



Association of Private Airport Operators (APAO)

Response to AERA's Consultation Paper No. 22/2013-14 dated 24th January 2014 addendum to Consultation Paper No. 14/2013-14 on determination of Tariffs for Aeronautical Services in respect of Kempegowda International Airport, Bengaluru for the first control period (01.04.2011 – 31.03.2016)

10th March 2014

TABLE OF CONTENTS

1.	INTRODUCTION	3
1.1.	AIRPORTS ECONOMIC REGULATORY AUTHORITY OF INDIA	3
1.2.	STAKEHOLDER CONSULTATIONS	3
1.3.	ISSUANCE OF ADDENDUM TO THE CONSULTATION PAPER FOR BENGALURU INTERNATIONAL AIRPORT, BENGALURU, INDIA	3
2.	SPECIFIC ISSUES RELATED TO BIA	4
2.1.	REGULATORY TILL	4
2.2.	REGULATORY ASSET BASE (RAB) AND TREATMENT OF LAND / REAL ESTATE	7
2.3.	COST OF EQUITY CALCULATION	8
2.4.	OTHERS	11
2.4.1.	QUALITY OF SERVICE REBATE	11
2.4.2.	FUEL THROUGHPUT FEE	11
2.4.3.	CARGO AND GROUND HANDLING SERVICES	11
3.	CONCLUSIONS	13

1. INTRODUCTION

1.1. Airports Economic Regulatory Authority of India

The Airports Economic Regulatory Authority of India (AERA or the Authority) was established pursuant to the enactment of the Airports Economic Regulatory Authority of India Act, 2008 (the Act), to perform the following functions for major airports:

- 1 Determine tariff for aeronautical services
- 2 Determine the amount of the development fee including the User Development Fee (UDF)
- 3 Determine the Passenger Service Fee (PSF)
- 4 Monitor the set performance standards relating to the quality, continuity and reliability of service as may be specified by the Government of India or any authority authorized by it in this behalf.

1.2. Stakeholder Consultations

Section 13(4) of the Act states that the Authority shall ensure transparency while exercising its powers and discharging its functions

- (a) by holding due consultations with all stake-holders with the airport
- (b) by allowing all stake-holders to make their submissions to the Authority; and
- (c) by making all decisions of the Authority fully documented and explained

1.3. Issuance of Addendum to the Consultation Paper for Bengaluru International Airport, Bengaluru, India

As part of the stakeholder consultation referred to in Section 1.2, the Authority had issued Consultation Paper No.14/2013-14 dated June 26, 2013 (Consultation Paper No.14) on determination of aeronautical tariffs in respect of Bengaluru International Airport (BIA or the Airport), Bengaluru, India for the first control period April 1, 2011- March 31, 2016. The Association of Private Airport Operators (APAO) had submitted its written responses to the key issues arising from Consultation Paper No.14 on September 19, 2013.

Subsequently, the Authority issued Consultation Paper No.22/2013-14 dated January 24, 2014 (Consultation Paper No.22) as an addendum to Consultation Paper No.14/2013-14 dated June 26, 2013. The Authority had sought *written evidence-based feedback, comments and suggestions from the stakeholders* by February 17, 2014. The Authority, by issuance of Public Notice No.14/2013-14 dated February 17, 2014, extended the last date for submission of comments to February 28, 2014.

This Revised Report includes LeighFisher's responses on behalf of APAO to the key issues arising from the Consultation Paper No.22 on behalf of the stake-holders represented by APAO.

2. SPECIFIC ISSUES RELATED TO BIA

2.1. Regulatory Till

As per Consultation Paper No.14, the Authority had sought to determine the aeronautical tariffs in respect of the Airport under Single Till. This recommendation was in accordance with the Order No.13/2010-11 dated January 12, 2011 (the Order) which laid down the regulatory philosophy and approach to the economic regulation of airport operators. The Authority had taken into consideration the following:

- (a) Concession agreement contemplated dual till
- (b) International Civil Aviation Organization (ICAO) policies on economic regulation
- (c) Provisions of the AERA Act, 2008
- (d) Planning Commission view on the choice of till

As stated in paragraph 1.8 of the Consultation Paper No.22, Bangalore International Airport Limited [BIAL] wrote a letter dated July 30, 2013 to the Authority in response to Consultation Paper No.14 in which it stated as follows:

"As you are kindly aware, while submitting the tariff proposal, BIAL had submitted its proposal, based on its interpretation of provisions of Concession Agreement, on Dual Till basis. It also submitted its proposal on Single Till basis only as per directions of the Authority.

While determining UDF for BIAL, MoCA, though of the view that no cross subsidization from non-aeronautical revenue is provided in the Concession Agreement, finalized UDF on the basis of cross subsidization of 30% from non-aero revenue. UDF decided by MoCA in the year 2008/09 was on ad-hoc basis and continued till the commencement of first control period.

BIAL had submitted a letter dated July 5th 2013 to MoCA, as it had granted the concession, reiterating for dual till, based on its interpretation of the concession agreement.

BIAL had been consistently contesting that Concession Agreement does not envisage cross subsidization. However, in order to reach to a workable solution, BIAL intends to agree with the tariff on hybrid till model and accordingly is in the process of submitting calculations based on Hybrid Till model with 30% cross subsidization. It will not be out of place to mention that even with this model, funds requirement of BIAL for expansion and debt repayment might need a special consideration.

Additionally, BIAL will file its detailed response to Consultation Paper referred above. In the meantime, we request the Authority to kindly consider request of BIAL to consider Hybrid Till model for determination of tariff for Bengaluru International Airport."

Further, as stated in paragraph 1.13 of Consultation Paper No.22, the Authority received a letter dated September 24, 2013 from the Ministry of Civil Aviation in respect of Consultation Paper No.14 which stated as below:

March 2014

“Ministry of Civil Aviation have carefully gone through the proposal contained in the Consultation Paper as well as the building blocks for economic regulation of Bengaluru International Airport contained therein. The Consultation Paper has proposed various charges for Aeronautical Services including User Development Fee (UDF) both under Dual till as well as Single till. The BIAL is undertaking substantial expansion to the terminal building and Second Runway etc. at Bengaluru International Airport. The Consultation Paper indicates that BIAL needs an additional amount of about Rs. 4,027 crore during the control period (2011 - 16) for expansion purpose.

The AERA has proposed a Single till approach wherein the revenue from Aeronautical Services as well as Non-Aeronautical Services as mentioned in the Consultation Paper are considered along with associated costs to determine the Aeronautical charges as well as the UDF. The Ministry of Civil Aviation feels that the requirement of capital for the expansion during the current control period would be difficult to be met under a Single till approach. A Shared Revenue till of 40% would strike an appropriate balance between the needs of expansion of the airport as well as passenger interest, in terms of keeping the user charges at reasonable level. Therefore, 40% of gross revenue generated by BIAL from Non Aeronautical Services may be reckoned towards subsidizing Aeronautical charges and UDF.”

The Authority has, therefore, considered the issue of making available some additional funds in the hands of the airport operator during the current control period for the purposes of carrying out expansion of the Airport. The Authority has therefore put forth for Stakeholders' Consultation, the Aeronautical Charges and UDF computed under the 40% Shared Revenue Till approach.

In **paragraph 22.23.14** of the Consultation Paper No.22, the Authority has noted that the part of the Non-Aeronautical Revenue which would remain in the hands of BIAL under 40% Shared Revenue Till would be used by BIAL for its capital expenditure needs towards the Airport expansion during the current control period. Hence, it has proposed an adjustment to the Aggregate Revenue Requirement (ARR) of the next control period as would have been required had the Authority computed tariffs under Single Till.

Further, the Authority has also noted that the difference between the UDF collected under 40% Shared Revenue Till and the Single Till during the remaining part of the current control period is currently estimated at Rs. 160 Crore. It has stated that this amount represents the transfer of resources from passengers to the Airport Operator on account of the proposed adoption of 40% Shared Revenue Till approach to facilitate expansion of airport facilities by BIAL. Hence, it has proposed a commensurate adjustment to the Regulatory Asset Base (RAB) at the beginning of the next control period.

APAO Response

Principally, APAO continues to maintain its position that the Dual Till approach should be made applicable in case of BIAL. As stated in its submission to the Consultation Paper No.14, this position is based on the following:

- **Concession Agreement:** The Concession Agreement clearly bifurcated the regulated and other charges. Bringing the other charges under the ambit of regulation goes against the letter and spirit of the Concession Agreement which does not envisage cross subsidy from non-aeronautical revenues to defray aeronautical charges. Hence, it could be inferred that the concession agreement envisaged adoption of Dual Till.

- **AERA Act:** The proviso to Section 13(1)(a) of the Act states that “different tariff structures may be determined for different airports having regard to all or any of the considerations specified at sub-clauses (i) to(vii)”. In other words, the Act recognizes the flexibility given to AERA to determine tariff structures for different airports having regard to various considerations including the concession granted by the Central Government.

So even though the AERA Act empowers AERA to regulate tariff for Aeronautical Services as defined in Section 2(a) of the AERA Act, in case any concession has already been granted by the Central Government, AERA is required to consider the terms of such concession. This is an exception to the mandate of the Act which is recognized and allowed by the Act itself

- **Global precedents-** in respect of Airports adopting the Dual Till approach

The Hybrid Till approach suggested by the Authority is not conventional, without precedent especially at greenfield airports and in emerging markets. It is crucial that the any regulatory till sought to be applied at BIAL (and potentially at other airports in the future) provides an assurance to current – and prospective - investors that returns on their investment are commensurate with the risks they have borne. This is especially the case with respect to Greenfield projects where the risks are higher and investments take longer to break even. The absence of adequate returns risks disincentivizing investment across India as investors pursue more remunerative opportunities both in India and more widely. The importance of this dimension is underlined by the potential for (and lack of success so far in attracting) FDI to Indian airports subsequent to the first round of investment in Indian airports between 2004 and 2006. The Regulator’s judgment needs to take full account of this need to attract investment into the sector.

- It is APAO’s understanding that the Authority would be making the Shared Revenue Till approach applicable to BIAL only to enable BIAL to overcome its funding paucity for capital investment in the forthcoming consultation period. However, APAO would like to bring to the Authority’s notice the fundamental issue that capital investment at BIAL is highly likely to be an ongoing and constant process for multiple consultation periods in the future given the forecast traffic demand levels and projected infusion of capacity (through capital investment) in order to maintain acceptable passenger levels-of-service. It is therefore unclear to APAO whether this approach is likely to be followed for each period in the future and if so whether the RAB will be constantly adjusted. If this is the case, it is not a sustainable approach for the airport operator given CapEx and OpEx forecasts and operational constraints. In addition, BIAL will need to have flexibility to use revenue accrued as the airport best sees fit.
- The application of Shared Revenue Till approach during its period of application should be unconditional. Imposing conditions would end up disincentivizing BIAL and also adversely impact its ability to generate adequate returns to make the airport project financially viable. BIAL will be experiencing severe shortage of funds, even under proposed Shared Revenue Till by Authority, and hence needs to be given complete flexibility in deciding whether the funds generated through application of the Shared Revenue Till approach should be used for operations, repayment of debts or undertaking expansion.
- The adjustments proposed by AERA to the Aggregate Revenue Requirement (ARR) and the Regulatory Asset Base (RAB) would effectively neutralize the benefits that would accrue to the

operator from the adoption of the Shared Revenue till approach. Further, the adjustment to RAB would effectively mean that a permanent reduction in RAB would be made even before the assets were capitalized and put to use. As outlined earlier, this is of particular concern given the likely capital investment profile at the airport over the next few consultation periods in order to meet demand levels. In addition, financing of such projects will be difficult with the approach proposed by the Authority.

- APAO would also like to bring to the Authority's notice the fact that the losses made by BIAL in the initial control period have not been taken into account in the calculations of return on investment and this needs to be factored into any calculation of returns at the Airport.

2.2. Regulatory Asset Base (RAB) and Treatment of Land / Real Estate

As regards the land leased by the Government of Karnataka (GoK) which was used by BIAL for commercial exploitation, the Authority had noted in Consultation Paper No.14 that it may not be correct for BIAL to benefit from the land being given mainly for the purpose of running an airport by exploiting it for commercial purposes. The Authority had thus sought to pass on to the users, the benefit of exploitation of the land so given, by reducing the Regulatory Asset Base.

In **paragraph 6.23** of Consultation Paper No.22, the Authority has stated as follows:

"Land transactions can be quite complex and the Capital and Revenue receipts generated from such transactions also depend on a variety of factors including its usage, tenure of lease, taxation etc....The Authority is cognizant of the fact that land has been acquired by the GoK for the public purpose of establishment of the Airport Project. Hence the Authority feels that GoK would be in appropriate position to ascertain the reasonableness or otherwise of the receipts accruing to BIAL on account of exploitation of land in excess of the requirements of the Airport Project. The Authority would take into account the manner of considering the receipts (both Capital and Revenue) to be reckoned towards determination of Aeronautical Tariffs based on appropriate response to be received from GoK and would take the same into account for the purposes of truing up the tariff computations for the current control period while determining Aeronautical tariffs in the next control period."

APAO Response:

As per Clause 4.1 of the Land Lease Deed, *"KSIIDC hereby grants permission and consent, to BIAL to use the Site, and BIAL agrees to use the Site in accordance with the Master plan, for carrying out of the Activities and the following..."*. 'Activities' is a defined term and includes both airport and non-airport activities as outlined in Schedule B to the land lease deed. Thus, per clause 4.1, BIAL is entitled and permitted to undertake all airport and non-airport activities as defined and described in the land lease deed.

As per Clause 4.2 of the Land Lease Deed, *"BIAL may, with the approval of KSIIDC (such approval not to be unreasonably withheld), in addition to the above Purposes, utilize the Site for any other purposes, which in its opinion is (i) conducive or incidental to implementation of the Project; and/or (ii) conducive or incidental to the operation and management of the Airport; and/or (iii) enhances the passenger/cargo*

traffic at the Airport; and/or (iv) improves the commercial viability of the Project; and/or (v) facilitates substantive further investment in or around the Airport."

As per Clause 4.2 (iii) of the State Support Agreement, BIAL shall *"promote the development of the Non-Airport Activities with the objective of progressively generating a higher share of revenues for BIAL from such activities"*

Further, Clause 10.2 of the State Support Agreement states that *"...GoK recognizes that BIAL may carry out any activity or business in connection with or related to the development of the Site or operation of the Airport to generate revenues including the development of commercial ventures such as hotels, restaurants, conference venues, meeting facilities, business centres, trade fairs, real estate, theme parks, amusement arcades, golf courses and other sports and/or entertainment facilities, banks and exchanges and shopping malls"*

Thus, it can be seen that the Land Lease Deed as well the State Support Agreement explicitly allow commercial exploitation of land.

The GoK has, in a letter written to the Authority dated August 26, 2013, stated as follows:

"...The guiding principles for utilisation of land are contained in Land Lease Deed (LLD), Concession Agreement (CA) and State Support Agreement (SSA). The relevant clauses are reproduced in the Annexure enclosed. ..."

Although the GoK has upheld the sanctity of the Land Lease Deed, Concession Agreement and the State Support Agreement, APAO is unable to fathom the Authority's proposal to seek GoK's opinion in respect of the reasonableness or otherwise of the receipts accruing to BIAL on account of exploitation of land in excess of the requirements of the Airport Project when it has been explicitly stated in the SSA and LLD. In APAO's view, since the guiding principles for utilization of land are already given in the SSA and LLD, there should be no ambiguity regarding the reasonableness of receipts or their treatment as capital or revenue. The details of aeronautical and non-aeronautical revenue submitted by BIAL to the Authority are in consonance with the usage of land in accordance with both the SSA and LLD. APAO is therefore categorically of the view that the details submitted by BIAL should be considered by the Authority in determination of aeronautical tariffs and that an opinion from GoK in this regard would be unnecessary.

As stated in our submission related to Consultation Paper No.14, it is APAO's view that assigning a value to the land and subtracting the same from the RAB is not consistent with the Concession Agreement. Such adjustment is also a disincentive for land monetization as it negatively impacts the internal accruals which would have been otherwise available for expansion. Such adjustment is in principle inconsistent with various clauses of the LLD and of the SSA on which the airport's development was based and investment attracted (representing a substantial retrospective adjustment to those terms) and is in practice inconsistent with regulatory best practice.

2.3. Cost of Equity Calculation

In Consultation Paper No.14, the Authority had proposed a 16%Return on Equity (post tax Cost of Equity) for the Weighted Average Cost of Capital (WACC) calculation both under Single Till and Dual Till based on the report issued by NIPFP.

Similarly, in Consultation Paper No.22, the Authority has proposed a 16% Return on Equity (post tax Cost of Equity) for the Weighted Average Cost of Capital (WACC) calculation both under Single Till and Shared Revenue Till.

APAO Response:

APAO submits that the Return on Equity especially for greenfield airports be considered at 24.4% as outlined earlier. It also wishes to reiterate the following points made in its submission in response to Consultation Paper No.14:

- **Nominal risk-free rate:** The NIPFP approach rests on the historic performance of the overall nominal rate as represented by the return on Government debt. However, such unadjusted historic debt rates will be most relevant to measuring future risk free rates when future conditions are anticipated to be very similar to those in the past. This is unlikely to be the case given the significant fluctuations in rates of inflation in India during the past decade. This effectively means that the returns which an operator would make would be substantially/totally wiped out on account of inflation. In effect, the real risk free rate would be negative. Against this background, the Authority might be better advised to use historic data to determine the underlying real interest rate, but to pay more attention to more recent inflation performance in determining the inflation rate to be incorporated into the nominal figure. To do otherwise risks setting a risk free rate below (and in this case, potentially significantly so) that which should be obtained going forward.
- **Comparator sets:** In APAO's view, instead of considering a simple average of an arbitrary list of airports and other utilities, appropriate weightage should have been assigned to each of the comparators based on the degree of their comparability. It may be worthwhile to note that NIPFP itself has commented on the difficulty in determining the comparator set as stated below:

"Since the private airport business in general, and these new mega-airports (like DIAL) in particular are relatively new, and AERA has a unique regulatory approach.....it is not possible to say at this stage which subset of airport companies would be the best comparators....As we come to understand more, it could be reasonable to take a bottom-up approach to constructing the beta, or take a smaller sample of comparable airport companies. In our view, at this stage, neither of these approaches is feasible".

(Source: Page 15 of the 'Cost of Equity for Private Airports in India-Comments on DIAL's response to AERA Consultation Paper No.32, and the report by SBI Caps' issued by the NIPFP Research Team on April 19, 2012)

The NIPFP has acknowledged in a way that the comparator set used may not be the best or adequate for determination of beta. However, it has not explored any alternative comparator set (such as the one proposed by BIAL) and instead sought to hastily conclude that taking a bottom-up approach or using a different sample of comparator companies is not feasible. Additionally, the conclusions drawn by the NIPFP are arbitrary at best as outlined in their comment on betas below.

- **Betas:** On the subject of beta, the NIPFP's rather weak conclusion is reproduced below:

"We accept the argument that it is possible that typically the macro-economic shocks would be likely to be strongly transmitted to the airport sector in a period of high traffic growth, but it is not clear to what extent this can be expected to happen in India's airports, given the mitigants in place and the

revenue sources. It is **possible** that the beta estimates we have arrived should be sufficient to cover for such risks”

(Source: Page 17 of the 'Cost of Equity for Private Airports in India-Comments on DIAL's response to AERA Consultation Paper No.32, and the report by SBI Caps' issued by the NIPFP Research Team on April 19, 2012)

In APAO's view, this is an insufficiently firm conclusion on which to base a regulatory judgment on cost of equity. The choice of the beta should give more than a 'possibility' that risks were covered. A regulator needs to be assured that on the balance of evidence the beta is, in an inevitably uncertain world, the right number. NIPFP's conclusion does not give that assurance. Also, the upper bound of the beta considered by the Authority for Kolkata and Chennai Airports in the Orders for tariff determination for the first control period 2011-2016 for these airports is 0.61. Both the Kolkata and the Chennai airports are owned and operated by the Government. The risk element attributable to these airports is likely to be significantly lower compared to privately operated airports. Therefore, it is inconceivable that the asset beta for both airports is higher than that proposed by the Authority for BIA (0.51) where the risk borne by the private sector operator is significantly higher especially in the case of greenfield projects such as BIA.

- **Mitigants:** The Authority seems to have sought to overplay the role of the mitigants such as the User Development Fee (UDF) to cover shortfall in revenues, granting monopoly for a certain area etc.

APAO's view is that the UDF was granted cover the shortfall of revenues during the process of tariff determination. Given the quantum of investment, this was the very least investors would expect.

The grant of monopoly to an airport seeks to insulate it against competition by not allowing an airport to be set up within a specified radius (e.g.150 kms) for a specified period (e.g.25 years) from the date of the opening of the airport. This is thought to reduce the beta relative to comparators which do not have this grant. However, a casual inspection of the list of airports provided by NIPFP suggests that most have de- facto as much of a 'monopoly' as BIA. In such circumstances, the grant of a monopoly is not a distinguishing factor reducing the risk of the airport relative to realistic comparators. The mention in the NIPFP report of the London market is inaccurate because, while the three airports are now in separate ownership, the betas referred to in the reports were based on a period when BAA indeed held a monopoly on possibly the largest urban agglomeration of flying passengers in the world (over 100 mppa).

- **Cost of Equity estimates:** The Cost of Equity estimates computed by various leading consulting firms are given below:

Sr No	Name of Consultant	Cost of Equity
1	Crisil Infrastructure Advisory	18.16-20.44%
2	KPMG India Private Limited*	20-25%
3	SBI Capital Markets Limited	18.5%-20.5%
4	Jacobs Consultancy (now LeighFisher)	24%

*Assignment commissioned by APAO

Further, KPMG India Private Limited was also appointed by BIAL to estimate the fair rate of return and it has estimated the cost of equity for the first control period to be in the range of 23.5%-27.9%.

As can be seen, the Cost of Equity estimates determined by NIPFP (12.02%) and the Authority (16%) are much lower than those arrived by the various consulting firms.

APAO therefore reiterates that Cost of Equity of 24.4% be considered for BIAL.

2.4. Others

2.4.1. Quality of Service rebate

APAO is grateful to the Authority for doing away with the rebate in tariff mechanism proposed in Consultation Paper No.14 and upholding the need to conform to the performance standards stated in the Concession Agreement

2.4.2. Fuel Throughput Fee

The Authority proposes to consider the Throughput Fee revenue from fuel farm service concession out by BIAL to IOSL as aeronautical revenue in the hands of BIAL.

APAO response:

Any revenues received by an airport in consideration for the various commercial arrangements it makes in relation to the granting of concessions, the rental or leasing of premises and land, and free-zone operations, would be classified as revenues from non-aeronautical sources even though such arrangements may in fact apply to activities that may themselves be considered to be of an aeronautical character. This principle is also underscored in **Paragraph 4.18** of the third edition of the **Airport Economics Manual (Doc 9562)** issued by the **International Civil Aviation Organization** in 2013 which states that all concession fees **including any throughput charges, payable by oil companies or any other entities for the right to sell or distribute aviation fuel and lubricants at the airport shall be classified as revenues from non-aeronautical activities**. APAO therefore submits that the Throughput Fee revenue should be considered as non-aeronautical revenue in the hands of BIAL.

2.4.3. Cargo and Ground handling Services

The Authority proposes to consider the amounts received by BIAL from Cargo and Ground Handling services as part of aeronautical revenues.

APAO Response:

As per Article 10 of the Concession Agreement read with Schedule-6 of that Agreement, the Regulated Charges are Landing charges, Housing charges, Parking charges, Passenger Service Fee (PSF) and User Development Fee (UDF). Further, as per Article 10.3 of the Concession Agreement, BIAL is free, without restriction, to determine the charges to be imposed in respect of the facilities and services provided at the Airport or on the site, other than the facilities and services in respect of which Regulated Charges are levied. Therefore, BIAL considered the revenue from services other than Regulated Services as non-aeronautical revenue. The initial business plan and financial model submitted to the Government of Karnataka by BIAL was also prepared on this basis.



March 2014

The Authority had, in Consultation Paper No.14, considered the amounts received by BIAL from Cargo and Ground Handling services as non-aeronautical revenues based on the fact that BIAL had concessioned out these services to independent third party service providers. This position was also in consonance with the Concession Agreement. We accordingly request the Authority to maintain this position and consider the amounts received by BIAL from Cargo and Ground Handling services as non-aeronautical revenue.

3. CONCLUSIONS

▪ **Regulatory Till:**

- Principally, APAO continues to maintain its position that the Dual Till approach should be made applicable in case of BIAL.
- However, APAO supports BIAL's proposal of a 30% Hybrid (or Shared Revenue) Till as a workable solution to overcome the deficit in funding required for expansion and smooth operations of the Airport given the likely capital investment profile over the next few consultation periods
- The extent of cross subsidization should be considered at 30% as proposed by BIAL instead of 40% as recommended by MoCA and the Authority for the period of the Shared Revenue Till approach
- The application of Shared Revenue Till approach should be unconditional. Imposing conditions would end up disincentivizing the operator and also adversely impact BIAL's ability to generate adequate returns to make the airport project financially viable. The Authority also needs to make clear how future capital expenditure is proposed to be funded given the uncertainty in the regulatory approach as banks and financial institutions are unlikely to accept the approach
- The adjustments proposed by the Authority to the Aggregate Revenue Requirement (ARR) and the Regulatory Asset Base (RAB) would effectively neutralize the benefits that would accrue to the operator from the adoption of the Shared Revenue Till approach. Further, the adjustment to RAB would effectively mean that a permanent reduction in RAB would be made even before the assets were put to use. In addition, the losses made by the Airport in the initial control period also need to be factored into any calculation on returns in the case of BIA.

- **Regulatory Asset Base (RAB) and treatment of land/real estate:** In APAO's view and as clarified by GoK, the guiding principles for utilization of land are already given in the SSA and LLD. Hence, APAO submits that the opinion from GoK in this regard would not be necessary for the purposes of truing up the tariff computations.

As stated above, it is APAO's view that assigning a value to the land and subtracting the same from the RAB is not consistent with the Concession Agreement. Such adjustment is also a disincentive for land monetization as it negatively impacts the internal accruals which would have been otherwise available for expansion. Such adjustment is in principle inconsistent with various clauses of the LLD and of the SSA on which the airport's development was based and investment attracted (representing a substantial retrospective adjustment to those terms) and is in practice inconsistent with regulatory best practice.

- **Cost of Equity calculation:** APAO submits that the Return on Equity be considered at 24.4% as proposed by BIAL. It reiterates its position on nominal risk-free rate, comparator sets, betas, mitigants and the cost of equity estimates of BIAL determined by several professional consulting firms and equally questions the strengths and conclusions of the NIPFP Report and its weak conclusions.

March 2014

- **Quality of Service rebate:** APAO is grateful to the Authority for doing away with the proposed rebate in tariff mechanism and upholding the need to conform to the performance standards stated in the Concession Agreement.

- **Fuel Throughput Fee**

Paragraph 4.18 of the third edition of the **Airport Economics Manual (Doc 9562)** issued by the **International Civil Aviation Organization** in 2013 states that all concession fees **including any throughput charges, payable by oil companies or any other entities for the right to sell or distribute aviation fuel and lubricants at the airport shall be classified as revenues from non-aeronautical activities**. APAO therefore submits that the Throughput Fee revenue should be considered as non-aeronautical revenue in the hands of BIAL.

- **Cargo and Ground Handling services**

The Cargo and Ground Handling revenues do not fall under 'Regulated Charges' stipulated in Schedule-6 of the Concession Agreement. Hence, they should be considered as non-aeronautical revenue. The initial business plan and financial model submitted to the Government of Karnataka by BIAL was also prepared on this basis. The Authority had, in Consultation Paper No.14, considered the amounts received by BIAL from Cargo and Ground Handling services as non-aeronautical revenues based on the fact that BIAL had concessioned out these services to independent third party service providers. This position was also in consonance with the Concession Agreement. We accordingly request the Authority to maintain this position and consider the amounts received by BIAL from Cargo and Ground Handling services as non-aeronautical revenue.
