serves. These are airports that have a hard runway of at least 1600 metres in length (sufficient to handle Boeing 737 aircraft) and at least 50,000 scheduled passengers in the year 1999 (Source: UK CAA Statistics, OAG World Airways Guide, Royal Aeronautical Society Directory of British Aviation).

In practice, the number of alternatives will often be greater still as there are other airports with only charter flights at the present time which could potentially handle scheduled services (e.g. Coventry near Birmingham).

TABLE 6

Competition between airports

Dublin and UK airports

Airport served by Ryanair	Alternative commercial airports within 60 miles (100 kilometres)*	Number of alternatives
Gatwick	Heathrow, Stansted, Luton, Southampton	4
Stansted	Heathrow, Gatwick, Luton	3
Luton	Heathrow, Gatwick, Stansted	3
Manchester	Liverpool, Leeds Bradford, Blackpool	3
Leeds Bradford	Manchester, Teesside, Humberside	3
Bristol	Cardiff Wales, Exeter, Bournemouth	3
Teesside	Newcastle, Leeds Bradford	2
Liverpool	Manchester, Blackpool	2
Bournemouth	Southampton, Bristol	2
Prestwick	Glasgow, Edinburgh	2
Londonderry	Belfast International, Belfast City	2

Birmingham	East Midlands	1
Cardiff Wales	Bristol	1
Dublin		0

* with 1600m hard runway and 50,000 scheduled passengers in 1999

It can be seen that all Ryanair's UK airports have at least one competing alternative, in most cases two or more. Dublin, in contrast, is a monopoly with no alternative commercial airport.

In the London area competition is potentially restrained by capacity shortages at many of the airports and the common ownership of Heathrow, Gatwick and Stansted by BAA. Nevertheless, even though Gatwick is one of the most slot constrained airports in Europe, where any service that is withdrawn would be rapidly replaced by another, the average charge paid by Ryanair is still below that at Dublin. This may be influenced by the regulation of airport charges at the BAA airports to prevent them functioning as a monopoly.

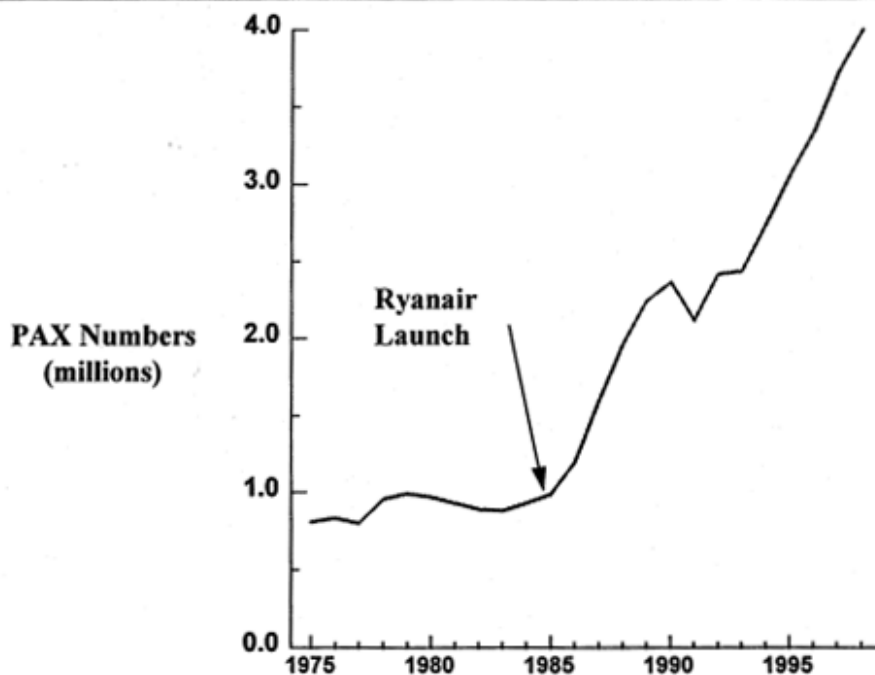
CONCLUSION

Dublin was the most expensive airport served by Ryanair in the 1995 study and remains the most expensive in the year 2000. The charge per passenger paid by Ryanair at Dublin has risen dramatically, by 64% over the five year period, whereas the airline's average airport charge has increased by only 16%. Charges at Dublin have escalated to such an extent that they are now double the average level paid by Ryanair across its network, whereas in 1995 Dublin was only 43% above average.

It is apparent that Ryanair has concentrated major expansion on Stansted in recent years at the expense of Dublin. Ryanair now carries more passengers from Stansted than from Dublin but Dublin alone still accounts for 50% of its total airport charge bill. The end to expansion by Ryanair at Dublin means that total growth at Dublin has faltered and the airport is no longer enjoying the rapid expansion currently experienced at UK airports such as Stansted, Luton, Liverpool and Prestwick. This growth is primarily driven by 'low-fares' carriers.

Ireland undoubtedly remains attractive as a tourist destination and rapid economic growth should create the potential for many more international air services. Dublin airport is never likely to be in the major league of airline hubs and hence will become progressively sidelined by the major carriers constructing their global alliance networks. This could lead to a concentration on feeder routes to nearby alliance hubs such as London, Paris and Amsterdam with a loss of direct services, as has already happened in many European countries. The best prospect for improving access to Ireland and creating a wider range of travel opportunities would appear to be the 'low-fares' carriers, such as Ryanair, with their proven ability to stimulate passenger volumes in every market that they enter. At almost every location that Ryanair serves except Dublin there is at least one alternative airport within a 60 mile radius. This provides the necessary conditions for competition between airports which in turn leads to downward pressure on the level of airport charges. With no realistic alternative airports to Dublin available and no terminal competition within the airport, as happens in the US, if Ireland is to benefit from the continued growth of air transport the current impasse over airport charges between Aer Rianta and Ryanair needs to be resolved.

The "Ryanair Effect": Dublin - London *



Note: * Including traffic to/from Heathrow, Gatwick, Stansted, Luton and City
 Source: Company (1985 through 1990, 1998)
 Dublin Airport Authority (1991 through 1997)



Most Profitable World Airport Authorities
 Airline Business Magazine December 1998

	Airport Company / Authority	Country	1997/98 Revenues Millions US\$	1997/98 Net Profits Millions US\$	1997/98 Passengers Millions	1997/98 \$ Profit per Passenger
1	CAM SAI de Macau	Macau	63	57	2.0	29.23
2	Hong Kong	China	463	209	29.0	7.21
3	BAA	UK	2,818	624	104.5	5.97
4	Aer Rianta	Ireland	374	64	13.4	4.78
5	Amdterdam Schipol	Netherlands	569	126	31.6	3.99
6	Flughafen Dusseldorf	Germany	316	57	15.5	3.68
7	Port Authority NY NJ	USA	1,148	297	83.9	3.54
8	Copenhagen Airports Authority	Denmark	232	49	16.8	2.92
9	SEA Milan	Italy	447	44	18.2	2.40
10	Zurich Airport Authority	Switzerland	319	43	18.3	2.35
11	Stockholm Arlanda	Sweden	565	34	14.9	2.28
12	Manchester Airport	UK	378	31	16.0	1.94
13	Federal Airports Corporation	Australia	497	86	45.1	1.90
14	Aeroporti di Roma	Italy	691	47	25.8	1.82
15	Metropolitan Minneapolis -St Paul	USA	189	52	30.2	1.72
16	Korean International Airports	S. Korea	240	94	56.6	1.66
17	Cairo Airport Authority	Egypt	65	12	8.0	1.50
18	Wayne County - Detroit	USA	137	47	31.5	1.49
19	London Luton Airport	UK	71	5	3.2	1.44
20	City and County of Denver	USA	414	48	34.9	1.38
21	Flughaven Frankfurt	Germany	1,373	52	40.3	1.29
22	Aeroports de Paris	France	1,241	71	60.4	1.18
23	Dallas - Fort Worth International	USA	221	67	60.4	1.11
24	Metro Washington Airports Authority	USA	232	30	29.3	1.02
25	Flughaven Munchen	Germany	509	17	17.9	0.97
26	City of Atlanta	USA	203	63	68.2	0.92
27	San Francisco Commission	USA	242	34	40.5	0.84
28	City of Phoenix Aviation Dept	USA	149	22	30.6	0.72
29	Toronto Airport	Canada	198	14	26.1	0.54
30	Airports Authority of India	India	58	10	21.5	0.47
31	Port of Seattle	USA	142	9	24.7	0.38
32	Salt Lake City Airport Authority	USA	90	7	21.1	0.31
33	City of Philadelphia Aviation	USA	133	7	22.4	0.31
34	Tokyo Airport Authority	Japan	1,270	0	25.7	-
35	Chicago Dept of Aviation	USA	443	0	80.2	-
36	Vienna Airport Authority	Austria	334	0	9.7	-
37	Brussels International	Belgium	200	0	16.0	-
38	Greater Orlando Aviation Authority	USA	190	0	27.3	-
39	Las Vegas McCarran	USA	155	0	30.3	-
40	Charlotte/Douglas International	USA	68	0	22.7	-
41	Kenton County Airport Board	UK	62	0	20.3	-
42	Osaka Airport Authority	Japan	981	(312)	33.4	-

Airport Financial Results 1997/98

Profit per passenger

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	Airport Company / Authority	Country	1997/98	1997/98	1997/98	1997/98
			Revenues Millions US\$	Net Profits Millions US\$	Passengers Millions	Profit per Passenger
1	BAA	UK	2,818	624	104.5	5.97
2	Aer Rianta	Ireland	374	64	13.4	4.78
3	Amdterdam Schipol	Netherlands	569	126	31.6	3.99
4	Flughafen Dusseldorf	Germany	316	57	15.5	3.67
5	Copenhagen Airports Authority	Denmark	232	49	16.8	2.91
6	SEA Milan	Italy	447	44	18.2	2.40
7	Zurich Airport Authority	Switzerland	319	43	18.3	2.35
8	Stockholm Arlanda	Sweden	565	34	14.9	2.28
9	Manchester Airport	UK	378	31	16.0	1.94
10	Aeroporti di Roma	Italy	691	47	25.8	1.82
11	London Luton Airport	UK	71	5	3.2	1.42
12	Flughaven Frankfurt	Germany	1,373	52	40.3	1.29
13	Aeroports de Paris	France	1,241	71	60.4	1.18
14	Flughaven Munchen	Germany	509	17	17.9	0.97
15	Vienna Airport Authority	Austria	334	0	9.7	-
16	Brussels International Zevantum	Belgium	200	0	16.0	-