F.No.AAI/JVC/Pune -Tariff/2021 Date : 08/02/2022

The Secretary,
Airports Economic Regulatory Authority of India,
AERA Building, Administrative Complex,
Safdarjung Airport
New Delhi-110003

Sub: - AERA's Consultation Paper No. 26/2021-22 in the matter of Determination of Aeronautical Tariff in respect of Pune Airport for the Third Control Period (01.04.2021 to 31.03.2026).
Ref:- AAI's counter comments in response to Federation of Indian Airlines (FIA) submission – Reg.

Sir,

This is in reference to the Federation of Indian Airlines (FIA) comments received through AERA e-mail dated 31.01.2022

In this regard, please find attached herewith the AAI's counter comments in response to FIA's submission.

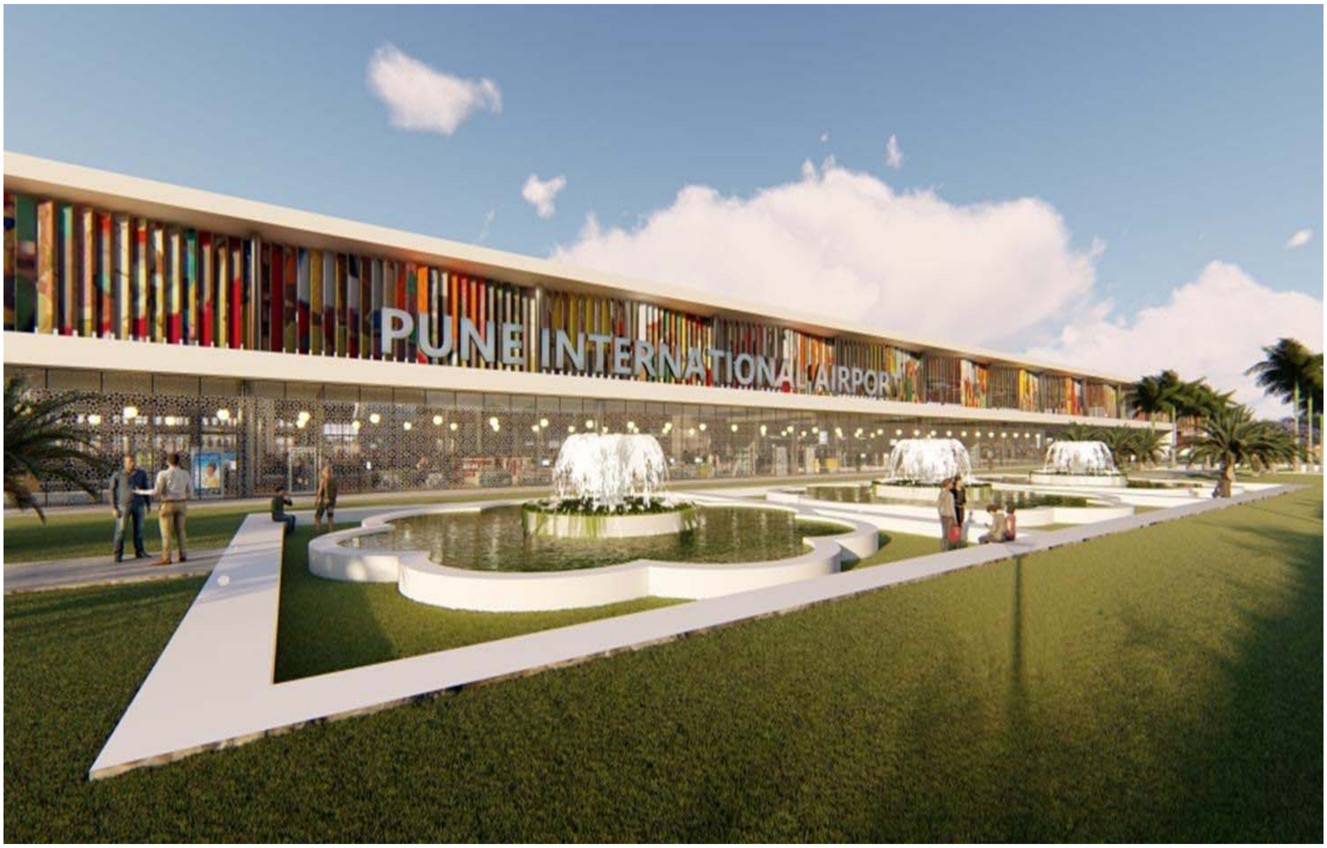
Thanking You,

Your faithfully

8/02/2022

(V.Vidya)
Executive Director (JVC & PPP)-I

Enclosed: *As above*



PUNE INTERNATIONAL AIRPORT (PNQ)

Response to Counter Comments of Federation of Indian Airlines (FIA) for Consultation Paper No. 26/2021-22 dated 30th December 2021 in the matter of Determination of Aeronautical Tariff for Pune International Airport (PNQ) for the Third Control Period (01.04.2021 - 31.03.2026).

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Comments from Federation of Indian Airlines (FIA)

1. Regarding Revenue from Air Navigation Services and Cargo services:
(Para 1.1.2, 1.4.3 and 1.4.4 of the CP)

It is submitted that as per section 2 of Airport Economic Regulatory Authority of India Act, 2008 (**AERA Act**), under subsection (a), "aeronautical services mean any services provided.

(i)For navigation, surveillance and supportive communication thereto for air traffic management.....

(v) for the cargo facility at an airport.."

It is submitted that considering the above provisions of the AERA Act, revenue from Air Navigation Services, Cargo services (100% revenue accruing to AAICLAS) should form part of aeronautical revenues and accordingly AERA should consider of the corresponding revenue and revise the tariff card.

Comments of AAI

The methodology adopted by the Authority to determine Aggregate Revenue Requirement (ARR) is based on AERA Act, 2008 and the Airport Guidelines issued by AERA. (para 3.3.1.)

As per the guidelines, for the Second Control Period, the Authority had adopted the Hybrid-Till mechanism for tariff determination, wherein, only 30% of the Non-aeronautical revenue is to be used for cross-subsidizing the Aeronautical charges. The Authority has considered the same methodology in the true up of the Second Control Period and for tariff determination in the Third Control Period. (para 3.3.2.)

The ARR under Hybrid Till for the Control Period (ARR) shall be expressed as under:

ARR =$\Sigma ARRt5t$=1

ARRt = (FRoR x RABt) + Dt + Ot + Tt - s x NARt" (para 3.3.3.)

AAI submits that the tariff determination for airports by AERA is done only for the Aeronautical charges collected by the AAI of Major airports.

Tariff for Air Navigation Services (ANS) for India as a whole has been revised by MoCA whereas, AAICLAS (Cargo services) is 100% subsidiary of AAI and tariff is determined separately by AERA.

2. **Regarding Aeronautical Capital Additions approved in the Second Control Period Order but deferred to the Third Control Period**: (Para 4.2.1, 4.2.2, 4.2.9, 4.2.20 & Table 57 and Table 65)

It is observed that Pune Airport has tendency to exceed the normative cost benchmarks as well as overestimate the capital expenditure and thereafter defer it to the subsequent control period. In this regard, we recommend that an adjustment of 1% or higher of the project cost, as deemed fit, from the ARR in case any particular capital project is not completed/capitalized as per the approved capitalization schedule, which should be applied on the deferred projects of the Second Control Period, other than those affected solely by the adverse impact of COVID-19.

In addition, we would request AERA to ensure that the operator complies with the AUCC consultative meetings and timelines thereof for all assets crossing the requisite threshold limit prescribed by AERA in Third Control Period, including an update on the progress of NITB project. Further, as mentioned under Para 9.9 of the Second Control Period Tariff Order issued by AERA for Pune Airport and further referred under 4.2.9 (C) of the present Consultation Paper, we request AERA to conduct independent study for reasonableness of capital expenditure so that appropriate adjustments are made to capital expenditure/ RAB for Second and Third Control Period.

Comments of AAI

Pune Airport has submitted calculation for Normative Cost for all the projects wherever applicable and the same has been validated by the Consultant appointed by AERA. The major project of New Integrated Terminal Building has been shifted from 2nd Control Period to 3rd Control period due to Covid-19 pandemic. Reconciliation of capex of 2nd control period as per Consultation Paper is placed below:

Table 16: Reconciliation of Additions (on total basis) allowed in Second Control Period Order and Actuals incurred at Pune International Airport

(Rs. in Lakhs)

Particulars	Ref	Amount
Additions as per SCP Order	**A**	**40,523.11**
Cargo related assets additions considered in SCP order now excluded	B	37.72
Capital Expenditure proposed in SCP but later, based on nature, classified as Repairs & Maintenance cost	C	39.97
Projects whose capitalisation is deferred to Third Control Period	D	38,085.41
Sub Total	**E=A-Sum(B:D)**	**2,360.01**
Variance in cost (between additions approved and incurred)	F	-419.85
Sub Total	**G=E+F**	**1,940.16**
Cargo assets forming part of Additions for SCP (Refer Note 2 below)	H	74.24
Capital additions incurred in the SCP but not approved in the SCP order (Refer Note 3 below)	I	6,874.08
Total	**J=G+H+I**	**8,888.48**
Financing Allowance (including FA for FY21)	K	212.95
Total Additions proposed by AAI in true up of SCP	**L=J+K**	**9,101.43**

AERA has sought various details on the unplanned capital expenditure during MYTP process. AAI submits that these are legitimate spends made after various levels of approval within the organization. Depending on the quantum of spend, the regional/central head-quarters are also involved. AAI submits that after careful consideration and discussion at appropriate levels within the organization, the additional unplanned capex was categorized as "essential".

At Pune Airport, the Capex of 2nd Control Period has not been shifted to 3rd Control period other than Proposed Terminal Building which was shifted due to Covid-19 Pandemic.

AUCC meeting has been conducted on 31.01.2022 and the same has been attended by various stakeholders. The detailed project investment file for AUCC has also been shared with all the stakeholders. Minutes of the Meeting of the AUCC has been provided to the AERA consultant on 08.02.2022

3. **True Up of O&M Expenses for the Second Control Period:** (Refer, 2.8.2 2.8.5 and Table 18 ,19)

We appreciate that AERA is of the considered view that stakeholders should not be burdened with interest/penalties paid to Government of India, due to various lapses/delays on part of the Airport Operator. Pune Airport has paid interest/penalties to Government of India at CHQ & RHQ level. We appreciate that such expenses have not been allocated to the respective airport.

In addition, it is observed that several estimations in the Second Control period had missed out items as well as not completely considered some items by Pune Airport at time of submission for the Second Control Period. AERA is requested to kindly treat these inaccurate submissions with scrutiny such that the final impact may not substantially vary from the estimates provided.

Further, it is noted that while AERA expected a reduction on the O&M expenditure over a period of time, still the O&M expenses in the Second Control Period spiraled. We would appreciate AERA to undertake suitable independent study for efficient capital expenditure – For e.g., as done in the case of Kolkata Airport, with an intent to bring down the cost and reduce the ARR during 'True Ups' accordingly.

Comments of AAI

Further, O&M expenses i.e. payroll and R&M, AAI has saved under both the heads as projected in the Second Control period.

- The actual O&M Expenses i.e. payroll and R&M expenses of AAI for the 2nd Control Period have gone down in comparison to 2nd Control Period Order thereby resulting in savings as shown below:

In lakhs

Particulars	Approved in SCP	Submitted for True -up	Variation
Pay Roll Expenditure	18750.00	13853.85	4896.15
CHQ & RHQ Payroll exp.	2850.00	1892.16	957.84
R&M Expenditure	4180.00	3550.41	629.59

- The O&M expenses are incurred by AAI are based on operational requirements. The expenses are incurred after due diligence based on the powers given to various authorities, and there are also tendering processes for awarding the O&M contracts.

- Justification for the variation have been provided to the AERA consultant.

4. New Aeronautical Capital Additions and Total Aeronautical Capital additions proposed by AERA: (Para 4.2.1, 4.2.4, and Table 58, 65, 69 and 72 of the CP)

We appreciate that considering the reduced traffic owing to COVID-19, AERA has rationalized the capital expenditure and excluded certain proposed additions by Pune Airport to RAB.

We appreciate that AERA has pointed out the non-consideration of the GST on Baggage handling system and passenger boarding bridge, which will be available as GST credit of Rs. 926.27 lacs. We also note that non-allowance of Finance allowance of Rs. 3,333.57. These items themselves have a substantial impact on determination of the ARR and Tariff; at the same time, the Operator may kindly avoid such claims in the future, such that the estimations may be able to reflect the true picture.

Stoppage of Non-safety related capital expenditure: Pune Airport has proposed capex in the respective control period and postponing it to the next control period. Further, AERA acknowledged the effect of the pandemic in the Second Control Period on certain capital expenditure projects. It is pertinent to note that AERA has observed in other consultation papers that a delay in the capitalization of works would unfairly burden the airport users without passing on the benefits to them. As mentioned above it will take around two (2) -three (3) years for the flight operations to reach to its pre COVID-19 peak levels. In view of the above, in order to support the airlines to continue and sustain its operations, all non-essential capital expenditure proposed by Pune Airport be put on hold/ deferred, unless deemed critical from a safety or security compliance perspective. Further, in case Pune Airport wants to make capital expenditure, then it should be at no additional expense to the airlines until the project is completed and put to use by the airlines. Similarly, if any proposed Capex projects can be deferred from the Third Control Period to the Fourth Control Period, the same should be considered by AERA.

Comments of AAI

AAI vide e-mail dated 16.11.2021, informed AERA that AAI will claim input tax credit for PBB & BHS for proposed Terminal Building.

Direction 5 of AERA (which entails the methodology of aeronautical tariff determination) allows Airport operators to be eligible for Financing Allowance as a return on the value invested in construction phase of an asset including the Equity portion, before the Asset is put to use.

The concept of Financing Allowance, its computation and how the Work in Progress Asset includes the Financing Allowance is provided in Paragraph 5.2.7 of the Direction No.05-2010-11. Extract of the same is provided below:

"5.2.7. Work In Progress assets (a) Work in Progress Assets (WIPA) are such assets as have not been commissioned during a Tariff Year or Control period, as the case may be. Work in Progress assets shall be accounted for as:
WIPAt = WIPAt-1 + Capital expenditure + Financing allowance – Capital receipts of the nature of contributions from stakeholders (SC) - Commissioned Assets (CA)
Where:
WIPAt = Work in progress Assets at the end of Tariff Year t
WIPAt-1 = Work in progress Assets at the end of the Tariff Year t-1
Capital Expenditure= Expenditure on capital projects and capital items made during Tariff Year t.

The Financing allowance shall be calculated as follows:

$$\text{Financing Allowance} = R_d \times \left(\text{WIPA}_{t-1} + \frac{\text{Capex} - \text{SC} - \text{CA}}{2}\right)$$

Where
Rd is the cost of debt determined by AERA according to Clause 5.1.4.
SC are capital receipts of the nature of contribution from stakeholders (including capital grants and subsidies) pertaining to the capital expenditure incurred in Tariff year t.
CA are Commissioned Assets which pertain to the accumulated value of the WIPA attributable to all assets that have been put into effective operation during Tariff Year t.

- AERA has further provided an Illustration on Page 28 detailing the working. The extract of the illustration is as under:

Illustration 7: The following example illustrates this approach for calculation of Work in progress assets, financing allowance and commissioned assets. The numbers in the illustration have been rounded to the nearest integers.

Forecast Work in Progress Assets

		2010-11	Tariff Year 1	Tariff Year 2	Tariff Year 3	Tariff Year 4	Tariff Year 5
Opening WIP: $WIPA_{t-1}$	OW	-	-	-	558	638	-
Capital Expenditure	CE	-	833	521	-	-	-
Financing Allowance	FA = R_d x (OW+(CE-CA-SC)/2)	-	-	37	80	43	
Capital Receipts	SC	-	200	-	-	-	-
Commissioned Assets	CA	-	633	-	-	681	-
Closing WIP: $WIPA_t$	CW = OW + CE + FA - SC – CA	-	-	558	638	-	-

- *The cost of debt, R_d, used for calculation of financing allowance, is the cost of debt determined by the Authority under Clause 5.1.4.*
- *The example illustrates that those assets, which have been acquired or commissioned within the same Tariff Year (i.e. Tariff Year 1), have been included both in Capital Expenditure and Commissioned Assets.*
- *The value of commissioned assets, as calculated, shall be used for forecasting RAB for the Control Period.*

- Further, Para 5.2.5 of Direction No. 05 details the forecasting of RAB wherein the commissioned assets (including the Financing Allowance on the assets, when it was in Work in Progress stage) has been added to RAB and forms part of the closing and average RAB workings.

- The Illustration 4 in Page 23 is given below:

Forecast RAB

		2010-11	Tariff Year 1	Tariff Year 2	Tariff Year 3	Tariff Year 4	Tariff Year 5
Opening RAB_{t-1}	OR	22,750	20,500	18,826	16,462	13,998	12,277
Commissioned Assets	CA	-	633	-	-	681	-
Depreciation	DR	2,250	2,307	2,364	2,364	2,402	731
Disposals	Di	-	-	-	100	-	-
Incentive Adjustments	IA	-	-	-	-	-	-
Closing RAB_t	CR=OR+CA-DR-Di+IA	20,500	18,826	16,462	13,998	12,277	11,547
RAB for calculating ARR	RA=(OR+CR)/2		19,663	17,644	15,230	13,138	11,912

- The Clause (d) of Para 5.2.6 defines Commissioned Assets as below:

  "Commissioned Assets: Represents investments brought into use during Tariff Year t, consistent with Clause 5.2.7 herein below."

- Thus, from the above clauses it is clear that the Financing Allowance is computed on the Work in Progress balance based on Capital Expenditure incurred which is funded by Equity/Internal accruals and is capitalized as part of Commissioned assets for RAB Computation. In the case of AAI, financing allowance is computed on the equity portion and IDC is computed on the debt portion of the capital spend.
- Thus, Direction 5 provides an explicit, detailed elaboration of Financing allowance. Manner and formulae of computation and addition of the "commissioned assets" into RAB including the Financing allowance are elucidated in detail with examples is contained in the same Direction.

  The regulatory principles laid down by AERA and based on which the tariff orders are determined provide a fundamental foundation of the regulatory clarity to the stakeholders on the manner in which different components of costs and revenues are treated. Following are the examples and extracts of inclusion of financing allowance in RAB by AERA in various Orders:

- **CIAL TCP Order:** Vide para 4.4.52 of CIAL order for third control period, for true up of SCP, AERA noted that, in the tariff order for the SCP, it was decided that FA would be trued up based on the final capex. In its MYTP submission, CIAL had proposed an addition of Rs. 11.9 crores in FY 2021 only as Financing Allowance for true up of SCP. Accordingly, AERA recomputed FA based on actual WIP capitalized and allowed for inclusion in the Order.

- **BIAL TCP Order:** Vide para 3.3.78 of BIAL Order for the third control period, AERA has agreed to allow the financing allowance for the second control period.

- Financing allowance was approved and given by AERA in the First and Second Control period for BIAL and in second control period order of CIAL.

- **MIAL and DIAL:** It is further to be noted that MIAL and DIAL are governed by tariff determination principles set forth in SSA and OMDA. SSA and OMDA do not contain the concept of financing allowance. Hence, AAI submits that these 2 airports are not comparable with AAI airports.

AAI's Request

- The AERA Act requires AERA to consider *"timely investment in improvement of airport facilities";* and *"economic and viable operation of major airports"*. The statement of objects and reasons of the AERA Act requires Authority to encourage investment in airport facilities, create a level playing field and foster healthy competition. The Airports Infrastructure Policy of 1997 and NCAP 2016 also emphasize the need to provide a commercial orientation and encourage private sector participation in the airport sector.

- Financing allowance computation is fully in compliance with Direction 5, affirmed by Authority in its various Orders in the past.

- Based on the above submissions, AAI submits that by non-consideration of Financing allowance is not in line with AERA guidelines. Further, allowing Financing allowance for private airports and not for AAI airports vitiates the principle of laying a level playing field for all airports – public or private in India and AAI airports would be denied of revenues that they are rightfully entitled to.

- It is to be noted that AAI has started making capital expenditure for Construction of New integrated Terminal Building at Pune Airport from F.Y. 2018-19 whereas, AERA has mentioned that "Pune International Airport is a brownfield airport and has lower construction and traffic risk". The building will be completed in the F.Y. 2022-23 amounting to Rs. 500 crores (approximately). It includes both Term Loan and Internal accruals.

- AAI therefore requests AERA to consider the financing allowance of Rs. 2.12 crores computed for 2nd Control Period additions as well as for 3rd Control Period Capital additions. Further, AAI requests AERA to also consider these additions by way of financing allowance for depreciation computation and return on RAB accordingly.

Stoppage of Non-safety related capital expenditure:

The contract awarded to the agency is consolidated contract for NITB. Mobilizing material, Machinery, and labor after a break in construction is not feasible. There may be huge monetary escalations on material and labor costs. The Construction of a Terminal of this magnitude requires Specialized fabrications and skilled manpower. Bringing all the specialized agencies currently on board after a break may lead to coordination issues. There shall be contractual obligations, if the work is halted for more than the specified timelines in the contract.

As commented by FIA to capitalize only those costs pertaining to NITB being proportional to the usage area of NITB in the Third Control Period. It is submitted that all the functions are integrated at the proposed Terminal Building, so the entire cost to be capitalized in the 3rd Control period.

It is further submitted that AERA, in the Order No. 57/2020-21 for DIAL has analyzed as follows:

4.5.2 Authority has also examined the comments made by IATA, AOC, BAOA and the response to their comments by DIAL regarding the freeze and review of Expansion Capex. In this regard, Authority is in agreement with DIAL and BAOA that the expansion of airport should not be put on hold as the traffic for the airport is expected to reach the pre-COVID levels within the next two years and post the same is expected to follow the past growth trajectory which would require the presence of the added capacity expansion facilities for efficient and effective handling of traffic. Authority is of the view that the current Covid-19 pandemic which has resulted in a massive drop in traffic could be utilized to expedite the construction activities in the airport.

4.5.3 Authority is of the view that capex projects being long term in nature should not be withheld or suspended due to temporary phenomenon including the pandemic which is expected to not have a consistent long-lasting impact on the traffic in the long-term future. The necessity for capex for Phase 3A could be questioned if there is enough justification that the traffic handled pre-COVID shall never be achieved. However, such a prediction could mean that economic growth will also come to a halt in the future and will never be able to achieve the earlier achieved levels. As such a prediction cannot be justified, Authority considers that the capex schedule for Phase 3A expansion has to be considered with the necessary delays due to Covid-19 as submitted by the airport operator.

Authority would like to add that given the magnitude of the capex that is being undertaken by DIAL, mandating a complete freeze on all capex activities could indeed lead to a much higher escalation in costs associated with delay and could in the end lead to a much higher cost burden being passed on to the passengers. Authority has hence decided to consider the timelines as submitted by DIAL for the capex for Phase 3A expansion which have been assessed post impact of COVID pandemic.

AAI submits that the current dip in traffic is only a temporary phenomenon, and this should not affect the development of infrastructure to cater to anticipated growth for the future. AAI re-iterates that all infrastructure projects should aim at future proofing and should not be hindered by short term situations.

5. **Regarding Terminal Building Ratio and Actual Usage of Terminal Building:** (Refer 4 & 4.2.40, 4.2.23 of the CP)

AERA has sought stakeholders' views on the non-aeronautical component of the terminal building ratio (TBLR), as Pune Airport has proposed in the range of 5-7%, whereas AERA stated that this is in contrast to the 8-12% range as per IATA and IMG norms. AERA has proposed to consider a TBLR of 90:10 for the Third Control Period.

In our view, while we agree with AERA that the non-Aeronautical ratio proposed by Pune Airport is on the lower side, we request AERA to kindly undertake detailed scrutiny examination with the assistance of an independent study to be conducted on or before the tariff determination of the Third Control Period.

Furthermore, as per para 4.2.23, it is to be noted that as per submissions by AAI and considered by AERA, at the end of FY2022-23 the building will have the holding capacity of 19 MPPA, it further states due to Covid-19 there is fluctuation in the traffic and usage capacity of the building has changed from 47% to 59%. However, the entire cost of building has been capitalized in the Third Control Period. We would request AERA to capitalize only those costs pertaining to NITB being proportional to the usage area of NITB in the Third Control Period.

Comments of AAI

- AERA proposed to consider the ratio of 91.37% **:** 8.63% (Aero : Non-aero) for common assets within the Terminal building during the Second Control Period.
- AAI submits that the ratios submitted are based on actual floor space usage and considering the ratio of SCP i.e. 91.37% **:** 8.63% (Aero : Non-aero) by comparing with other airports/generally accepted ratios may not reflect the true ground scenario in Pune Airport.
- Detailed workings for all the aeronautical ratios applied for various assets was submitted during MYTP stage to AERA for its perusal.
- In SCP order, the ratio of 91.37% for TBLR was based on actuals of 2015-16. Same has submitted on actual basis for the period from 2016-17 to 2020-21.
- The design capacity for commercial activities at the existing Terminal Building comes out to 6% (approx.).
- Considering the fact that true up of the ratio, AAI has submitted the aero ratio working based on actual aero additions for SCP.
- The ratios have been computed based on the actual space in the terminals. Hence, AAI submits that assuming a different ratio based on international benchmarks when there is no substantial change in the terminal building composition during TCP may not be justified. AERA has

determined the Terminal Building ratio including proposed New Terminal Building as 91.37% in SCP. Now again in TCP, AERA proposes 90% as TBLR for the same Old Terminal Building.

- The earmarked area for commercial activities (design) for proposed Terminal Building works out to 8%
- It is requested to keep the same TBLR Ratio as approved in the SCP in order to maintain consistency and uniformity.
- As commented by FIA to capitalize only those costs pertaining to NITB being proportional to the usage area of NITB in the Third Control Period. It is submitted that all the functions are integrated at the proposed Terminal Building, so the entire cost to be capitalized in the 3rd Control period.

6. Fair Rate of Return (FRoR): (Refer 5.2.9 of the CP)

We appreciate that AERA has considered a lower FRoR of 11.63 %, which is net of income tax return to the airport operator, for the Third Control Period. However, while such fixed/ assured return favors the service provider, it creates an imbalance against the airlines, which are already suffering from huge losses and bear the adverse financial impact through higher tariffs.

Due to such fixed/assured returns, Airport Operators like Pune Airport have no incentive to look for productivity improvement or ways of increasing efficiencies, take steps to reduce costs as they are fully covered for all costs plus their hefty returns. Such a scenario breeds inefficiencies and higher costs, which are ultimately borne by airlines. In the present scenario any assured return on investment to any services providers like Pune Airport, in excess of three (3) % (including those on past orders), i.e., being at par with bank fixed deposits (i.e., return on investment after the income tax), will be onerous for the airlines.

Without prejudice to the above, in case AERA is unable to accept our recommendation mentioned above, it is requested to conduct an independent study for determination of FRoR to be provided to Pune Airport. Such independent study can be exercised by the powers conferred under the AERA Act and in line with studies being conducted by AERA in case of certain major airport operators.

Comments of AAI

AAI had appointed M/s KPMG to carry out a study on Cost of Equity during 2011 the results of which are given below:

Table 3: Beta of comparable airports

Airport / Group	Country	Equity Beta	Tax Rate	Debt (in Billion local currency)	Mkt Cap (in Billion local currency)	Debt /Mcap	Asset Beta
Airports of Thailand PCL	Thailand	1.14	30%	56.2	54.3	1.03	0.66
Beijing Capital International Airport	China	1.03	25%	18.5	14.8	1.25	0.53
Guangzhou Baiyun International Airport	China	0.91	25%	0.0	8.3	0.00	0.91
Shanghai International Airport	China	1.04	25%	2.5	22.0	0.11	0.96
Xiamen International Airport	China	0.95	25%	0.0	4.1	0.00	0.95
Grupo Aeroportuario del Sureste SAB de CV (Group of 9 airports in Mexico)	Mexico	0.94	30%	0.6	21.0	0.03	0.92
Grupo Aeroportuario del Pacifico SAB de CV	Mexico	0.84	30%	1.0	27.2	0.04	0.82
Grupo Aeroportuario Centro Norte, S.A. de C.V.	Mexico	0.99	30%	1.0	9.2	0.10	0.92

The median value of asset beta for the above comparable set is 0.92 which is being used as the asset beta for airport operations business of AAI. This needs to be re-levered as per the expected gearing of AAI in the control period to estimate the equity beta for AAI.

Table 4: Equity Beta for AAI

Estimated asset beta for AAI	0.92
Gearing for AAI	8.84%
Tax rate for AAI	32.45%
Equity beta for AAI	0.98

Equity beta for AAI works out to 0.98.

For full Report, please refer Consultation Paper No. 16/2012-13.

Based on the above report, AAI submitted during SCP consultation that the CoE was 16%. AERA in the SCP order had also considered CoE of 16% and since there was low debt, the FRoR was determined to be 14%. AAI submits that the debt was taken only during the end of FY 21 and hence, requests AERA to consider FRoR of 14% for SCP.

- The Equity estimation can also yield a range of values depending on the assumptions employed.
- Cost of Equity depends on ownership structure, Comparable Airports & Revenue Till
- Asset Beta plays an important role in determination of Equity Beta even if Debt/Equity Ratio is low (low gearing). Cost of Equity depends on both Asset Beta and Equity Beta.
- In 1st Control Period, AAI had submitted a study conducted by M/s KPMG in regards to calculation of Cost of Equity wherein, Estimated Asset Beta was 0.92 and corresponding Equity Beta works out to 0.98. The cost of Equity submitted by AAI works out to 16.82%
- If AERA considers the debt equity ratio as 48:52 as ideal ratio and provides Asset Beta @ 0.92 then the FRoR will increase to more than 16%.

- In MIAL, DIAL, HIAL and CIAL the Cost of Equity has been considered @ 15+%. Thus AERA is requested to consider the Cost of Equity @ 16% as submitted by AAI.

- AAI had requested AERA to consider the FRoR as submitted instead of an Average FRoR @ 11.63% for TCP.

AAI hence submits that not having a leveraged financing structure has already been factored by AAI by considering an FRoR of 14%. Further, suggesting that a return equal to interest rate of bank to be applied does not factor in the risks associated with the aviation business and more specifically the uncertainties in this current pandemic scenario.

7. **Operating and Maintenance Expenses:** (Refer 2.8.42, 6.2, 6.2.2 and Table 44, 89 & 90 of the CP)

As per para 2.8.42 & Table 44, AERA has raised concerns regarding the inefficiencies and high cost of O&M expenses and directed AAI to lower their Aeronautical Operating & Maintenance expenses for the Second Control Period. However, as seen from Para 6.2.21 & table 90, despite the directions of AERA we observe that there is further increase in proposed O&M expenditure for Third Control Period.

We are unaware as to whether Pune Airport has taken cost cutting measures including re-negotiations of all the cost items on its profit and loss account. It may be noted that cost incurred by Pune Airport impacts the airlines, as such most of the cost is passed through or borne by the airlines.

In view of the above, we request AERA should:

- Put on hold any increase in operational expenditure by Pune Airport;
- Advise Pune Airport to review its spending on operational expenditure and re-negotiate all the operational expenditure costs in a significant manner and address any increase in fees sought by Pune Airport. It may be noted that across various industries, instead of cost escalations, all the costs have been renegotiated downwards substantially. Accordingly, Pune Airport needs to significantly reduce all such costs in a very aggressive manner. Pune Airport may be advised to reduce its cost by at least 35% and no escalation should be permitted; and In view of the above, Pune Airport should be directed to pass on cost benefits to the airlines.
- In particular, we submit that:

i. Expenses on account of CSR as given in table 43 of Consultation paper may be excluded. This will be in line with the similar treatment to CSR expenditure, given to CIAL at Cochin International Airport.

ii. Y-O-Y increase in the O&M expenses proposed by Pune Airport is approximately 4% to 7%. Instead of a significant reduction in cost items of operating expenses, AERA has proposed a Y-O-Y percentage increase of around 3% to 5% between 2022 and 2026. Such an increase in the name of escalation, in a highly uncertain environment, where airlines are operating under curtailed operations, appears to be without any rationale and should be avoided.

iii. **Payroll Cost:**

Although the activity level has gone down drastically, rather than significant reduction in the cost, the employee expenses as proposed by AERA are to increase Y-O-Y each year by 3% over the five (5) year control period.

We submit that while the aviation sector, including airlines, have incurred huge losses and are struggling to meet their operational costs, the Pune Airport on the other hand seems to have paid/will pay incremental salaries which may not appear prudent considering the significant losses incurred by the aviation sector. It appears that Pune Airport wants to recover its full employee cost from the airlines, which are facing significant challenges to meet its operating expenses.

We submit that there should not be any increase in manpower till the existing manpower is effectively utilized as it will take another two (2)- three (3) years to recover. Existing manpower can be reviewed and any additional costs due to contract manpower or otherwise should be reduced.

Comments of AAI

At Pune Airport, in 3rd Control Period, two Terminal Buildings (i.e. Old Terminal Building and Proposed New Integrated Terminal Building) would be there. Obviously, the operational cost would increase in 3rd Control Period. The costs to run the airports are mostly fixed and as per operational requirements.

- **R&M Expenses:** There are various heads of R&M expenses which are incurred for Operational Requirements, Regular maintenance of the airport infrastructure and equipment at the airport.

- The costs captured by the airports in their respective trial balances are based on the actual spend. To determine the costs, there are detailed tendering mechanisms for every contract and approving authorities. Further, the airports are subject to C&AG audit on a yearly basis

- AERA in the SCP has approved Rs. 41.80 Crores for R&M Expenses Whereas, AAI has submitted for true-up of SCP expenses amounting to Rs. 35.28 (includes F.Y. 2020-21 projections). Thus, there is a saving of Rs. 5.5 crores for the SCP true-up.

ACTUAL REPAIR & MAINTENANCE EXPENSES FOR THE SCP

Amt. in Lakhs

GL Code & Name		F.Y. 2016-17	F.Y. 2017-18	F.Y. 2018-19	F.Y. 2019-20	F.Y. 2020-21
OAAI/731001000	R & M Civil Runways	11.44				
OAAI/731002000	R&M-Civil T/w, Aprons	114.19	0.07	0.12		
OAAI/731003000	R&M-TB & Other Buildings	140.86	130.79	69.20	107.18	127.86
OAAI/731004000	R&M-Cargo Bldg.	5.76				
OAAI/731006000	R&M-Other Building	3.19	0.13			0.00
OAAI/731008000	R&M-Fencing, B/w	6.64				
OAAI/731009000	R & M: Civil:General	126.23	180.38	67.15	13.73	-0.91
OAAI/731010000	R&M:Road & Culverts	7.54				
OAAI/731011000	R & M: Spl Repairs			0.11		
Sub-total		**415.84**	**311.38**	**136.58**	**120.90**	**126.95**
OAAI/731101000	R&M-A/C EQPt	59.29	46.62	82.98	135.59	148.40
OAAI/731102000	R&M:POWR SU.&GEN.SET	3.48	5.96	4.20	3.65	8.83
OAAI/731103000	R&M-GRND LIGHT	7.95				
OAAI/731104000	R & M: ELEC. INSTAL.	80.47	95.55	74.79	90.41	134.75
OAAI/731105000	R & M: ELEC.:OTHERS	48.54	7.07	36.22	39.20	68.67
OAAI/731106000	R & M: Spl Repairs	0.00		0.03		
Sub-total		**199.73**	**155.20**	**198.21**	**268.86**	**360.65**
OAAI/731206000	R & M: FF VEH.& EQPT	0.00		0.62	25.97	4.44
OAAI/731207000	R & M: VEHICLE:OTHER	2.20	0.72	0.93	0.72	0.48
OAAI/731209000	R&M-Te.MT.Fire.S.Rep			0.03		
Sub-total		**2.20**	**0.72**	**1.58**	**26.69**	**4.92**
OAAI/731302000	R & M: F&F-T.Bldg				1.09	2.95
Sub-total		**0.00**	**0.00**	**0.00**	**1.09**	**2.95**

OAAI/731401000	R&M:- Surveillance Eq	2.49		8.55	13.05	21.30
OAAI/731402000	R&M-Comm. Eqpts	1.50	1.19	4.67	2.98	2.32
OAAI/731406000	R&M:-Facil.Eqpts					0.48
OAAI/731407000	R&M-Sec.Eqpts.	6.95	16.13	5.08	0.35	0.71
OAAI/731407005	R&M BOT XBIS LEASE		24.40	68.83	2.26	
OAAI/731407010	R&M-Electron-Spl Rep	1.82	1.58	2.25	3.11	0.91
OAAI/731409000	R&M-Other CNS Eqpt	0.67	0.69	0.74		1.01
OAAI/731501000	R&M: COMP., IT H/W	10.19	21.83	22.39	35.56	37.69
OAAI/733001000	AOCC Expenses	170.40	212.62	170.04	169.19	170.04
Sub-total		**194.03**	**278.43**	**282.54**	**226.51**	**234.44**
Grand Total		**811.80**	**745.74**	**618.91**	**644.05**	**729.91**

Note: *Table contains actual figures for the F.Y. 2020-21 submitted to AERA vide e-mail dated 24.12.2021*

- Pune Airport is more than 40 Years old. Terminal Building expansion was in two phases, 1st phase during 2006 and then in 2010. Old Apron expansion was in two phases, first in 2007 and then in 2008. New Apron is constructed in 2018 for which no maintenance work other than Apron markings is done till date. The assets are very old and warranty period got over within one year of construction i.e. almost 10 years back from the beginning of second control period.

- AAI submits that with ageing of the building and associated equipment, the R&M will only increase over the years. Applying a ratio on the depreciated WDV will further reduce the cost whereas the reality is that the costs will only increase over the years to make good the wear and tear over the years.

- Every station of AAI is subject to C&AG audit on a yearly basis. Hence, the costs captured by the airports in their respective trial balances are based on the actual spend.
- AAI requests AERA to consider the actual costs incurred for the second control period without restricting it to 6% on opening Net RAB.

- Basis of considering 6% on opening RAB of TCP has not been provided in the CP

- AAI requests AERA to consider the projected costs for TCP without restricting it to 6% on opening RAB of the TCP. Moreover, applying a ratio on the depreciated WDV will further reduce the cost whereas the reality is that the costs will only increase over the years to make good the wear and tear over the years.

- It has been observed that AERA has not considered Digi yatra Opex expenses from F.Y. 2023-24 onwards.

- AERA notes that Civil R&M costs are not likely to incur for new Terminal Building for 1 to 2 years. AAI submits Defect Liability period for the proposed Terminal Building is only for 1 year. It is requested to consider AMC of Civil work of New terminal building.

- AAI request to consider other regular R&M increase by 10% from F.Y 2023-24 onwards as proposed by AAI.

- **CSR:** In accordance with the requirements of the DPE guidelines on CSR and Sustainability and Section 135 of the Companies Act, 2013, two percent of the average net profits (to be calculated in accordance with the provisions of the Act) during the three immediately preceding financial years will be allocated for CSR activities every year.

- AAI has constituted a CSR Committee. The composition and terms of reference of the CSR Committee is provided in the Report on Corporate Governance, which forms part of this Annual Report. AAI has also formulated a Corporate Social Responsibility Policy, which is available on AAI's website.

- The overview of various CSR projects and programme undertaken by AAI and detail amount spent on CSR across India in different projects are there in the Annual Report at AAI website.

- CSR Budget will be utilized for implementing CSR projects approved by the Board on an annual basis. The budget allocation to the CSR Schemes shall be made in the beginning of every financial year after considering the CSR budget for that year. AAI is committed to play a larger role in India's sustainable development by embedding wider economic, social and environmental objectives.

- CSR provisions are made on the basis of 2% of Average profits of preceding 3 financial years at Corporate Headquarter Level.

- CSR calculation for 2nd control period of Pune Airport has been carried out on the basis of Aeronautical and Non-Aeronautical Revenue for the F.Y. 2013-14, 2014-15 & 2015-16 (Single Till basis) whereas, Hybrid Till i.e. 30% of the Non-aeronautical Revenue has been considered w.e.f. 2016-17 onwards.

- In case of Pune Airport, the CSR amount to be reimbursed are as under:

Statement of Calculations for CSR Expenditure in respect of PUNE Airport									In Lakhs
Particulars	**2013-14**	**2014-15**	**2015-16**	**2016-17**	**2017-18**	**2018-19**	**2019-20**	**2020-21**	**Total**
Revenue from Regulated Services (a)	2310.00	2620.00	3330.00	4124.07	8147.45	18810.78	17504.58	4800.08	
Revenue from Non-Aeronautical Services 30% (b)	2130.00	1820.00	2160.00	918.20	1048.48	2029.85	1840.48	664.65	
Operating Expenditure (other than CSR included in Admin & Gen Expenses) (c)	4730.00	4960.00	5270.00	5882.78	7705.50	9875.43	10345.46	9542.11	
Working Capital Interest (d)	-	-	-	-	-	-	-	-	
Depreciation (e)	310.00	690.00	760.00	713.86	709.07	795.93	941.13	1118.29	
Total Expenditure (c)+(d) +(f) = (f)	5040.00	5650.00	6030.00	6596.64	8414.57	10671.35	11286.59	10660.40	
Regulatory operating Profit before tax (a+b)-(f) = (g)	-600.00	-1210.00	-540.00	-1554.36	781.35	10169.27	8058.47	-5195.67	
Average of previous 3 FY's Aeronautical profits (h)				-783.33	-1101.45	-437.67	3132.09	6336.36	
2.00% of the average PBT (mandatory spend) (i=2%*h)							62.64	126.73	**189.37**
Actual Amount Spent on CSR Activities				10.67	21.78	115.4	59.99	59.99	**267.84**
NOTE: In the F.Y. 2013-14, 2014-15 & 2015-16 Tariff was determined on the basis of Single Till, therefore 100% Non-Aero Revenue considered for these Years. From F.Y. 2016-17 onwards Hybrid Till is considered.									

On the basis of the above statement, an amount of Rs. 189.37 Lakhs is required to be reimbursed by AERA for Pune Airport as AAI has incurred expenditure on account of CSR as per the provisions of Section 135 of the Act, the Companies (CSR Policy) Rules, 2014 and the DPE Guidelines, 2014.

AAI as a whole has incurred CSR Expenses from F.Y. 2016-17 to 2020-21 are as under:

In Crores

Particulars	2016-17	2017-18	2018-19	2019-20	2020-21
CSR Expenses	60.19	71.91	83.79	125.70	40.23

In view of above, like income tax reimbursement it is requested to reimburse an amount of Rs 189.37 lakhs for Pune Airport during 2nd control period on account of CSR Expenditure.

Upkeep Expenses: The upkeep expenses merely not linked with the area of building but there are other factors like cleaning with modern and high technology equipment, wages of the labor, escalations in the prices of the materials, cleaning of Transparent Glass Facades, Ceilings, Covid-19 protocols etc. The minimum wages of labor plays an important role in deciding the upkeep expenses at airport.

Therefore, AAI requests AERA to allow the expenditure as submitted by AAI instead of restricting it to inflation of 4.9% from F.Y. 2021-22 and thereafter.

Payroll Cost: 7% is the average increase in the payroll due to annual increment of 3% in salary, increase in HRA, and quarterly increase in DA and Employer contribution to PF. The figures for the F.Y. 2020-21 are actual as submitted by on 24.12.2021

- The following illustration clearly shows that there is an average 7% increase in the Payroll expenditure.

Calculation of incremental increase in Salary (in %age terms)

Particulars	Per Month	Salary Year 1	Q1	Q2	Q3	Q4	Salary Year 2	(In Rs.) Yearly Incremental
Basic Pay	10000	120000	30900	30900	30900	30900	123600	3600
DA	1800	21600	6798	7725	8343	8652	31518	9918
HRA	2700	32400	8343	8343	8343	8343	33372	972
PERKS	3500	42000	10815	10815	10815	10815	43260	1260
EPF	1200	14400	3708	3708	3708	3708	14832	432
Total	**19200**	**230400**	**60564**	**61491**	**62109**	**62418**	**246582**	**16182**

Particular	**%age Increase**					
DA	18%		22%	25%	27%	28%
HRA	27%		27%	27%	27%	27%
Perks	35%		35%	35%	35%	35%
EPF	12%		12%	12%	12%	12%

Total Increase (in Rs.)	**16182**
% increase	**7.02**

- ***Assumptions :***
- Year 1 Means Previous Year
- Year 2 Means Current Year
- Basic Pay – 3% yearly increase considered.
- Dearness Allowance- Quarterly increase considered.
- HRA, Perks & EPF – Considered Constant
- In the above mentioned example, the Salary expenditure for Year 1 shown as Rs. 230400/- per employee. Whereas, in the year 2 the salary expenditure is shown as Rs. 246582/- per employee. On the basis of above assumptions, the incremental expenditure on the head of salary is Rs. 16182/- per employee which comes out to 7.02% on Year on Year basis.

8. Non-Aeronautical Revenue: (Refer 7.2.11 and Table 95 of the CP)

We request AERA to kindly undertake a detailed scrutiny examination with the assistance of an independent study to be conducted on the non-aeronautical revenue before the tariff determination of the Third Control Period, as we are of the view that the low figures of Pune are conservative. It is further requested that Pune Airport explores all avenues to maximize revenue from the utilization of terminal building (including NITB) for non-aeronautical purposes, as deemed fit.

Without prejudice to the above, our submission is that increase in non-aeronautical revenue is a function of passenger traffic growth, inflationary increase, and real increase/escalations in contract rates. AERA is requested to ensure no adjustments are proposed to non-aeronautical revenue which is not dependent on traffic but are derived from agreements with concessionaires.

Royalty:

Any attempt to award the contracts by the airport operator on the highest revenue share basis should be discouraged as it breeds inefficiencies and tends to disproportionately increase the cost. It is general perception service providers have no incentive to reduce its expenses as any such increase will be passed on to the airlines through tariff determination mechanism process and indirectly airlines will be forced to bear these additional costs. There needs to be a mechanism for incentivizing the parties for increasing efficiencies and cost savings and not for increasing the royalty for the airport operator.

As you are aware, royalty is in the nature of market access fee, charged (by any name or description) by the Airport operator under various headings without any underlying services. These charges are passed on to the airlines by the airport operator or other services providers.

The rates of royalty at Pune airport are as high as up to 1315% for some services. It may be pertinent to note that market access fee by any name or description is not practiced in most of the global economies, including European Union, Australia etc. Sometimes it is argued by the airport operators that 'Royalty' on 'Aeronautical Revenues' helps in subsidizing the aero charges for the airlines, however royalty in 'Non-Aeronautical Revenues' hits the airlines directly without any benefit.

In view of the above, we urge AERA to abolish such royalty which may be included in any of the cost items.

Comments of AAI

- Generally, increase in traffic is not proportionate with increase in NAR.
- It is to mention that in view of Covid-19 pandemic, AAI had provided Concessionaire Support Scheme (CSS) to various contractors linked to the passenger traffic till 31/12/2021. Under the CSS, license/concession fee was charged based on actual passenger traffic during a particular month. In addition, additional discount was also given due to adverse impact on buying behaviour of the passenger.
- In view of the above, revenue growth after 31/12/2021 is not to be linked with passenger traffic growth. Most of the commercial contracts have been awarded by AAI on fixed license fee basis having annual escalation provision of 10%. Therefore, AAI projections are based on the consistent revenue increment trend during pre- Covid years
- Hence, projections from FY 2022-23 onwards should be delinked with total traffic numbers and AAI circulars 24&26. Further, in the revenue projection for FY 2021-22, additional discount provided under CSS in license fee due to adverse impact on passenger buying behaviour has also to be factored in.

- AAI has provided same rate for Rent & Services to Airlines for the F.Y. 2020-21 as per rates of F.Y. 2019-20. Further, for 2020-21 the rates of Rent & Services has been reduced by 8% for AC and 20% for Non-AC.

- **Royalty:** AAI has initiated tender as per the terms and conditions, period of license etc., mentioned in line with the AAI commercial manual. Commercial Department is collecting 13% of GTO from Inflight Caterers for doing business at Airport. Collection of 13% royalty from Inflight catering service provider is prevailing in all the AAI managed Airports as per the internal policy.
- AAI is incurring huge expenditure on providing the infrastructure to facilitate the Ground Handling Agencies for providing their services to the airlines. Further, the royalty on Ground handling charges (Revenue Share) payable by Ground Handling Agency has been brought down to 3% of Actual Gross Revenue from Scheduled Domestic Passenger Flights and 15% of Actual Gross Revenue from users other than Scheduled Domestic Passenger Flights and RCS flights. This is effective from 1st October 2021.

9. Application of 'Single Till'

FIA submits that in Para 1.2.2 & 2.4.3 Consultation Paper, it is stated that the AERA shall determine tariffs for using the 30% Hybrid Till model including for true ups as applicable. It is to be noted that the Federation of Indian Airlines has from time to time advocated the application of a Single Till model across the airports in India. FIA submits that AERA should adopt Single Till basis across all Control Periods, including by way of true up, in view of the following legal framework:

In the Single Till Order, AERA has strongly made a case in favor of the determination of tariff on the basis of 'Single Till'. It is noteworthy that the AERA has, inter alia, in its Single Till Order:

(i) Comprehensively evaluated the economic model and realities of the airport – both capital and revenue elements.

(ii) Considered the legislative intent behind Section 13(1)(a)(v) of the AERA Act.

(iii) Concluded that the 'Single Till' is the most appropriate for the economic regulation of major airports in India.

(iv) The criteria for determining tariff after considering standards followed by several international airports (United Kingdom, Australia, Ireland and South Africa) and prescribed by ICAO.

(v) Further, AERA in its AERA Guidelines (Clause 4.3) has followed the 'Single Till' approach while laying down the procedure for determination of ARR for Regulated Services.

(vi) The fundamental reasoning behind the 'Single Till' approach is that if the consumers/passengers are offered cheaper airfares on account of lower airport charges, the volume of passengers is bound to increase leading to more footfall and probability of higher non-aeronautical revenue.

(vii) The benefit of such non aeronautical revenue should be passed on to consumers/passengers and that can be assured only by way of lower aeronautical charges. It is a productive chain reaction which needs to be considered by the AERA.

Comments of AAI

As per National Civil Aviation Policy 2016 [Page17 para-c] *"to ensure uniformity and level playing field across various operators, future tariffs at all airports will be calculated on a 'hybrid till' basis, unless otherwise specified for any project being bid out in future. 30% of non-aeronautical revenue will be used to cross-subsidise aeronautical charges. In case the tariff in one particular year or contractual period turns out to be excessive, the airport operator and regulator will explore ways to keep the tariff reasonable, and spread the excess amount over the future".*
AAI has prepared MYTP on Hybrid Till Basis and AERA has considered it.

AERA may also offer its views.

10. Tariff/Government Restrictions: (Refer 12.2.4 and 12.2.5, 15.2 Annexure II of the CP)

i. **Overall Tariff:**
While AERA has proposed a decrease of approx.15 % in the Parking Charges and UDF for the aforementioned charges. However, keeping in view the adverse impact caused to the airline due to the COVID-19 pandemic, we are of the view that there should be a further reduction in the existing charges, considering our submissions & recommendation mentioned above, we can bring the tariff levels down. AERA may appreciate that it is in the interest of all stakeholders to reduce tariffs in order to encourage middle class people to travel by air, which will help in sharp post-COVID-19 recovery of aviation sector.

ii. **UDF Charges:**
As per para 15.2.2, Annexure - II of the Consultation Paper, rate of collection of UDF charges has not been clarified. We understand that such rate of Collection Charges (being clarified in other Consultation Papers is Rs. 5 (Rupees five only) per departing passenger. We request that the same is clarified in the Tariff Order for Pune Airport. We further request that the Collection Charges, the entitlement for airlines, should be against AAI having received the 'undisputed' invoiced UDF amount with the applicable due date.

Comments of AAI

Overall Tariff: The financial condition of AAI during the Covid-19 Pandemic has deteriorated to a great extent. AAI has incurred a loss of Rs. 1962 Crores (approx.) in F.Y. 2020-21. AAI has resorted to borrowing from market to finance its capital as well as opex. Although it is expected that the Aviation sector is likely to bounce back to Pre-Covid level by F.Y. 2023-24, yet for AAI's current survival, it is required to improve cash flows. Under the present situation there is no hope to augment Non-aeronautical revenue.

Collection Charges: Policy referred to with respect to collection charges: Rs.5/- plus GST per passenger will be paid by AAI to the Airline Operators if they make the payment within 15 days from the receipt of the invoice. No collection charges shall be paid in case the airline fails to pay the UDF invoice to AAI within the credit period of 15 days or in case of any part payment. This is as per the Credit Policy of AAI which has been provided in the tariff card by AERA.