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Director Policy & Statistics
Airports Economic Regulatory Authority of India
AERA Building, Administrative Complex
Safdarjung Airport
New Delhi – 110003

Via email: director-ps@aera.gov.in; rajan.gupta1@aera.gov.in; secretary@aera.gov.in

Dear Sir,

IATA COMMENTS ON AERA'S CONSULTATION PAPER FOR THE DETERMINATION OF AERONAUTICAL TARIFFS FOR CHAUDHARY CHARAN SINGH INTERNATIONAL AIRPORT, LUCKNOW (LKO) IN THE THIRD CONTROL PERIOD

The International Air Transport Association (IATA) is the trade association for the world's airlines, representing some 300 airlines or 83% of the world's air traffic. Many of our member airlines operate in the Indian market including Air India, IndiGo, SpiceJet and Vistara. We support many areas of aviation activity and help formulate industry policy on critical aviation issues.

India is one of the fastest growing aviation markets in the world. With plans for privatization of more airports, the importance of the role of AERA as the independent economic regulator cannot be understated. Economic regulator should be supported, strengthened and empowered to drive the optimal outcome in the long term for aviation industry and the Indian's economy at large.

IATA commends AERA for the close scrutiny of the proposal put forward by the Airport Operator (AO) where a number of issues were identified and corrected by AERA, such as the asset and cost allocations, revenue estimates and returns proposed/claimed by the AO.

Similar to the situation with AMD, the approach by the Adani Group as the operator at LKO has introduced new challenges and revealed some gaps in the regulatory approach which IATA will highlight in this submission for consideration by AERA.

True Up of AAI and AO for the 2nd Control Period

- IATA maintains our view that the FROR of 14% is on the higher side and does not reflect the business risk assumed by AAI, given the true-up approach adopted by AERA. This is even more so as the industry was impacted by the COVID19 pandemic, whereby it would be expected that the allowable returns be lowered, especially in FY20/21.

- IATA agrees with removing the burden of interest & penalties, due to lapses on the part of the Operator.
- Regarding point 4.5.8 (Reclassification of assets transferred by AAI to the Airport Operator), we appreciate AERA for enforcing the separation of costs associated with non-airport services such as ANS and adjusting the allocation of the assets accordingly.
- We note AERA's proposal about not including land in the true-up calculation, and disallowing the same being claimed by AAI as part of true up of the pre-COD period. We agree with this, as well as the proposal to disallow the pre-COVID losses from the true-up. We also agree with AERA's proposal to rationalise the CHQ/RHQ expenses. However, we would like to highlight that the expenses that were allowed under this head in the 2nd control period was Rs. 71.2 Cr. Therefore, the same should be allowed, and not Rs. 198 Cr, as done in the current CP.
- In context of the green energy initiatives cost/investment mentioned in the point 4.5.6, we would like to share the position paper developed by IATA on [Airport Environmental Sustainability](#).

Traffic Projections for the 3rd Control Period

- We agree with AERA's assessment of traffic projections based on the available facts and analysis, expecting recovery to pre-covid levels of domestic traffic by FY2022-2023 and international traffic by FY2023-2024.

CAPEX

- IATA supports the proposed reduction of 1% of uncapped project costs from the ARR, by AERA.
- With regard to procurement and award of capital projects at LKO, IATA would like to recommend that the AO must also include disclosures on related-party transactions. The independent studies too should focus on related party transactions within the group; ensuring that the award of projects has been through competitive bidding, and does not suffer from restrictive terms or cost escalations that may arise from awards to related parties.
- IATA agrees with disallowing the significantly high quotes of the AO for artworks, landscaping; and also rationalizing the cost of drainage works.
- AERA has also proposed that the Phase II of the integrated T3 project should be commissioned during the next Control period; as well as its proposal to derive the cost of T3 project based on the Normative Approach to ensure that the overall cost is reasonable. This is in line with IATA's views during the AUCC meeting that was held in Jul-2021; and IATA fully supports this.

FROR

The CP brings focus on many pertinent issues such as the higher cost of debt associated with the AO's borrowings and inter-corporate deposits from related parties within the same shareholder group.

- We agree with AERA treating the cost of debt in line with average cost of debt of other PPP airports. We also agree with the cost of equity being pegged at 15.18% for the 3rd control period based on independent studies for other PPP airports.
- We believe that the AO has to work on delivering value on lowering all of the components that make up the FROR i.e. the cost of equity; cost of debt; and the debt to equity gearing.

O&M

- We commend AERA for leveraging on the independent studies such as for O&M expenses, which demonstrates that very close scrutiny is needed to ensure that all allocations are done accurately; and reflect the required efficiency level as expected from a private airport operator.
- IATA supports AERA's decision on the expectation to optimize O&M expenditure over a period of time. We believe that there is room for greater rationalization of not just O&M expenses with the transition from AAI to the new private airport operator. This will be in line with the objective of the privatization delivering greater efficiency in the management of the airport.
- There were high annual increases proposed by the AO, with employee cost projected increases of 15% YoY, & significant increase in head count in the 3rd Control period. These have been rightfully adjusted in its proposal by AERA.

Non-Aeronautical Revenue (NAR)

As in the case of Ahmedabad airport tariff proposals, we are concerned that the NAR which is meant to cross-subsidize the Aeronautical charges, are clearly under-developed and under-projected in the case of LKO airport as well. AERA has correctly highlighted that the NAR projected is lower than when the airport was under AAI; and that the increase in non-aero activities with the terminal expansion has not been factored in; especially given that the traffic growth of over 20% is expected, as mentioned in the presentation by AO at the time of stakeholder consultation. We appreciate AERA for closely overseeing this aspect.

- Additionally, as mentioned in AERA's current Consultation Paper for the Lucknow airport, the AO has entered into a Master Services Agreement (MSA) with Adani Airport Holdings, which is supposed to pay the AO a minimum guarantee amount of Rs. 22 Cr or 10% of the 'Gross Revenue', whichever is higher.
 - The 'Gross Revenue' referred to in the MSA is in fact the NAR of the airport – and under the hybrid till mechanism, 30% (and not 10%, or even an absolute amount of Rs 22 Cr) of the NAR is to be used to offset aeronautical costs.

- While the AO's submission makes a mention of 'Revenue from Master Service Agreement', the component necessary for tariff determination purposes has to be 30% of total NAR; and not 30% of the 10% MSA Revenue Share (30% of 10% of total NAR is in fact only 3% of the total NAR earned).
- The current arrangement of including a Master Concessionaire between the NAR flowing to the AO, significantly reduces the level of effective NAR for the tariff determination by AERA and cannot be justified.
- IATA urges the Authority to correct the AO's understanding by explicitly stating/confirming in the final Order that: i). 30% (in adherence to the hybrid till policy, and not any lower) of the total NAR of the Airport is to be recognized in offsetting aeronautical costs; and ii). the level of 'Revenue from Master Service Agreement' earned by the AO is not material to tariff determination. This will help bring back the NAR from its current artificially low levels in the airport's current understanding.
- IATA would expect that any shortfall in the NAR will NOT be trued up in the next control period.

Tariff Card

- We notice the significant increase that has been proposed by the AO in its Tariff card, both on landing & parking charges, as well as significant hike in User Development Fees.
- We request that AERA adopts the same approach as in the determination for other airports by moderating the increases to facilitate a recovery in traffic and consider a significant reduction in the Airport's current proposal for landing & parking and UDF charges.
- In the case of Lucknow airport, given that the Phase II of T3 goes to the next Control period, IATA recommends that part of the ARR recovery should be carried forward to the 4th Control period.

IATA appreciates the opportunity to provide our comments to AERA on behalf of our member airlines. Feel free to contact us should further clarification is needed.

Yours Sincerely,



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cc. Richard Tan, IATA Regional Manager Operations, Safety and Security – Asia Pacific