



INDEPENDENT CONSUMER & COMPETITION COMMISSION

Issues Paper
PNG Air Transport Industry

20 March 2006



Submissions

The Government as part of its 2006 Budget Strategy has directed the Independent Consumer & Competition Commission (“Commission”) to undertake a comprehensive review of the Airlines industry in Papua New Guinea (“PNG”) with a view to identifying regulatory impediments and competition constraints.

In accordance with the official referral by the Minister for Finance & Treasury under section 123 of the *Independent Consumer & Competition Commission Act 2002* (ICCC ACT) of the Review, the Commission must meet the deadlines in terms of its preparation and release of the Issues Paper, Draft Report and Final Reports and subsequent presentation to the Government including making available copies of the relevant documents at those stages of the Review. Hence, the timetable for the current Review is as follows:

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|---|----------------|
| • Receipt of Submissions on the Issues by | 21 April 2006 |
| • Release of Draft Report | 5 June 2006 |
| • Receipt of submission on Draft Report | 14 July 2006 |
| • Release of Final Report | 18 August 2006 |

Consistent with the requirements of Section 124 (2) of the ICCC Act, public and industry stakeholders’ involvement would form an important element in the entire process. Hence, this Issues Paper is intended to provide a brief overview of the issues that will be considered as part of the Review and to invite submissions from stakeholders and interested parties.

Submissions to the Commission will be available for public inspection unless the Commission agrees that all or part of the submission should remain confidential. However, in accordance with the provisions Section 124 of the ICCC Act, it is intended to make the Review a process as transparent as possible, and to this end, submissions would normally be available for public inspection unless there are exceptional commercial-in-confidence reasons why submissions should be held confidential.

Submissions to this Issues Paper should be received by 21 April 2006, and should be directed to:

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Executive Summary

The Government, as part of its 2006 Budget Strategy, announced that it will be examining a number of industries with a view to considering competition issues and the role and place of regulation. As part of this strategy the Independent Consumer and Competition Commission (the Commission) has been instructed by the PNG Government to review the Air Transport industry. This review is expected to go hand in hand with another review currently being undertaken, namely the Coastal Shipping review.

In terms of the air transport sector, the Government has foreshadowed a review of the impediments to competition around air transport with a view to increasing competition and reducing air transport costs. Included as part of this review are both passenger and freight air transport sector and the operation of air transport on international routes into and out of PNG as well as internal domestic routes. The industry for purposes of this Review will also include the provision of air and passenger side services and flight servicing arrangements.

This Review is intended to look at a wide range of issues relating to the regulation of the industry with a particular focus upon ways of increasing competition and reducing air transport charges and user costs. This recognises the significance of air transport to the efficient operation of the domestic economy and the reliance on air links between PNG and the wider world to strengthen and build the national economy through international trade and commerce.

The air transport sector has been identified as an important component of the overall transportation system in PNG in the movement of both passengers and freight within the domestic jurisdiction and abroad. In the current domestic context, air transport plays a crucial and important role due to the following:

- The absence of effective national road link or rail system;
- The demographics and topography of PNG; and
- The reliance of PNG on international trade links outside of the country and links to remote export mining and agricultural activities within the country.

In addition, there are a number of charter operators which provide services to PNG's key industry, mining, and a small percentage of cargo which is brought into and out of PNG's geographically diverse population and resource base. However, the industry faces significant issues, most notably increased costs associated with high fuel costs and increased security costs have resulted in unique challenges to the industry.

The cost and efficiency of the air transport sector has important economic consequences which affect, inter alia, the profitability and viability of export industries, including tourism industry, local transportation of passengers, goods and commodities within PNG.

At the conclusion of this review, the Commission will make recommendations on what action may be appropriate to be taken by the Government to rectify any problems in the current regulation and operation of the air transport sector with a view to improving competitiveness and reducing air transport costs.

As part of this review the Commission is seeking stakeholder comments on a number of issues, including:

The Commission seeks comments from the public and any interested parties on the scope of services included below:

Freight and passenger services;

Charter services;

Flight schools and training;

Air navigational flight control services;

Airport facilities and amenities;

Airport services including aircraft parking and refuelling services;

Retail services at airports; and

Safety licensing regulation.

The Commission seeks comments from the public and any interested parties on any matters relating to the legislative environment and the operation of the air transport sector and whether it provides an appropriate legal framework for the efficient operation of the industry.

The Commission seeks comments from the public and any interested parties in respect of the industry administrative functions performed by the Department of Transport and the Civil Aviation Authority.

Further, the Commission is interested in seeking comments in relation to the effectiveness of the functions performed and whether any of these functions may be deemed as an impediment to the effective operation of the industry.

The Commission seeks comments from the public and any interested parties on any matters relating to the ownership, operation, maintenance and management of airports and related facilities both major and minor airports throughout the country.

The Commission also seeks comments on the effectiveness of the current ownership arrangements and whether it contributes to any inefficiencies in the industry.

The Commission also seeks comments from the public and any interested parties on matters relating to the current state of PNG's airport infrastructure.

The Commission seeks comments from stakeholders regarding the effectiveness of the safety and security aspects of the industry. In particular, the Commission is seeking to understand what impacts, if any, these matters have on the efficiency of the industry.

The Commission seeks comments from interested stakeholders regarding the structure of the air services pricing.

The Commission seeks comments from stakeholders on the validity of travel agents using a default service provider. Does the position of a default service provider result in an unfair competitive position over other service providers?

The Commission seeks comments from stakeholders as to whether or not the existing airport infrastructure should be rationalised to support a higher concentration of services which are in turn more profitable to operate.

The Commission is seeking stakeholders' views as to whether or not the current ownership structure of airports is limiting competition in the provision of Airport infrastructure.

The Commission seeks submissions from stakeholders on the availability and allocation of existing airport terminal space.

The Commission invites comments and submissions from the public, stakeholders and any interested parties on the level of air services, particularly freight and passenger services, and whether there is adequate services to cater for the needs of all air sector users.

The Commission seeks comments from stakeholders on the current access arrangement for new entrants into the PNG international segment of the airline market.

The Commission seeks comments from stakeholders as to the adequacy of training facilities within PNG. In particular, the Commission is seeking to understand whether or not the current training regime is sufficient to provide pilots and crew capable of piloting and servicing aircraft to an appropriate standard.

The Commission is also interested in understanding how pilots and crew are accredited to perform these functions.

The Commission seeks comments from stakeholders on the issue of recognition of qualifications received in other jurisdictions.

The Commission seeks comments as to whether these requirements represent a barrier to new entrants entering the market.

The Commission seeks comments from stakeholders as to whether any participant in the market is able to exercise its market position to minimise competitive pressure from other service providers.

The Commission seeks comments from stakeholders as to the level of cross subsidisation in the industry from any route to another route. The Commission is seeking to understanding the rationale for this cross subsidisation.

The Commission seeks views from stakeholders on the likely developments or changes in the existing structure of the air transport industry including entry of new service providers, over the next decade.

1. INTRODUCTION

The Independent Consumer & Competition Commission (Commission) is a statutory body, established under the provisions of the *Independent Consumer and Competition Commission Act 2002* (the ICCA Act), which has been given responsibility for the promotion of competition & fair trading, the regulation of prices for certain goods and services, and the protection of consumers' interests and other related purposes.

In terms of the air transport sector, the Government has foreshadowed a review of the air transport industry with a view to increasing competition and reducing air transport costs. Included as part of this review are both passenger and freight air transport issues and the operation of air transport on international routes into and out of PNG as well as internal domestic routes. The industry for purposes of this review will also include the provision of air and passenger side services and flight servicing arrangements.

The provisions of Part VIII of the ICCA Act empowers the Commission to conduct specific enquiries necessary and desirable for the purposes of the Commission in carrying out its functions or as directed by the Minister responsible for Treasury matters or by Parliament. On the 26 January 2006, the Minister for Finance & Treasury (Treasurer) formally referred the Commission to undertake a comprehensive review (Review) into the Air Transport industry in Papua New Guinea. The main purpose of the Review is to consider competition issues and the role and place of regulation within that industry. This referral is part of the Government's 2006 Budget Strategy.

The Review is intended to look at a wide range of issues relating to the operation of the industry including its regulations with a particular focus upon ways of increasing competition and reducing air transport charges and user costs. This recognises the significance of air transport to the efficient operation of the domestic economy and the reliance on air links between PNG and the wider world to strengthen and build the national economy through international trade and commerce.

In PNG there are approximately 30 registered air service operators with the 3 major players being:

- Air Niugini Limited (ANL) which dominates with about 80 to 85% of the air transport market;
- Airlines PNG (APNG); and
- Airlink;

In addition, there are a large number of other smaller operators including aviation based operators and specialists which provide service across the industry.

Carrier licences are issued by the Department of Transport while air operators certificates are issued by the Civil Aviation Authority (CAA) which is the main regulatory authority for the air transport industry. The CAA awards about 20 licences/permits including appropriate certificates on an annual basis. The smaller airline operators operate mainly charter services to the mining townships or the smaller communities located in remote location across the country. In addition, they run some aerial and flight training services.

1.1 Objectives of the Review

The principle objectives and deliverables of the Review are to:

- Report on the current impediments, both regulatory and non-regulatory, to improved operating efficiency and competitiveness in the air transport industry in PNG; and
- Identify issues and areas where Government action may be appropriate to improve the overall cost competitiveness and efficiency of the air transport industry in PNG.

At the conclusion of this review, the Commission will make recommendations on what action may be appropriate to be taken by Government to rectify any problems in the current regulation and operation of the air transport sector with a view to improving competitiveness and reducing air transport costs.

1.2 Why is the Commission conducting this Review

As noted the Government has recognised the air transport sector as an important component of the overall transportation system in PNG in the movement of both passengers and freight within the country and internationally. In the current domestic context, air transport plays a crucial and important role due to the following:

- The absence of effective national road links or rail systems;
- The demographics and topography of PNG; and
- The reliance of PNG on international trade links outside of the country and links to remote export mining and agricultural activities within the country.

There are a number of charter operators which provide services to PNG's key industry, mining. In addition, a small percentage of cargo which is brought into and out of PNG's geographically diverse population and resource base via charter flights. However, the industry faces significant issues, most notably

increased costs associated with high fuel costs and increased security costs have resulted in unique challenges to the industry.

1.3 What services are covered?

The Commission's terms of reference is relatively wide and could be interpreted to cover the entire value chain of the air transport industry. This would include at an absolute minimum, services supplied by the industry which is predominantly, passenger and freight/cargo services as well as other services such as passenger side services and flight servicing arrangements including the licensing and other regulatory services provided by the CAA. The Commission has identified the following key services to be included in the Review:

- Freight and passenger services;
- Charter services;
- Aerial chartering services;
- Flight schools and training;
- Air navigational flight control services
- Airport facilities and amenities;
- Airport services including aircraft parking, and refuelling services
- Retail services at airports; and
- Safety licensing regulation.

The Commission seeks comments from the public and any interested parties on the scope of services to be included in the review.

1.4 Conduct of this Review

The Commission will undertake a detailed consultation process to ensure that all stakeholder comments are received and considered. This will be supported by the Commission's own analysis and research. This consultation will include all major stakeholders including ANL, APNG, other smaller air operators, the Department of Treasury, the CAA, other interested parties and the general public. Should circumstances allow, the Commission will hold at least two public hearings, one in Port Moresby and one possibly in Lae, as part of the Review to provide an opportunity for stakeholders to present their views on any issues associated with this Review.

The Commission will consider all matters raised in response to this Issues Paper and following further consultation with stakeholders will release a Draft Report which will again provide the opportunity for further consultation. The Commission will consider all comments before releasing its Final Report in response to the Government's terms of reference. Table 1.1 sets out the Commission's expected timetable for this Review. Importantly, the Commission is required to provide the Government a response to this review by 18 August

2006. All consultation will need to be completed in time for the Commission to have the opportunity to provide appropriate consideration of all issues raised in advance of this date.

The timetable for the current Review is as follows:

Table 1.1: Timetable for the Review

Deliverables	Deadline
Release of Issues Paper	20 March 2006
Submissions due on Issues Paper	21 April 2006
Release of Draft Report	5 June 2006
Submissions due on Draft Report	14 July 2006
Formal release of Final report	18 August 2006

1.5 Structure of this report

This issues paper is designed to solicit responses from the various industry players in the market including users of aviation services. It provides background and context to the industry and will ask a series of questions designed to stimulate concerns of stakeholders including the public. These questions should not be seen as the Commission's likely conclusions to this Review. Further, they should not be seen as dictating the scope of the Review. Hence, the Commission welcomes submissions on other matters stakeholders believe should be addressed.

The paper is structured as follows:

- Chapter 2 provides a background to the industry;
- Chapter 3 provides an overview to the market and current state of the industry; and
- Chapter 4 discusses the issues facing the industry.

2. BACKGROUND AND INDUSTRY OVERVIEW

2.1 Country Overview

PNG is located on the eastern half of the island of New Guinea located to the north of Australia. PNG comprises both the mainland and some 600 offshore islands. According to the 2000 National Census, PNG's population was about 5.2 million¹ of which around 15 percent of the population live in the ten major urban areas. The major city and capital of the country is Port Moresby with a population of just over 220,000. Other main towns and cities include Lae, (population around 90,000), Madang (30,000), Mt Hagen (40,000), Wewak (23,000) and Goroka (25,000). Other main centres include Rabaul/Kokopo, Alotau and Kimbe. Arawa, the once thriving urban centre and provincial capital of Bougainville and neighbouring townships of Kieta and Panguna have been deserted due to the Bougainville conflict. The township of Buka is now the new centre for government and commerce of that island province.

PNG has a dualistic economy with a traditional quasi subsistence rural sector which provides the livelihood for about 85 percent of the population while the balance is employed in the formal monetary sector. The formal sector provides a rather narrow employment base, consisting of workers engaged in mineral production, a relatively small manufacturing sector, public sector employees and service industries including finance, construction, transportation and utilities.

After several years of economic contraction, the PNG economy grew by 2.8 percent in 2003, and 2.6 percent in 2004². Other macroeconomic indicators have also improved with both inflation rates and interest rates declining. Despite this more positive outlook, the PNG economy continues to be highly dependent on price fluctuations in the external sector, through export earnings. Economic prospects from year to year are mainly determined by international commodity prices, particularly those of gold, oil, copper, logs, coffee, copra and cocoa (exports), and petroleum products. Oil, agricultural and mineral exports are equivalent to 42 percent of PNG's GDP, and account for 90 percent of its exports.

The geography of PNG consists of volcanic mountains and low coral atolls. There are 20 provinces of which 15 are located on the coast. As a result of the difficult geography, air transport plays a predominant role in terms of passenger transportation and to certain extent cargo and freight movement including the delivery of labour and inputs for the mining and minerals sector.

¹ NSO Final Figures for 2000 Census

² Treasury budget papers- 2004

2.2 Industry overview

The airline industry plays a crucial role in the transportation of freight and passengers within PNG and internationally. In general, existing air services can be categorized as follows:

- International travel;
- Domestic travel between the main airports; and
- Third-tier airlines serving minor airports and charters to remote locations and mining townships including charter, aerial services and flying schools.

Airlines operate different types of aircrafts both jets and turboprops including helicopters and other smaller aircrafts. There are more than 30 licensed air service operators in the aviation market. Amongst them, ANL and APNG are the only airlines currently licensed to operate both international and domestic services. There are also 8 other licensed third level operators as well as 26 other operators issued with charter and aerial services licenses. These operators operate through 22 major domestic destinations plus other provincial and remote destinations.

International services operated by ANL and APNG provide regular passenger and freight services to and from South East Asia, including Singapore, Hong Kong, Japan, Cairns, Brisbane and Sydney. APNG operates a scheduled passenger services between Port Moresby and Cairns but also provides direct charters from Cairns to major mining townships in PNG. Jacksons International handles all the international flight. Other major airports include Kagamuga, Nadzap, Tokua and Gurney, all of which have the potential to handle some international flights. The other main airports in PNG include Goroka, Madang Hoskins, and Kimbe.

2.3 Legislative environment

The three major pieces of legislation that provide the legal framework that governs the operations and management of the aviation industry in PNG are:

- *National Airlines Commission Act 1973* (Consolidated to No 1 of 1996) (NAC Act);
- *Civil Aviation Act 2000* (CAA Act); and
- *Aerodrome (Business Concessions) Act 2000* (ABC Act)

The NAC Act establishes the National Airlines Commission (NAC) to operate a national flag carrier, whilst the CAA Act establishes the CAA to provide all aviation support services and safety regulation for the airline industry. The ABC Act provides for the granting of leases and licences for business purposes on aerodromes.

Other legislation that also affects the industry includes:

- *Companies Act 1997;*
- *Investment Promotion Act 1992; and*
- *Public Finances Management Act 1995*

An overview of these legislations and their implications on the air transport industry are detailed in Appendix B of this paper.

The Commission seeks comments from the public and any interested parties on any matters relating to the legislative environment and the operation of the air transport sector and whether it provides an appropriate legal framework for the efficient operation of the industry.

2.4 Airlines regulation

Prior to the inception of the Civil Aviation Authority (CAA) in 2001, the then Department of Civil Aviation (DCA) had full responsibility for the administration of the aviation industry and other related aviation matters. However, following recent industry reform in 2000, the CAA was established. The CAA now assumes full responsibility of the technical and safety aspects for the industry. CAA's major objectives and corporate goals are to be:

- Profitable and efficient in its commercial activities and to ensure that aviation safety is not compromised;
- An employer of choice, with a personnel policy which is generally deemed and accepted to be fair and proper including the treatment of employees in all aspects of their employment, included but not limited to:
 - good and safe working conditions;
 - an equal opportunities employment programme;
 - the impartial selection of suitably qualified persons for appointment; and
 - opportunities for the enhancement of the abilities of individual employees; and
- An organization that exhibits a sense of social responsibility by having regard to the interests of the community in which it operates and by endeavouring to accommodate or encourage these, where necessary.

Since the passing of the CAA Act in 2000 and the subsequent establishment of CAA, safety regulatory functions including airport management functions are now performed by the CAA. The CAA's main responsibilities as conferred by the CAA Act are to:

- Undertake activities that promote safety in civil aviation at a reasonable cost;

- Ensure the provision of air traffic services, aeronautical communications services and aeronautical navigation services;
- Ensure the provision of meteorological services and science; and
- Own, operate, manage and maintain airports.

Under the same Act, CAA's major functions are to:

- Initiate and formulate policy proposals on Air Transport;
- Administer legislation pertaining to Civil Aviation;
- Provide Civil Aviation Services, including maintenance of Government Flying Unit Aircraft;
- Maintain and control Civil Aviation navigational aids;
- Operate for the Civil Aviation Training College;
- Maintain and control Civil Airport Fire Services;
- Provide services to Air Accidents Investigation Branch
- Stand as an ad hoc organization relating to the functions of the Department, responsible for the design and maintenance of aerodromes; and
- Provide meteorological services to the air transport industry.

The CAA is also responsible for the regulation of penalties for breaches of established safety requirements, certification rules and other airworthiness requirements including other necessary imposts where appropriate for the purposes of fulfilling its legislative objectives.

The Department of Transport – Air Services Division (DoTAS) is the main policy agency responsible for the aviation industry. The DoTAS issues carrier licences to air service operators. These licences are regulated by the CAA and all operators must comply with and satisfy CAA's operational requirements.

The Commission seeks comments from the public and any interested parties in respect of the industry administrative functions performed by the Department of Transport and the Civil Aviation Authority.

Further, the Commission is interested in seeking comments in relation to the effectiveness of the functions performed and whether any of these functions may be deemed as an impediment to the effective operation of the industry.

2.5 Airport Ownership and Management

In PNG, most of the Airports and terminal facilities are owned and operated by the Government through the CAA, although some remote and district airfields and related facilities are privately owned and operated by commercial interests and some missions and remote villages. Primarily, the major mining and exploration companies maintain and operate their own air fields.

The major airlines such as ANL and APNG have also built and operate terminal facilities at various provincial airports throughout the country. In terms of access arrangements for the use of these terminals, most operators do not charge access fees. However, operators have in-principle agreements to provide each other with unrestricted access.

CAA owns and operates 24 major airports of which eleven are capable of landing aircraft up to F28s or 737s equivalents and a further thirteen secondary airports which are capable of landing aircraft up to DHC- 8s. The remaining 300 minor airports are also owned by CAA but most are non-operational due to lack of maintenance. These airstrips only offer basic aviation services. There are also five private airports maintained by mining companies (Moro, Gobe, Tabubil, Lihir, and Misima) and some strips owned by timber companies which are capable of landing aircraft up to Twin Otter size.

CAA main tasks in relation to the operations of the airports are to:

- Improve, develop, maintain, and operate or manage the 24 major airports
- Carry out any business in connection with an airport;
- Facilitate and assist in the establishing of airport authorities;
- Provide aviation security services;
- Provide aviation rescue and fire-fighting services;
- Develop for airport related purposes, any land surplus to the requirements of an airport;
- Enter into licence arrangements or joint ventures with a province for that province to establish an airport authority; and
- Enter into leasing or management arrangements with a suitable person or persons, on terms and conditions to be approved by the Minister, for any airport.

The general state of these airports varies from location to location. CAA is required to maintain certain operational standards at the major and minor airports that it owns and operates. On the 2nd March, 2006, the Minister for Transport and Civil Aviation announced that, CAA has a 10 year airport maintenance program for routine resealing and maintenance works on runways and taxiways at major airports for the introduction of new aircraft such as F100's.

For the privately owned ports such as Moro, Gobe, Tabubil, Lihir, and Misima, the standard of the airstrip services and safety standards including the infrastructure can be quite high.

The smaller PNG airports suffer from the lack of maintenance and are consequentially below minimum standards. The provincial governments have the responsibility to maintain these airports, but they lack finance and skills to maintain the airports. Pilots are reluctant to use these strips which results in there being little incentive for investments in the supporting infrastructure

which in turn exasperates the limited usage of these ports as the airports are well below the minimum required standards. Accordingly, many of the airports are too hazardous for use.

The Commission seeks comments from the public and any interested parties on any matters relating to the ownership, operation, maintenance and management of airports and related facilities both major and minor airports throughout the country.

The Commission also seeks comments on the effectiveness of the current ownership arrangements and whether it contributes to any inefficiencies in the industry.

The Commission also seeks comments from the public and any interested parties on matters relating to the current state of PNG's airport infrastructure.

2.6 Aircraft Maintenance Services

Aircraft maintenance is regulated by the CAA. However, CAA does not carry out aircraft maintenance itself but issues licences to the airline operators to undertake aircraft maintenance. Licences are granted to provide compulsory aircraft maintenance services to all aircrafts. Aircraft maintenance is currently carried out by ANL and other airline operators who have their own certified aircraft engineers. The airline companies recruit qualified engineers who meet the requirements of the CAA and the airline operator to carry out aircraft maintenance.

Aircraft engineers are required to possess an 'aircraft maintenance engineer licence' in order to provide maintenance in accordance with the standards set out by CAA. Currently APNG is the only airline operator who has certified Civil Aviation Services Australia (CASA) and CAA approved aircraft maintenance engineers. By having CASA engineers in PNG APNG estimates that is able to save 20% on the cost of servicing its aircraft in Australia. ANL does not have CASA qualified engineers and as such services its aircraft servicing international routes in either Australia or New Zealand. This is despite APNG having engineers in PNG capable of providing these services. However, ANL services all of its own aircraft in PNG.

2.7 Licensing Arrangements

The Department of Transport grants "Carrier Licences" to the airline operators, while CAA is the licensing authority, who grants licences, permits and certificates to airline operators for the usage of the PNG airspace and aviation services.

The CAA awards about 20 licences/permits including appropriate certificates on an annual basis. The other smaller airline operators operate mainly charter services as well as other aerial and flight training services which services predominantly the mining townships.

These smaller airline operators must be certified under Parts 125 and 135 of the CAA air operator's certification. Part 119 is the general air operator's certification which all airline operators must satisfy the requirements contained therein.

Airline operators can be formally registered and licensed or can operate under a permit. Section 17(1)(a) gives the Director of the CAA discretionary powers to issue various industry licences, certificates and permits which also includes the issuance of permits to airline operators.

Rules made under the CAA Act may require that airline operators to have an aviation document (Licence/ Permit or Certificate) for the following purposes:

- Registration of a Papua New Guinean aircraft;
- Licensing all aircraft pilots and flight crew members, aviation security services personnel and training organisations, aircraft maintenance personnel and design, manufacture and maintenance organizations;
- Air services, including air traffic services;
- Aerodromes and aerodrome operators;
- Aeronautical navigation service providers; and
- Aviation meteorological, communications, and medical examinations.

2.8 Safety and security issues

The principal aim of regulation of the aviation industry is safety and security. Under the Chicago Convention to which PNG is a signatory, market forces and insurance companies are not permitted to set safety standards. As part of the obligations under the Chicago Convention, international airports, international operators, airspace rules and other requirements should comply with the standards and recommended practices set for aviation by the International Civil Aviation Organisation (ICAO).

During 2005, the CAA achieved certification for the PNG Civil Aviation rules which are based on the ICAO requirements. These rules govern the safe operations of air transportation within PNG. At present CAA meets the minimum safety standards specified in the Civil Aviation Regulations Part 171 of the Air Traffic Services Technical Standards, Part 172 for Air Traffic Services Operational (Air Traffic Control) and Part 139 of Jacksons International Airport requirements³. This certification indicates that CAA has responded to safety standard and minimum standards of service provision.

³ Post Courier Pg: 13, 2nd March 2006

Recently, the Australian Government, through its overseas aid department, AusAid, committed funds to the Balus Program which has the primary goal to enhance safety, and efficiency in the PNG civil aviation service sector in a sustainable manner. The program is designed to facilitate access to the air transport network; and to ensure safe, smooth flow of passengers, aircraft and cargo within that system so that it can contribute to the economic and social development of PNG.⁴

In terms of security, Part X and XV of the CAA Act have provisions designed to enhance aviation security and safeguard international civil aviation operations against acts of interference, and protect persons and property from dangers arising from the aviation industry.

One issue of concern in PNG has been the continuous vandalism of aircraft navigation equipment installed at the airports around the country. Vandalism of the airport navigational equipment is costing the Authority approximately K8 to K9 million annually.⁵

The Commission seeks comments from stakeholders regarding the effectiveness of the safety and security aspects of the industry. In particular, the Commission is seeking to understand what impacts, if any, these matters have on the efficiency of the industry.

2.9 Community Service Obligation

The CAA seeks to recover its costs through various charges made on the industry. However, it is not able to achieve full cost recovery because of the potential impact on the continuing viability of some of the operators in the industry. Thus depending on the government's willingness to provide necessary funding, CAA will pursue additional renovations and improvements to terminal facilities and other related airport services beyond that which it is currently able to fund. These costs are currently beyond CAA's financial capabilities and as such the CAA argues it will require a CSO to provide for these upgrades.⁶

Many airports and airways routes in PNG could not support full cost recovery by the CAA. However, these airports and routes provide essential services to isolated communities, allowing them to participate in the broader social and economic life of the country.⁷

⁴ Correspondence Rules Rewrite Team (Submission to CAA)

⁵ *ibid* Pg 3

⁶ *Ibid* Pg 13

⁷ CAA Budget papers Pg 27



It is recognised by the CAA, the industry and the Department of Treasury and Finance that the domestic industry, and the clients they serve, could not afford to support full cost recovery of facilities that, from a commercial perspective, are under recovering their operating costs. The cost incurred by CAA are partially recovered from the industry, but the balance of the cost as well as depreciation, major capital works and periodic maintenance, and debt servicing costs have been subsidized by governments (national and/ or provincial) as part of a government CSO. Currently, CSOs are still part of the government's annual budgetary assistance to CAA notwithstanding that CAA is able to fully recover its costs for Jacksons Airport and Air Traffic Services.

3. THE CURRENT STATE OF THE MARKET

3.1 The Market

The bulk of the passenger air travel to and from PNG is business and expatriate travel, the latter on business or travelling to and from Australia. The only scheduled international services operate into Port Moresby. Recent Government announcement indicated that the Gurney Airport in Milne Bay may in future potentially be an international airport for the purposes of promoting the tourism industry. Only five percent of arrivals by air are the leisure purposes.

A range of dedicated regular charter services to and from Australia operate for several mining companies. APNG is the main charter operator in this field. Domestic operations are extensive and frequent and are vital in the absence of road links.

There are irregular freight charters to Japan, carrying tuna and other marine products, although most of this traffic is hubbed through Australia. Freight is carried into Asia by ANL as part of its passenger links to Manila and Singapore. There is a strong market for air freight into PNG. This consists of documents, fresh food products, and components for machinery for the mineral and transport sectors.

There are 183 aircrafts currently registered on the civil register in Papua New Guinea under the P2 national identity label operated by 39 air service operators. These 39 air service provide the following services:

- International services;
- Scheduled domestic air transport; and
- Private charter operators for both domestic and international services.

There are 453 pilots licensed by the CAA and 410 licensed engineers. There are upwards of 400 landing strips and 24 major domestic airports.

Until 2001, domestic fares were regulated under the Prices Regulation Act. During this time ANL was unable to sustain operations as revenues were below costs. Since 2001, after the deregulation of the fares, ANL has made significant increases of around 20% to domestic fares. This has also resulted in a return to profitability for ANL which has reported an operating profit on its domestic operations⁸ for last two years. Currently there is no regulation of airfares in PNG. However, the airline industry is covered by the boarder market conduct provisions of the ICCA Act.

⁸ www.airniugini.com.pg//html/news

3.2 Domestic Air Services

There are more than 30 licensed air service operators in the aviation market. Amongst them, ANL and APNG are the only airlines currently licensed as international as well as domestic operators, with another nine licensed third level operators and 21 others licensed as charter and aerial services. Table 3.1 sets out the existing operators in the various categories of the market.

Table 3.1: Existing Air Service Operators

Operators	Category				
	International Airline	Domestic Airline	Third Level Airline	Charter & Aerial Services	Flying School
Air Niugini	✓	✓	✓	✓	
Qantas	✓				
Airlines PNG	✓		✓	✓	
Airlink			✓	✓	
Hevilift			✓	✓	
Islands Airways			✓	✓	
Islands Nation Air			✓	✓	
Regional Air			✓	✓	
Trans Niugini Airways			✓	✓	
Missionary Aviation Fellowship			✓	✓	
Mapmakers				✓	
Heli Niugini				✓	
Moresby Air Services				✓	
Tropic Air				✓	✓
Pacific Helicopters				✓	
South West Air				✓	
National Aviation Services				✓	
Royal Police Wing				✓	
Air Transport Squadron				✓	
Government Flying unit				✓	
North Coast Aviation				✓	
PNG Adventist Association				✓	

CAA and ICCC analysis

There is some direct competition between the charter operators and major scheduled services domestic third level operators. However, the third level operators basically schedule their services to complement the existing routes and schedules operated by the major domestic operators. Several third-level airlines compete for service among domestic destinations within PNG. It has been argued that high airfares in PNG means that air services meets the needs

of the business traveller but is unaffordable for the majority of the population and uneconomic for most freight⁹ .

3.3 Air Niugini Limited (ANL)

ANL commenced operations as a subsidiary of the NAC¹⁰ which was established as a statutory Authority prescribed under the NAC Act in 1973 to provide aviation services as the national flag carrier throughout PNG and abroad. NAC Act gives the NAC responsibility to:

- Establish a national airline;
- Transport passengers and goods for reward by air;
- Transport mail;
- Engage in other activities to the extent that they are within the limits of the powers of the Commission under a provision of this Act other than this section;
- Provide for reward, aviation services and such other related services as can conveniently be provided by the use of the resources of the Commission;
- Carry out the policy of the National Executive Council as directed from time to time; and
- Prepare an annual financial report for the Minister for presentation to the Parliament,

In June 1996, the government embarked on a major economic reform strategy which included the resuscitation and eventual privatization of major state owned enterprises and commercial statutory authorities which included the NAC and subsequently ANL as a subsidiary of NAC. Air Niugini was then corporatised and eventually incorporated as a company under the PNG *Companies Act* 1997 to become known as Air Niugini Limited (ANL).

The primary objectives of the privatization strategy pursued by the Government at that time were to:

- Remove political involvement and or interference in commercial activities;
- Improve operational and financial performance of state owned business by improving their corporate governance; and
- Using proceeds to retire public debt.¹¹

To date ANL has not been privatized. In essence there are two existing government owned aviation entities one being the company ANL under the

⁹ Integrated Safeguards Data Sheet (Updated), Papua New Guinea: Highlands Highway Rehabilitation Project, Project ID: P059066, 09/12/202, p.2

¹⁰ National Airlines Corporation

¹¹ Government White Paper on Privatization Policy. September 2002.

Companies legislation and the other being NAC, which is a commercial statutory authority. Whilst the Commission understands that the NAC Act was to be repealed to reflect the cessation of NAC. This process is yet to be finalised. The IPBC holds the shares in ANL in trust for the Independent State of PNG.

ANL provides international services through a code sharing arrangement with Qantas. It operates an aircraft fleet consisting of B767-300, F100, F28-4000s, F281000s and Dash 8-200 aircraft. The B767-300 and Forker 100 service the Australian and other overseas routes. The latter aircraft services the Cairns-Port Moresby route. Direct international services also operate to Honiara (twice weekly with Forker 100), Singapore, Manila, and Narita. These operations rely mostly on low yielding sixth freedom traffic flows between the Asian points and Australia. That is, consumers travel through PNG on route to an alternative destination, usually Australia.

ANL is the main the international scheduled operator serving PNG. APNG operates to a smaller extent in terms of its service to and from Cairns. This partly reflects the restrictive regime under the Air Service Agreements between PNG and Australia where only two licences are available for operators in PNG to operate into Australia. Another factor in this process is the role played by Qantas, which uses code sharing arrangements than supplies services independently to ensure connections to its Australian domestic network. This results in Qantas not competing on the major international route linking Sydney, Brisbane and Port Moresby. This contrasts with the situation a decade ago, when major airlines such as Cathay Pacific and Singapore Airlines, along with Ansett and Qantas operated in PNG.

ANL also operates most scheduled domestic services, covering some 16 destinations with Dash 8s, F28-4000s and F100s.

3.4 Airlines of PNG ("APNG")

APNG is the largest privately owned aviation company in PNG. It provides services within PNG and operates, on average 400 scheduled and chartered flights a week to 120 destinations¹².

APNG¹³ has a fleet of 13 aircraft comprising;

- Dash 8s;
- Beech 1900Ds;
- Twin Otters;
- C550 Citation;
- B200 Kingair; and
- Rotary Wing AOC

¹² Pacific Regional Infrastructure Study, 2004

¹³ The airline was near debt free until it acquired Qantas eight Dash 8.

In addition to the scheduled flights, APNG provides charters for the resource and mining sector throughout PNG. This includes international charter services covering Port Moresby to Cairns, Moro and Misima. APNG operates mining contracts for a variety of companies and mine sites including, Placer Dome, Oil Search, Porgera, Misima Mines, and InterOil.

3.5 International Air Services

The international segment of the market is dominated by ANL and Qantas using the code sharing arrangement. In its international operations, ANL flies to:

- Cairns;
- Brisbane ;
- Sydney;
- Singapore;
- Manila;
- Narita; and
- Honiara.

During 2004, there were about 61,000 international travellers using these services. Of these, 62 per cent were business and government visitors and 38 per cent were tourists and those visiting friends and relatives. The Airline's wholesale programs and holiday packages from Australia, and marketing initiatives in Europe, Asia and the USA, in co-operation with the PNG Tourism Promotion Authority (TPA), made a major contribution to an increase in tourists to PNG¹⁴ in recent years.

According to ANL, its market share has increased on the key Port Moresby to Brisbane, Cairns and Sydney route from 51.6 per cent in 2003 to 53.4 per cent in 2004¹⁵. The remaining market share is sold to Qantas under the code share arrangement. APNG's recent introduction of a regular Port Moresby-Cairns service is providing the first real competition to ANL for some years¹⁶.

3.6 Other Air Services Operators

Apart from ANL, there are more than 30 other licensed air service operators in the PNG aviation market. Amongst them, APNG and Airlink are the two major privately owned operators. APNG is currently licensed as an international and third level carrier whilst Airlink is only licensed as a third level carrier and is restricted to operate scheduled flights within PNG. There are also eight other smaller third level licensed domestic passenger and charter carries within PNG.

¹⁴[http:// www.airniugini.com.pg/news/index.htm](http://www.airniugini.com.pg/news/index.htm)

¹⁵ Air Niugini, Market developments, 2005

¹⁶ APNG's weekly flights from Port Moresby to Cairns could be seen as some sort of a competition although, it does not place the incumbent (ANL) under any competitive pressure

Although there is some direct competition between the charter operators and major domestic third level operator, the smaller operators basically schedule their services to complement the existing routes operated by ANL.

ANL is the dominate player in the market for scheduled services and operates as the major operator in terms of both load factor and fleet utilisation rate due to its ability to realise cost efficiencies across its operations and its ability to cross subsidise between its international and domestic operations.

3.7 Passenger and Freight Charges

3.7.1 Domestic Passenger Fares

Up until 2001, passenger fares were regulated under the *Prices Regulation Act*, the fares were fixed to certain level. However, since 2001, passenger fares have been deregulated. Subsequently, airfares for all routes serviced have been set by the airlines themselves.

The ability to raise fares is constrained to some extent by public pressures and, increasingly, by the price sensitivity of the bottom end of the market. While there appears to be a growing proportion of expatriate and government business travel, while travel demand from smaller businesses and the general public is steady. A report by the ADB in 2000 found that passenger fares are significantly higher than any country within the region. They are much higher than those operating in Fiji, Vanuatu and Solomon Islands.¹⁷

Table 3.2 provides details the current schedule of ANL's domestic passenger fares.

¹⁷ Report to PNG Department of Works and Transport, ADB TA 3619

Table 3.2: ANL's Domestic Passenger Fare

	GUR	BUA	GKA	HKN	KVG	CMU	LAE	LNV	MAG	MAS	MDU	HGU	PNP	POM	RAB	TIZ	VAI	WBM	WWK
ALOTAU		1006	667	701	881	663	563	1025	665	856	747	675	463	369	849	808	988	763	822
BUKA			1054	460			710	1411	820			1043	849	738	309				966
GOROKA				748	928	710	610	1072	713	904	794	722	510	416	896	855	1035	811	869
HOSKINS					293		353	1105	463	917	828	738	543	432	252	888	804	844	638
KAVIENG							546	1286	562	327		918	724	612	256				831
KUNDIAWA							606	1068	709			718	506	412					865
LAE								967	210	403	689	600	405	294	502	750	913	706	385
LIHIR ISLAND									1070	1261	1152	1080	868	774	1253	1212	1393	1168	1227
MADANG										335	792	703	508	397	611	853	442	809	276
MANUS												894	699	588	1067				1040
MENDI												802	590	496	976	179			949
MT HAGEN													518	406	886	863	1025	818	859
POPONDETTA														212	672	651	831	606	665
PORT MORESBY															580	557	719	512	553
RABAU/TOKUA																1036	917	992	787
TARI																			1010
VANIMO																			266
WAPENAMANDA																			965
WEWAK																			

Source: ANL and ICCC analysis

The fares above are base rates which are exclusive of GST, insurance surcharge per sector of K15 and fuel surcharge of K42 as well as terminal facility charge of K10 for Port Moresby departures only.

ANL also has special domestic fares during non-peak periods. These special fare arrangements start on the 4th February and end on the 4th December each year. The discounted rates are grouped into different categories as follows:

- Wantok fare 50% of normal economy return fare;
- Weekender fare: 60% of normal return fare; and
- Nambawan fare: 70% of normal economy return fare.

3.7.2 Air freight and courier market

There is a strong market for air freight and courier services in PNG. This consists of documents, some fresh vegetables and produce, components for capital machinery, and mail services. Operators generally have full load factors on outward bound services from the major port, i.e. Port Moresby or Lae, but are generally almost empty on inward bound services, i.e. once they have dropped their cargo off to the various mining or remote townships throughout PNG. ANL's indicative freight rates for domestic general cargo are detailed in the table below:

Table 3.3: Domestic Cargo rates

	GUR	BUA	GKA	HKN	KVG	CMU	LAE	LNK	MAG	MAS	MDU	HGU	PNP	POM	RAB	TYZ	VAI	WBM	WWK
ALOTAU	9.5	5.67	6.41	8.24	5.88	5.09	9.19	6.14	8.03	6.67	6.2	4.04	3.15	7.88	7.19	9.29	6.93	7.67	
BUKA		9.87	4.57	4.73	10.13	7.19	13.39	8.24	6.93	10.92	10.45	8.35	7.4	3.1	11.39	11.29	7.77	9.66	
GOROKA			6.83	8.66	6.3	5.46	9.61	6.51	8.4	7.09	1.79	4.46	3.52	8.35	7.67	9.71	7.35	8.09	
HOSKINS				2.94	7.09	3.52	10.34	4.73	6.35	7.82	7.4	5.25	4.57	2.52	8.4	10.55	8.19	6.41	
KAVIENG					8.72	5.46	11.71	5.62	3.31	9.4	9.19	7.09	6.14	2.57	9.87	7.67	9.77	9.14	
KUNDIAWA						5.78	9.71	6.72	8.66	7.19	6.83	4.57	3.78	8.56	7.77	8.77	7.46	8.3	
LAE							8.98	2.21	4.46	6.46	5.99	3.89	3.05	4.99	7.09	9.14	6.77	3.83	
LIHIR ISLAND								10.03	11.92	10.45	10.13	7.88	7.09	11.81	11.08	13.18	10.82	11.6	
MADANG									5.15	7.46	7.09	4.88	3.99	6.14	8.03	10.13	7.82	2.84	
MANUS										9.19	8.93	6.77	5.88	4.83	9.66	5.36	9.5	6.88	
MENDI											7.61	5.36	4.52	9.29	1.63	10.71	n/a	9.08	
MT HAGEN												4.99	4.1	8.87	8.14	10.24	7.93	8.61	
POPONDETTA													1.94	6.77	5.93	8.14	5.62	6.64	
PORT MORESBY														5.83	5.04	7.19	4.78	5.51	
RABAU/TOKUA															9.82	9.19	9.66	7.88	
TARI																11.24	8.87	9.61	
VANIMO																	11.13	2.73	
WAPENAMANDA																		9.45	
WEWAK																			

Source: ANL and ICCC analysis

These are variable rate per kilogram in Kina terms. The flagfall charge is K30. These rates are exclusive of Goods and Services Tax (GST).

The Commission seeks comments from interested stakeholders regarding the structure of the air services pricing.

4. ISSUES

There are a number of issues in the PNG Air Transport industry which are likely to provide potential barriers to competition. The Commission must consider issues in the context of the overall economic efficiency as there may be overriding factors which would justify the continuation of these barriers to competition. As such throughout this review the Commission will be very mindful of its task at hand, to review the current arrangements in terms of economic efficiency. This section provides an overview of some of the issues the Commission has identified as potential barriers to economic efficiency in the PNG economy resulting from the current arrangements in the air transport industry. This list is no way comprehensive and the Commission seeks comments from all parties as to any additional issues which have not been raised in this section.

4.1 Tourism Issues

Tourism has the potential to have a major impact in the PNG economy. At present, it is an important foreign exchange earner for PNG and contributes about 2.5 percent to the Gross Domestic Product (GDP). In terms of air transport, airfare is the single biggest expenditure by tourists to PNG. It accounts for about 47.2 percent of their total spending. Of this, international airfare accounts for about 83 percent and domestic airfares accounts for about 17 percent¹⁸.

A report by the Asian Development Bank in 2000 found that passenger fares in PNG are significantly higher than any countries within the region. They are much higher than those in Fiji, Vanuatu and Solomon Island.¹⁹ The Tourism Promotion Agency has identified higher fares as one of the core impediments to tourism growth in PNG. The TPA has noted that one of the reasons for the high ticket prices is the tax component built in ticket prices.

In preliminary discussions with the industry, the Commission has been made aware that ANL, as the largest operator in PNG, is often used by travel agents as the default service provider in the distribution system when customers are booking travel throughout PNG. This potentially results in an unfair competitive advantage to ANL as consumers are not allowed to choose between carriers. This may lead to information break down which negatively impact the efficiency of the market.

¹⁸ Tourism Promotion Authority, *Tourism Expenditure*, 2005

¹⁹ Report to PNG Department of Works and Transport, ADB TA 3619

The Commission seeks comments from stakeholders on the validity of travel agents using a default service provider. Does the position of a default service provider result in an unfair competitive position over other service providers?

4.2 Airport Infrastructures Issues

There are 24 major airports in PNG in addition to the international airport at Port Moresby. Of those seven can handle international traffic. However, only Jackson airport is currently operating as an international airport. The major issue associated with this infrastructure is the low standard of upkeep on these potential international airports. This has been primarily driven by a lack of funding²⁰. As a consequence of the poor state of individual airports there has been a decline in the level of traffic utilising many airports. This has in turn resulted in a reluctance to spend money on the existing infrastructure which consequently exasperates the problems associated with service standards at airports.

As noted, there are in excess of 300 air fields in PNG which are under the control of the CAA. The decentralised nature of PNG population has facilitated a situation where there are numerous airfields throughout the country. At the same time this has meant that demand for many airfields is actually very low. The decentralisation of the aviation industry may have resulted in an over capacity in terms of airstrips which needs to be carefully considered in the context of the overall performance of the industry.

The Commission seeks comments from stakeholders as to whether or not the existing airport infrastructure should be rationalised to support a higher concentration of services which are in turn more profitable to operate.

The majority of airport infrastructure assets are currently owned by the Government through the CAA. In a number of countries, there has been a transfer of ownership of airport infrastructure from public ownership to the private sector. This has been based on the assumption that the private sector is more efficient in terms of delivering the necessary services to airport customers. It also provides incentives to owners to compete for air traffic by providing better services than competing airports.

²⁰ The Commission is aware of the Australian government's Balus Programme which has initiated an extensive programme to provide funding to upgrade all airport infrastructures in PNG.

The Commission is seeking stakeholders' views as to whether or not the current ownership structure of airports is limiting competition in the provision of airport infrastructure.

There is a concern expressed by some participants in the industry that there was a lack of terminal space, including access to terminal gateways, tarmac parking, freight and passenger terminal facilities and other air side and passenger side facilities. This lack of space is limiting the ability of industry participants to expand their activities and is generally consistent with the issues raised above regarding the facilities at existing airports. The existing allocation of terminal space in favour of one carrier over another could also potentially be a form of non tariff barrier to entry which needs to be addressed as part of this review.

The Commission seeks submissions from stakeholders on the availability and allocation of existing airport terminal space.

4.3 Service adequacy

Various freight companies and users of aviation services have raised concerns in respect of the current charges including the amount of space available for freight and courier services on international routes. Concerns were also raised in relation to preferential treatment of operators for their own freight which results in undue delays faced by the other freight and courier companies seeking to use the airlines concerned. This situation arises due to carriers filling their aircraft with their own goods to capacity before they are able to take additional cargo on board. Given this apparent capacity constraint some of these companies have called for another international wide body aircraft to operate the international routes. There may also be issues raised under the ICCC Act from the behaviour of freight carriers should preference to their own freight over freight from other competitors.

While some form of alternative transport may be available, for example by ship, this may take longer to deliver and not meet the requirements of the market.

The Commission invites comments and submissions from the public, stakeholders and any interested parties on the level of air services, particularly freight and passenger services, and whether there is adequate services to cater for the needs of all air sector users.

4.4 International Issues

In accordance with provisions of section 162(6) of the CAA Act, ANL and Qantas have entered into a commercial arrangement known as Code Share under which

ANL has replaced its A310 aircraft with a B767-300, compatible in configuration with Qantas aircraft of this type, and has taken over flight operations on the profitable route from Port Moresby to Sydney via Brisbane. Qantas has participated on all services as ANL's code share partner, but no longer services this route with its own aircraft. There are currently 18 services per week on this route. Three of the services operated by ANL operate on the Brisbane-Port Moresby sector. ANL and Qantas also code share the Port Moresby to Cairns route. However ANL now faces competition from APNG on this route.

According to the terms of the agreement, Qantas code share on a "hard block" basis on each ANL B767-300 service. The block involves the purchase of 12 business class and 70 economy seats on each ANL flight. Qantas also has an option to purchase up to a further 4 business and 30 economy seats ("soft block")²¹. Furthermore, Qantas is also required to purchase cargo space on each space on a similar basis.

The code share arrangement ensures the continuation of ANL international services. The benefits associated with ANL operating this route were deemed to be too important and as such a joint arrangement between ANL and Qantas was deemed to be more efficient than both carriers exiting the market. The impact of this might be strongly felt in flow-on consequences for tourism and other aviation related industries. However, the already limited degree of competitive pressure on airfares on this route is lessened further under the current arrangement which covers all sectors on the route.

The claimed economic merits of this arrangement are that without such commercial arrangement ANL would be commercially forced to withdraw from the route or otherwise disadvantaged in terms of cost outruns. The continuation of services is vital to maintaining commercial and social links between Australia and PNG and other internal destinations. In the absence of a commercial arrangement, it is argued that ANL would have to shut down its entire international segment of the market, with adverse impacts on its domestic operations. Under this arrangement, ANL had access to more modern aircraft, with a considerable higher utilisation rate that provides improved cost recovery and efficiencies.

The code sharing arrangement, while advantaging ANL, may act as a barrier to new entrants into the market. In effect, while allowing ANL to achieve a better cost recovery outcome, other companies may find the entry costs too high to consider the route into PNG a potential option as part of their international networks.

The Commission seeks comments from stakeholders on the current access arrangement for new entrants into the PNG international segment of the airline market.

²¹ International Air Services Commission, Decision [2002] IASC 219,

4.5 Training

The skill and commitment of staff working in the air transport industry is vital to the economic efficiency of the industry. A lack of adequate training facilities may result in staff either receiving training at a lower standard than appropriate or in the costs of such training being prohibitive. Qualifications from one country should where possible be recognised in other country where the standards are consistent. A lack of recognition of qualifications can be used as a barrier to entry and can have a consequential flow on affect for air transport costs in PNG

The Commission seeks comments from stakeholders as to the adequacy of training facilities within PNG. In particular, the Commission is seeking to understand whether or not the current training regime is sufficient to provide pilots and crew capable of piloting and servicing aircraft to an appropriate standard.

The Commission is also interested in understanding how pilots and crew are accredited to perform these functions.

The Commission seeks comments from stakeholders on the issue of recognition of qualifications received in other jurisdictions.

The Commission seeks comments as to whether these requirements represent a barrier to new entrants entering the market.

4.6 Cross subsidisation

The three main operators provide services over the main routes from Port Moresby. The main national carrier, ANL, services most major domestic destinations direct from Moresby. However, on certain routes it schedules its flights to fly in a triangle fashion over two or three destinations before arriving back at Port Moresby. This process of triangulation is common throughout the industry as it increases the airlines ability to maximise its load and utilisation factors. While the other two major carriers also provide services to these destinations they have lower frequency in terms of availability and there is a tendency to provide these flights on the basis of a timetable that does not directly compete with ANL. The decision to not compete directly with ANL on a timetable scheduling basis may be a commercial decision. That is, ANL is able to provide flights at a lower costs base due to the economies of scale it is able to achieve through its larger fleet and load configurations compared to the alternative operators. However, if ANL as the dominant market player is able to cross subsidise routes to protect its position in the market as a whole, it may be inappropriately exercising its market power to minimise competition.

The Commission seeks comments from stakeholders as to whether any participant in the market is able to exercise its market position to minimise competitive pressure from other service providers.

The Commission seeks comments from stakeholders as to the level of cross subsidisation in the industry from any route to another route. The Commission is seeking to understanding the rationale for this cross subsidisation.

4.7 Industry Outlook

In reviewing the air transport industry the Commission is interested in the likely future direction of the industry, in order to address issues and trends which are likely to emerge over the next ten years. In doing so the Commission is not attempting to forecast market outcomes. However, the Commission is attempting to ensure that all potential market outcomes are considered in the context of a potential improvement in the competitive environment.

The Commission seeks views from stakeholders on the likely developments or changes in the existing structure of the air transport industry including entry of new service providers, over the next decade.



Appendices

Appendix A: Official Terms of Reference

Appendix B: Overview of relevant Legislation in the Industry

Appendix C: Airlink's passenger fare and freight grid

Appendix A: Official Terms of References

Inquiry under Section 123 *Independent Consumer and Competition Commission (Act) 2002*

of Certain Business Impediments in the PNG Aviation Industry

The Government is committed to fostering a more efficient and faster growing economy through removing impediments to business. The Terms of Reference herein support the 2006 Budget announcement that business impediments in the aviation industry caused by regulation and barriers to competition will be assessed by the ICCC (the Commission) with a view to identifying regulatory improvements. The inquiry is conducted pursuant with the powers of the Minister for Finance and Treasury under Section 123 of the *ICCC Act 2006*.

In establishing a review, the Government is aware, among other things, that:

- owing to the dispersed nature of PNG's population, PNG's challenging geography and the lack of alternative viable transport for many routes, provincial and international air services are an indispensable business input in PNG;
- issues surrounding aviation competition and regulation have been raised by the Business Impediments Working Group
- PNG's aviation industry supports national economic growth and development, including through facilitation of private sector activity, the delivery of core government services and by being a key partner in the expansion of PNG's tourism sector; and
- a competitive aviation sector, effectively regulated to ensure safety, can foster a more efficient transport industry capable of contributing its full potential to the PNG economy.

Specific requirements of the Inquiry

- 1) The ICCC is to examine and report on impediments to business caused by regulatory and competitive constraints in the freight and passenger domestic and international market with reference to:
 - a) the current operation of the aviation industry in PNG, including through consideration of market characteristics, the degree of competition and countervailing power within the industry, the extent of substitutability for aviation services and the contribution of aviation to the tourist industry;
 - b) the current aviation regulatory arrangements including licensing, air traffic control, air space allocations and access to essential airport infrastructure;
 - c) current pricing practices within the industry, including the existence and rationale for any cross subsidy arrangements, the comparative price

attractiveness of PNG as tourist destination within the South Pacific, pricing and access arrangements for essential airport infrastructure, the setting of fees for regulatory services and the extent to which government fees or charges are incurred by the industry;

- d) possible barriers to entry and potential for the entry of new competitors into the air transport industry; and
 - e) the extent to which some aviation services and facilities are supplied implicitly as community service obligations for the purpose of attaining social objectives.
- 2) The ICCC is to identify:
- a) where justified, improvements that can be made to the efficiency of aviation in PNG through reducing regulatory costs and increasing competition; and
 - b) the potential benefits for the national economy.
- 3) In discharging its responsibilities under this review, the Commission is to consult with stakeholders, through both public hearings and submissions on specific matters as the Commission considers appropriate, and follow a three stage reporting and consultation process through:
- a) presentation to the authorizing department on the findings of 1 (a) to (e) of the terms of reference and preliminary comments on 2;
 - b) presentation of a written draft report for consideration and comments by the Government and other interested parties, including a one month opportunity for submission of written comments on the Draft Report; and
 - c) presentation of a fully documented written Final Report to the Treasurer for presentation to wider Government.

The Review is to submit its final report by 18 August 2006.

Minister for Treasury and Finance

January 2006

Appendix B: Applicable Legislations in the Industry

Legislation	Scope
National Airlines Commission Act	<p>Amongst other purposes, this legislation provides for the establishment of the NAC in order to establish and operate a national flag carrier which became known as Air Niugini. Since the corporatisation and incorporation of ANL, this legislation was supposed to have been repealed; however it has not been done so to date.</p>
Civil Aviation Authority Act 2000	<p>The CAA Act provides for the establishment of CAA to be endowed with the following functions :</p> <ul style="list-style-type: none"> • promotion and enhancement of safety standards in the civil aviation sector at reasonable costs; • operational requirements including the issuing, suspending and revocation of aviation licences; • provision of air traffic services, aeronautical communication and navigational services; • provision of meteorological services in accordance with international conventions and acceptable standards are implemented; • ownership and management of major airports throughout PNG; and • the independence of the Authority in relation to the enforcement of the relevant sections of CAA Act
Aerodrome (Business Concession) Act 2000	<p>The legislation provides for the granting of leases and licenses for business purposes on aerodromes. The purpose of Aerodrome Act is to regulate or restrict a right or freedom in and around a land designated for the purposes of:</p> <ul style="list-style-type: none"> • landing; • departure; • movement; and • servicing of aircraft • as well as any buildings in connection with the aerodrome. <p>Persons who are legally licensed and leased are allowed to operate these services.</p>
Investments Promotion Authority Act	The main objective of the IPA Act, amongst other

	<p>things, includes the encouragement and facilitation of investments in PNG. The Act enables foreign enterprises to carry on business only if certified to do so. The Act also stipulates certain business activities as “reserved activities” which may only be undertaken by citizens of PNG.</p> <p>In terms of the air transport sector, such specific activities include;</p> <ul style="list-style-type: none">• airport terminal building maintenance;• airport terminal Kiosks leases;• airport business concession leases;• airport access road design and documentation;• airport retaining wall design;• aerodrome staff housing design;• airport water supply;• aerodrome concession lease;• air services licenses; and• Navigational aids site clearance. <p>Further the following activities are reserved for national enterprises (generally an enterprise more than 50% of which is owned directly by a citizen):</p> <ul style="list-style-type: none">• Aircraft maintenance companies; and• Aircraft hangar concessions. <p>The effect of this Act is clearly to restrict competition in these activities and industries from foreign competitors.</p>
Companies Act 1997	<p>The companies’ legislation provides the reporting, corporate governance and compliance framework for all incorporated companies under this legislation. Hence airline companies or other companies involved in the industry which are registered under this legislation would be subject to its requirements including the lodging of Annual Returns, audit requirements and other compliance issues and requirements imposed by the legislation.</p>
Public Finance Management Act.	<p>Since ANL is wholly owned by the Government, it is subject to the ambit of this legislation. Furthermore, since the NAC Act has not been repealed, ANL is within the scope of this legislation and more particularly the requirements for Audit by the Auditor General of PNG even though it is incorporated as an entity under the Companies legislation.</p>

Appendix C: Airlink fare and freight grid

Table A.1: Airlink Passenger Fare

	BUA	GMI	GOE	GKA	HKN	JAQ	KDR	KVG	LAE	LNK	MAG	HGU	ATN	IIS	POM	RAB	TAJ	TIZ	VAI	WWK
BUKA																				
GASMATA																				
GONALIE																				
GOROKA		169																		
HOSKINS				577																
JAQUINT BAY			66		216															
KANDRIAN		165			217															
KAVIENG	497																			
LAE NAZAB				186	338															
LONDOLOVIT	479							333												
MADANG				221	443				200											
MOUNT HAGEN				167	600				251		257									
NAMATANAI	442							346		145										
NISSAN ISLAND	201							531		533			433							
PORT MORESBY				400	417				281		378									
RABAU	295		264	684	241	286		245	479	247	584	755	147	329	553					
TADJI				612					570		423	489			680					
TARI				339					371		429	215								
VANIMO				621					631		423	498			687		234			
WEWAK				411					369		264	287			528		245		254	

Source: Airlink and ICCC analysis

Through fares are shown in the shaded box, and apply only to Airlink flights with same day travel. If same day (through fare) travel is broken at the passenger’s discretion then additional sector fare(s) apply. Transit points for through fare are indicated by X on the ticket. For an infant under two (2) years not occupying a seat but accompanied by an adult there is no charge. These charges are only base rates and therefore are exclusive of GST, insurance charge, fuel charges and terminal dues for Port Moresby departures.

Table A.2: Airlink Air Freight Rates

	BUA	GMI	GOE	GKA	HKN	JAQ	KDR	KVG	LAE	LNK	MAG	HGU	ATN	IIS	POM	RAB	TAJ	TIZ	VAI	WWK
BUKA																				
GASMATA																				
GONALIE																				
GOROKA	9.36	1.69																		
HOSKINS	4.41			6.35																
JAQUINT BAY			0.66		2.16															
KANDRIAN		1.65			2.17															
KAVIENG	4.97																			
LAE NAZAB				1.86	3.38			5.2												
LONDOLOVIT	5.27			8.88	4.9			3.3	7.5											
MADANG	7.83			2.21	4.73				2	9.0										
MOUNT HAGEN	9.94			1.67	6.6			9.1	2.5	9.98	2.57									
NAMATANAI	4.42							3.5		1.45										
NISSAN ISLAND	2.01							5.3		5.33			4.33							
PORT MORESBY	7.05			3.48	4.17			2.8	7.01	3.78	3.87									
RABAU	2.95		2.64	7.52	2.41	2.86		5.8	4.8	2.47	5.84	8.31	1.47	3.29	5.53					
TADJI				6.12				2.5	5.7		4.23	4.89			6.80					
TARI				3.39					3.7		4.72	2.15								
VANIMO				6.68					6.9		4.23	5.48			6.87		2.34			
WEWAK				4.52					3.8		2.82	3.16			5.51	7.53	2.45		2.72	

Source: Airlink and ICCC analysis

The basic charge to all consignment is currently K30. There are other applicable surcharges that apply such as the dangerous goods charges where goods carried fall within the definition of dangerous goods under the applicable regulation. These additional surcharges include the following:



- Carriage of acceptable dangerous goods at K75;
- Carriage of live animals which is the 175% of applicable freight rate; and
- Consigned freight delivery rate at per consignment
 - ⇒ up to 5Kg and under: K5.00
 - ⇒ over 5Kg up to 50Kg: K1.00/Kg
 - ⇒ prior arrangement for 50Kg