

DETERMINATION

RENEWAL OF DETERMINATIONS A-9 AND B-4 ALLOCATING CAPACITY ON THE JAPAN ROUTE TO QANTAS AIRWAYS LIMITED (ACN 009 661 901)

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1. The Determination subject to renewal

1.1. On 22 July 1992, the Minister issued Determinations A-9 and B-4 (the determinations) which allocated a total of 52 B767-200 units of capacity per week to Japan to Qantas Airways Limited ACN 009 661 901 (Qantas). Determination A-9 was subsequently amended by Decisions IASC/DEC/9303, IASC/DEC/9504 and IASC/DEC/9608 which varied the aggregate allocation of capacity to 51 B767-200 units of capacity per week and approved the operation of code share services with Japan Airlines (JAL) effective from 30 March 1997. Determination B-4 was originally an interim determination which was renewed by the Commission on 9 August 1993 in favour of Qantas for 5 years from 1 July 1992.

1.2. The determinations, issued under section 54 of the *International Air Services Commission Act 1992* (the Act) and effective from 1 July 1992, expire on 30 June 1997.

2. The applications

2.1. The Act requires the Commission to commence its consideration of the renewal of a determination at least 12 months before that determination is due to expire. In accordance with its procedures, on 20 May 1996, the Commission invited Qantas to express its interest (or otherwise) in renewing the determination. On 24 May 1996, Qantas wrote to the Commission seeking a renewal of the determination.

2.2. On 21 June 1996 the Commission published a notice inviting submissions from any interested person about the renewal of the determination and other applications for an allocation of all or part of the capacity that is subject to renewal. The closing date for submissions and other applications was 19 July 1996. An application was received from Ansett International Limited ACN 060 622 460 (Ansett) for 14 B767-200 units of capacity to enable it to operate a daily B747 service Sydney - Tokyo - Brisbane - Sydney.

2.3. All non-confidential material supplied by the applicants is filed on the Register of Public Documents. Confidential material supplied by the applicants is filed on the Commission's confidential register. A copy of the Qantas - JAL Memorandum of Understanding of Cooperation is filed on the Commission's confidential register.

3. Submissions

3.1. Submissions were received from the:

- Australian Competition and Consumer Commission (ACCC);
- Queensland Office of Tourism (QOT);
- Western Australian Tourism Commission (WATC);

- Board of Airline Representatives of Australia (BARA);
- Northern Territory Tourist Commission (NTTC);
- Flight Attendants Association of Australia (FAAA); and
- Australian and International Pilots Association (AIPA).

3.2. The ACCC argued that scarce capacity should be allocated in a manner which would encourage the entry of new carriers. The WATC supported the concept of a competitive environment, as long as any competition is by a competent, efficient, viable and experienced operator. The WATC stated that it had “no major concerns” with Qantas and expressed a preference for increases in capacity rather than have airlines battling for market share of existing capacity. The FAAA and AIPA both supported Qantas’ current operations. The BARA and the NTTC declined to make any specific comments about the applications.

3.3. Ansett originally submitted that:

- whether a route has been effectively serviced requires some assessment of whether the service provided on that route has satisfied the objectives underlying the allocation of capacity and whether the results contemplated by that allocation of capacity have been achieved;
- that such an evaluation should comprise a review of the performance of the incumbent carrier on that route in light of the criteria specified in sections 4 and 5 of the Policy Statement;
- Ansett’s entry on routes throughout the Asia-Pacific region has stimulated the inbound travel market;
- Qantas has little incentive to develop tourism from Tokyo as Narita Airport is effectively closed to new competition;
- slots are not the property of individual airlines and therefore if Ansett is allocated capacity to Tokyo, there is an obligation for it to be given some of the slots at Narita currently used by Qantas; and
- there would be greater public benefits if Ansett were granted additional capacity rather than renew all of Qantas’ allocation.

3.4. In response to the Draft Determination, Ansett submitted that:

- one of the reasons for the slow down in growth of inbound tourism from Japan is the high cost of air fares and that more competition, particularly in the Tokyo market, would be an important means of overcoming this problem;
- additional competition in the Tokyo and Nagoya markets would benefit inbound tourism but that slot constraints at both airports mean that Ansett is restricted from entering these markets;
- the Qantas and Japan Airlines alliance is further evidence of a likely future lack of competitive product in the market, particularly at Tokyo;
- Qantas' performance in relation to consumer and tourism benefits criteria has been lacklustre given the size and economic scope of the Japanese inbound market;
- the fact that Qantas overhauled its business class product in response to the service standards offered by Ansett does not affect the majority of tourists because they travel in economy class; and
- the current allocation of Australian capacity does not satisfy the competition policy and industry structure criteria contained in paragraph 5.1(d) of the Policy Statement.

3.5. On 21 October 1996, Qantas made a submission stating that no evidence had been provided by any interested party which would lead the Commission to conclude that Qantas has not serviced the route effectively.

3.6. Copies of the submissions are filed on the Register of Public Documents.

4. Current services to Japan

4.1. Subsequent determinations by the Commission have increased Qantas' total weekly capacity allocation to 63.2 B767-200 units of capacity between Australia and Japan. Its capacity is operated as follows:

- Sydney* - Tokyo & v.v. (seven B747 services per week);
- Sydney* - Cairns - Nagoya & v.v. (seven B747 services per week);
- Brisbane - Cairns - Tokyo & v.v. (six B747 services per week);
- Brisbane - Cairns - Tokyo - Brisbane (one B747 service per week);
- Sydney - Brisbane - Tokyo & v.v. (one B747SP service per week);
- Cairns - Fukuoka - Cairns - Melbourne (two B767-300 services per week);
- Cairns - Fukuoka - Cairns - Brisbane (one B767-300 service per week);
- Sydney - Cairns - Fukuoka - Cairns (one B767-300 service per week);
- Perth - Tokyo & v.v. (two B767-300 services per week);

- Perth - Tokyo - Darwin - Perth (one B767-300 service per week);
- Sydney - Cairns - Sapporo - Cairns (two B767-300 services per week);
- Cairns - Sapporo & v.v. (one B767-300 service per week);
- Sydney - Osaka - Brisbane - Sydney (five B767-300 services per week); and
- Melbourne - Osaka - Cairns - Melbourne (one B767-300 service per week).

* A number of services originate in Melbourne, involving a change of aircraft at the Sydney International Terminal.

4.2. Qantas fully utilises all of its allocated capacity.

4.3. Ansett has been allocated ten B767-200 units of capacity per week and fully utilises its capacity as follows:

- Sydney - Osaka - Brisbane - Sydney (five B747 services per week)

4.4. JAL operates the following services between Japan and Australia:

- Tokyo - Sydney & v.v. (seven B747 services per week);
- Tokyo - Cairns - Brisbane & v.v (seven B747 services per week);
- Osaka - Cairns - Sydney - Osaka (three B747 services per week); and
- Osaka - Brisbane - Sydney - Osaka (four B747 services per week).

4.5. All Nippon Airways operates the following services between Japan and Australia:

- Tokyo - Sydney & v.v. (four B747 services per week);
- Tokyo - Brisbane - Sydney - Tokyo (three B747 services per week); and
- Osaka - Brisbane - Sydney - Osaka (two B767 services per week).

4.6. Air New Zealand operates the following services between Australia and Japan:

- Auckland - Brisbane - Osaka & v.v (two B767 services per week).

5. Relevant route characteristics

5.1. The Commission considered the characteristics of the Australia - Japan route in its determinations allocating capacity to Ansett and Qantas in 1993 (Determinations IASC/DET/9308 and 9309).

5.2. In assessing the various submissions made in this case, the Commission has analysed the statistics on inbound tourism from Japan.

5.3. According to those statistics, inbound tourism has continued to grow since 1991 (although below the forecasts of the Bureau of Tourism Research and Australian Tourist Commission referred to in the earlier determinations) as shown in the following table:

Year ended 31 December	Short Term Visitor arrivals from Japan	Annual Growth rate compared with previous year:
1990	479,709	-
1991	527,826	10.0%
1992	629,555	19.3%
1993	670,899	6.6%
1994	719,277	7.2%
1995	781,845	8.7%

Source: Australian Bureau of Statistics

6. Provisions of relevant air services agreements

6.1. The Memorandum of Understanding of 9 December 1992 and the Australia - Japan Air Services Agreement of 27 April 1956 provide for the operation of air services between Australia and Japan, the multiple designation of Australian carriers, and for the operation of joint services between the designated airlines of each country.

7. Draft Determination

7.1. The Commission issued a draft determination on 20 December 1996 and invited submissions on the draft, requesting comments by 10 January 1997. The only submission received was from Ansett.

8. Legislative framework

8.1. The renewal of a determination is made in accordance with the *International Air Services Commission Act 1992*. The legislative framework for considering a renewal of a determination under the Act is set out in Attachment A.

8.2. Under section 11 of the Act, the Minister may make Policy Statements setting out matters relevant to the Commission's performance of its functions. The current Policy Statement (No.2) was issued by the Minister on 27 March 1995 and includes criteria to be applied by the Commission in considering the renewal of a determination.

8.3. The criteria applicable to assessing the renewal of a determination in circumstances where:

- the incumbent carrier is seeking renewal of a determination;
- the capacity is limited under a bilateral arrangement;
- the route is not in the start-up phase; and
- there are other applications for the capacity subject to renewal,

are those set out in Attachment B. Those criteria apply to these applications.

9. Commission's consideration of the renewal of the determination

9.1. Under the Policy Statement, as set out in Attachment B, there is a rebuttable presumption in favour of the carrier seeking the renewal, except where paragraph 8.1(a) applies.

9.2. Paragraph 8.1(a) does not apply in this case and therefore the Commission should allocate the capacity to the carrier seeking renewal unless the Commission is satisfied that both of the following criteria are met:

- (a) the carrier seeking renewal has failed to service the route effectively;
and
- (b) the use of the capacity in whole or in part by another Australian carrier which has applied for that capacity would better service the public having regard to the criteria set in paragraphs 4 and 5 of the Policy Statement.

9.3. The first question is, therefore, whether Qantas has failed to service the route effectively. In this regard:

- there were a number of submissions to the effect that Qantas has serviced the route effectively;
- information concerning the nature of Qantas' services over the past four years supports the submissions made by others that Qantas had serviced the route effectively; and
- a submission by Ansett suggests that Qantas has little incentive to stimulate traffic from Tokyo because Narita airport is effectively closed to new entrants due to congestion.

9.4. Of central importance to consideration of the Ansett submission is the meaning to be given to the phrase "failed to service the route effectively" in paragraph 8 of the Policy Statement.

9.5. As paragraph 8.2 of the Policy Statement makes clear, it is not unless the Commission finds that the incumbent carrier has "failed to service the route effectively" that the Commission is able to give consideration to competing applications for capacity up for renewal. This test needs to be satisfied before dealing with any other matter.

9.6. If the Commission were to regard this test as involving not much more than that a carrier had not provided the best possible service to maximise benefits to the Australian public, then it would be relatively easy to identify some aspect of the carrier's service which did not meet the required standard and regard the test as satisfied.

9.7. On the other hand, if the Commission were to regard this test as requiring it to be demonstrated that the carrier had performed quite unsatisfactorily on the route, then the test would be very difficult to meet.

9.8. Two points need to be noted in relation to paragraph 8.2 of the Policy Statement. First, the paragraph sets up a rebuttable presumption in favour of re-allocation to the incumbent carrier. Secondly, the word "failed" has been used in the relevant paragraph rather than a more neutral phrase such as "has not".

9.9. This seems to the Commission to indicate that the Minister's intention was to set a high hurdle before an incumbent airline will be judged as having failed to service the route effectively. Such an approach would appear consistent with section 8(2) of the Act which makes it clear that, on a renewal application, the Commission should make the same allocation as the original determination unless it is satisfied that the allocation "is no longer of benefit to the public".

9.10. It does not follow that the hurdle is necessarily as high as the alternative suggested above. If the test were that high it is doubtful whether it would be met except in cases of serious neglect. The position seems to the Commission to be somewhere between the two extremes.

9.11. In order to rebut the presumption in favour of the incumbent carrier the following would seem to the Commission to be relevant considerations:

- The public interest will best be served if a carrier utilises capacity in a manner which maximises achievement of the criteria set out in paragraph 5.1 of the Policy Statement to the extent that those criteria are relevant. However, a carrier will not be regarded as failing to service a route effectively merely because the public interest is not maximised by the manner in which the carrier services the route.
- Furthermore, a carrier will not be regarded as failing to service a route effectively merely because another carrier offers a service proposal that might better serve the public interest.
- Some significant deficiency in the way in which the carrier must be established before an incumbent carrier will be regarded as failing to service the route effectively.
- Whether or not there is such a deficiency is a matter to be considered on a case by case basis.
- The presumption that the incumbent carrier has serviced the route effectively can only be overturned by evidence that demonstrates the claimed deficiencies. It is not up to the incumbent carrier to show that it has serviced the route effectively.

9.12. In applying this approach, the Commission sees merit in the Ansett submission that evaluations of the performance of an incumbent carrier should use the criteria specified in paragraph 5.1 of the Policy Statement. The Commission proposes to use relevant paragraph 5.1 criteria as a guide.

9.13. Following this approach, the Commission's assessment is:

Tourism and Consumer Benefits

- As the table at paragraph 5.3 indicates, inbound tourism from Japan has increased each year since 1990. The Commission is satisfied, based on visitor arrival statistics, that in spite of increased competition on the route the trend in Qantas passenger traffic has been positive. The Commission would expect a somewhat different trend had Qantas not been servicing the route effectively.;
- A variety of factors account for the recent decline in the rate of growth of tourists from Japan - these include a weakening of the Japanese economy. The Commission is not satisfied that, in this case, the decline can be attributed to a failure on the part of Qantas to service the route effectively.
- There is evidence that Qantas has been responsive to the changing pattern in passenger demand. Since July 1992, Qantas has introduced new services to Sapporo (under separate capacity entitlements it has also introduced services to Osaka), increased its capacity to Fukuoka and Nagoya and maintained its capacity to Tokyo.
- Qantas is the only carrier on the route operating to Japanese ports other than Tokyo and Osaka.
- There is evidence that Qantas has catered for requirements beyond Australian gateways. Qantas has provided a link between its services on the route and its substantial domestic network for passengers wishing to travel from behind or beyond the Australian gateways.
- The Commission considers that a history of serious deficiencies in cabin standards or other passenger services would be relevant to the issue of servicing the route effectively. Although Ansett has suggested that Qantas has not focused on improving its economy class cabin on the route, no evidence has been presented which would indicate that Qantas cabin standards are deficient.

Trade Benefits

- Qantas provides freight capacity on its passenger aircraft between a range of Australian and Japanese ports. There has been no evidence submitted to the Commission that Qantas has failed to satisfy freight requirements on the route.

Competition Policy

- Ansett has criticised the Qantas/JAL code share. The code share arrangement between Qantas and JAL does not come into effect until the commencement of the Northern Summer 1997 scheduling period. The code share arrangement as approved by the Commission has conditions designed to prevent anti-competitive conduct. Should there be evidence of such conduct at some future time the Commission would of course review the Qantas approval. If evidence were found that the code share arrangement was leading to anti-competitive conduct this would constitute strong grounds for believing that the airline had not been servicing the route effectively.
- Ansett has pointed to the difficulties with slot allocations at Narita. These concerns, although important, do not reflect on the effectiveness of Qantas' service on the route. The slot constraints at Narita limit the extent of competition that Qantas faces between Tokyo and Australia. Although there are three airlines offering services between Tokyo and Australia, Qantas has a code share agreement with one of the other airlines, JAL but only in relation to Cairns and Brisbane.

9.14. Taking all of the above factors into account, and accepting that access to Narita by Ansett would be likely to increase competition, the Commission does not believe it has sufficient grounds on which to conclude that Qantas has not serviced the route effectively.

9.15. Had the Commission concluded that Qantas had failed to service the route effectively, the Commission would then have assessed whether Ansett's proposals better served the public taking into account all of the matters raised by Ansett in its submissions. However, since the Commission is not satisfied that Qantas has failed to service the route effectively, there is no need to consider the matter further.

9.16. Accordingly, the Commission will renew Determinations A-9 and B-4 allocating capacity to Japan to Qantas.

10. Other issues

Terms and conditions of the fresh determination

10.1. Under section 19(3) of the Act, the Commission may make such changes (if any) to the terms and conditions included in the original determination as it is satisfied are warranted because of changes in circumstances since the original determination was made.

10.2. Since the original Section 54 Determination was made, the Commission has had an opportunity to refine the terms and conditions which should apply to its

determinations. In these circumstances the Commission believes that fresh determinations which renew original determinations should contain terms and conditions which are consistent with those applying to determinations currently issued by the Commission. These are set out below.

Period of the fresh determination

10.3. The Commission will grant Qantas a fresh determination for a period of five years effective from 1 July 1997.

Utilisation of the capacity

10.4. The Commission will specify that Qantas is required to fully utilise the capacity from 1 July 1997.

10.5. The Commission will specify that:

- the capacity is only to be used by Qantas; and
- Qantas may utilise the capacity to provide services jointly with JAL subject to the limitations specified in this fresh determination.

Ownership and control of the carrier

10.6. The Commission's view is that the determination should include the usual limitations on changes in the ownership and control of Qantas. These are specified below.

11. Determination for renewal of Determinations A-9 and B-4 allocating capacity on the Japan route to Qantas (IASC/DET/9701)

11.1. The Commission makes a fresh determination in favour of Qantas, allocating 51 B767-200 units of capacity per week in each direction between Australia and Japan under the Australia - Japan Air Services Agreement.

11.2. The determination is for five years from 1 July 1997.

11.3. The determination is subject to the following conditions:

- Qantas is required to fully utilise the allocated capacity from 1 July 1997.
- only Qantas is permitted to utilise the capacity;

- Qantas may use the capacity to provide services jointly with Japan Airlines in accordance with:
 - the Memorandum of Understanding of Co-operation between Qantas and Japan Airlines, or as varied except in relation to:
 - the number of seats to be exchanged exceeding 1500 per week in each direction; or
 - the number of services to be operated; or
 - the city pairs served; or
 - any financial adjustment;
 - variations to the Memorandum of Understanding of Co-operation which relate to any of the excepted matters referred to above, subject to the prior approval of the Commission; or
 - any new joint service arrangements between Qantas and Japan Airlines for operations on the Australia - Japan route, whether or not it replaces the existing agreement, with the prior approval of the Commission;

and, in any case, in accordance with the Determination;

- to the extent that the capacity is used to provide joint services with Japan Airlines:
 - Qantas must price and sell its services on the route independently;
 - Qantas must not share or pool revenues under any such agreement; and
 - Qantas must take all reasonable steps to ensure that passengers are informed, at the time of ticket reservation, of the carrier actually operating the flight.
- changes in relation to the ownership and control of Qantas are permitted except to the extent that any change:
 - results in the designation of the airline as an Australian carrier under the Australia - Japan Air Services Agreement being withdrawn; or
 - has the effect that another Australian carrier, or a person (or group of persons) having substantial ownership or effective control of another Australian carrier, would take substantial ownership of Qantas or be in a position to exercise effective control of Qantas, without the prior consent of the Commission, and

- changes in relation to the management, status or location of operations and Head Office of Qantas are permitted except to the extent that any change would result in the airline ceasing to be an airline designated by the Australian Government for the purposes of the Australia - Japan Air Services Agreement.

Dated: 20 January 1997

James K Bain
Chairman

Brian L Johns
Member

Russell V Miller
Member

A. Legislative framework

1. Under subsection 17(1) of the Act, the Commission must start its consideration of the renewal of a determination at least 12 months before the end of the period during which the determination is in force.

2. Under subsection 17(2) of the Act, before starting its consideration, the Commission must, by notice, invite submissions about the renewal.

3. Under subsection 17(3), any person may make submissions to the Commission about the renewal.

4. Under subsection 8(1), the Commission may, at any time while a determination is in force, make a fresh determination allocating capacity to which the original determination relates.

5. Under subsection 8(2), the fresh determination:

(a) must make the same allocation of capacity as the original determination unless:

(i) the Commission is satisfied that that allocation is no longer of benefit to the public; or

(ii) the original determination is an interim determination; and

(b) comes into force immediately after the end of the period during which the original determination was in force.

6. Under subsection 8(3), if the fresh determination does not make the same allocation of capacity as the original determination, it must not make a different allocation of capacity unless the Commission is satisfied that that allocation would be of benefit to the public.

7. In assessing the benefit to the public of an allocation of capacity, the Commission must apply the criteria set out for that purpose in the Policy Statement dated 27 March 1995 made under section 11 of the Act. The criteria applicable to assessing benefit to the public for the purposes of renewal of determinations are those contained in paragraph 8 of the Policy Statement.

8. Subsection 19(1) of the Act relates to the contents of determinations made under section 8 of the Act. Subsection 19(2) specifies the period during which the determination is to be in force.

9. Under subsection 19(3), in including terms and conditions in the determination, the Commission may make such changes (if any) to the terms and conditions included in the original determination (including adding or deleting terms and conditions) as it is

satisfied are warranted because of changes in circumstances since the original determination was made.

10. Section 20 relates to notifications of determinations.

B. Relevant criteria under paragraphs 5, 6 and 8 of the Policy Statement

Paragraph 5 requirements

5. ADDITIONAL CRITERIA FOR ASSESSING BENEFIT TO THE PUBLIC

5.1 The following additional criteria are applicable in assessing the benefit to the public in all circumstances other than as provided in relation to particular circumstances described in paragraph 6:

Tourism

(a) The extent to which proposals will promote tourism to and within Australia. The Commission should have regard to:

- the level of promotion, market development and investment proposed by each of the applicants; and
- route service possibilities to and from points beyond the Australian gateway(s) or beyond the foreign gateway(s).

Consumer Benefits

(b) The extent to which proposals will maximise benefits to Australian consumers. The Commission should have regard to:

- the degree of choice (including, for example, choice of airport(s), seat availability, range of product);
- efficiencies achieved as reflected in lower tariffs and improved standard of services;
- the stimulation of innovation on the part of incumbent carriers; and
- route service possibilities to and from points beyond the Australian gateway(s) or beyond the foreign gateway(s).

Trade Benefits

(c) The extent to which proposals will promote international trade. The Commission should have regard to:

- the availability of frequent, low cost, reliable freight services for Australian exporters and importers.

Competition Policy

(d) The extent to which proposals will contribute to the development of a competitive environment for the provision of international air services. The Commission should have regard to:

- the need to develop strong Australian carriers capable of competing effectively with one another and the airlines of foreign countries;
- the number of Australian carriers using capacity on a particular route and the existing distribution of capacity.

Industry Structure

(e) The extent to which proposals will impact positively on the Australian aviation industry.

Other Criteria

(f) Such other criteria as the Commission considers relevant.

5.2 The Commission is not obliged to apply all the criteria set out in paragraph 5.1 if it is satisfied that the important criteria in the circumstances have been met.

Paragraph 6.1 requirements

6. CRITERIA APPLICABLE IN PARTICULAR CIRCUMSTANCES

Capacity not limited

6.1 In circumstances where capacity is not limited under a bilateral arrangement, only the criteria in paragraph 4 are applicable.

Paragraph 8 requirements

8. RENEWAL OF DETERMINATIONS

8.1 Subject to paragraph 6.1, the criteria for assessing the benefit to the public for the purposes of renewal of determinations, other than interim determinations, are as set out below.

(a) During the start-up phase on the route:

- the start-up phase allocation criteria set out in paragraph 7 apply in relation to that part of the capacity which is reasonably necessary for a level of scheduled international passenger services necessary to permit the development of efficient, commercially sustainable operations; and

- the criteria set out in paragraph 8.2 reflecting a rebuttable presumption in favour of the carrier seeking renewal apply to the balance of the capacity.
- (b) After the start-up phase on the route, the criteria set out in paragraph 8.2 reflecting a rebuttable presumption in favour of the carrier seeking renewal apply.

8.2 Where the rebuttable presumption in favour of the carrier seeking renewal applies, the criteria for assessing benefit to the public are:

- (a) whether the carrier seeking renewal has failed to service the route effectively; and
- (b) whether use of the capacity in whole or in part by another Australian carrier which has applied for that capacity would better serve the public having regard to the criteria set out in paragraph 4 and paragraph 5,

and the Commission should allocate the capacity to the carrier seeking renewal unless both of those criteria are met, in which case all or part of the capacity can be reallocated.