

DECISION

APPLICATION BY QANTAS AIRWAYS LIMITED (ACN 009 661 901) TO CODE SHARE WITH JAPAN AIRLINES ON THE JAPAN ROUTE

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Members:

Russell V Miller
Lonergan
Chairman

Michael L Lawriwsky
Member

Stephen
Member

CONTENTS

	Page
1. The application	3
2. Current services to Japan	3
3. Characteristics of the Australia - Japan route	5
4. Provisions of relevant Air Services Agreements	6
5. Applicant's proposal and claims	7
6. Other submissions.....	7
7. Legislative framework	9
8. Commission's assessment.....	9
Public benefits.....	10
Conclusion.....	17
9. Role of the ACCC	17
10. Other issues	18
Non - compliance with Act	18
Slots	18
Frequencies.....	18
Duration of the code share arrangement.....	19
The code share agreement	20
11. Decision (IASC/DEC/9816).....	20

ATTACHMENTS

A. Legislative framework.....	23
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1. The application

1.1. On 30 July 1998 Qantas Airways Limited ACN 009 661 901 (Qantas) applied to the Commission for a variation of Determinations IASC/DET/9404 and IASC/DET/9804 (the Determinations) allocating capacity on the Japan route to Qantas.

1.2. Qantas is seeking a variation of the Determinations to permit it to provide services jointly with Japan Airlines (JAL), a designated airline of Japan, between Australia and Osaka. The Qantas proposal to code share does not relate to the entire Australia - Japan market, but is restricted to the route between Osaka and Australia.

1.3. On 7 August 1998, the Commission published a notice inviting submissions from any interested persons about the Qantas application. The only submission received by the closing date of 21 August 1998 was from the Australian and International Pilots Association (AIPA) supporting the Qantas application.

1.4. On 18 September 1998 the Commission issued a draft decision and submissions were received from Tropic Isle Retail Stores Pty Ltd (Tropic Isle), the Queensland Government and the Australian Tourist Commission (ATC). None of the submissions opposed the Commission's proposed decision.

1.5. All non-confidential material, including a summary of the proposed code share agreement, supplied by the applicant is filed on the Register of Public Documents. Confidential material supplied by the applicant is filed on the Commission's confidential register.

2. Current services to Japan

2.1. Current services between Australia and Japan are listed in the following table. As indicated in the notes below, some services are operated on a code share basis.

Airline and aircraft type	Weekly Frequency	Route
JAL		
B747	7	Tokyo-Sydney & v.v..
B747	7	Osaka-Brisbane-Sydney-Osaka (Note 1)
B747	7	Tokyo-Brisbane-Tokyo (Note 2)
Qantas		
B747	7	Sydney-Tokyo-Sydney
B747	7	Sydney-Cairns-Nagoya & v.v.
B747	7	Brisbane-Cairns-Tokyo & v.v. (Note 3)
B767	3	Perth-Tokyo-Perth
B767	3	Cairns-Fukuoka-Sydney (Note 4)

B767	2	Cairns-Fukuoka-Cairns-Brisbane (Note 4)
B767	1	Tokyo-Sydney
B767	3	Sydney-Osaka-Brisbane-Sydney
Ansett		
B747	7	Sydney-Osaka-Brisbane-Sydney

All Nippon Airways			
B747	5		Tokyo-Brisbane-Sydney-Tokyo (Note 5)
B767	6		Osaka-Brisbane-Sydney-Osaka

(1) Qantas code shares on three of these services. (2) Qantas code share on these services. (3) JAL code shares 191 sets per flight on the services between Cairns and Tokyo. (4) To be suspended from October 1998. (5) Withdrawn from 1 July 1998.

3. Characteristics of the Australia - Japan route

3.1. In the year ended 30 April 1998 traffic on the Australia - Japan route totalled approximately 1,885,300 passenger movements. Of these passenger movements 85% were passengers with a destination of either Australia or Japan travelling directly between the countries (direct traffic). A total of 7% of movements involved passengers travelling indirectly between the two countries (indirect traffic). The remaining 9% of the movements involved passengers travelling directly between Australia and Japan to and from countries beyond Japan or Australia (beyond traffic).

3.2. Details of the passenger movements on the route between the years ended 30 April 1995 and 30 April 1998 are summarised below.

Table 1: Australia - Japan Passenger Movements for years ended 30 April 1995 to 30 April 1998

Traffic category	Year ended April				Compound annual growth rate 95-98
	1995	1996	1997	1998	
Direct traffic (Annual % change)	1,404,200	1,583,200 (+12.7%)	1,597,500 (+0.9%)	1,596,600 (-0.1%)	(84.7%) 4.4%
Indirect traffic (Annual % change)	150,800	157,400 (+4.4%)	142,200 (-9.7%)	127,200 (-10.5%)	(6.7%) -5.5%
Beyond traffic (Annual % change)	110,700	124,000 (+12.0%)	144,900 (+16.9%)	161,600 (+11.5%)	(8.6%) 13.4%
Total traffic (Annual % change)	1,665,700	1,864,600 (+11.9%)	1,884,700 (+1.1%)	1,885,300 (+0.0%)	(100.0%) 4.2%

Note: Data in this table have been derived from information supplied by the Australian Bureau of Statistics and includes both scheduled and charter traffic. Figures may not add to totals due to rounding.

3.3. In the year ended 30 April 1998, non-Australian residents comprised 93% of the passenger traffic with origin/destination Japan. Visitors to Australia did so mainly for a holiday (89%) or business (4%).

3.4. In the year ended 30 April 1998 passenger traffic on the Osaka route grew by around 9%.

3.5. While the Japanese international air travel market has softened in the wake of a stagnant domestic economy, the Osaka route, being newer, has held up well compared with the more mature Tokyo route. However, the Osaka region has an industrial base which is susceptible to economic downturn and indications are that international travel is likely to slow over the next scheduling season. Substantial increases in aircraft capacity on the Osaka sector over 1997 as a result of the introduction of new services by Ansett International Limited (Ansett International) and All Nippon Airways (ANA) have widened the gap between passenger demand and aircraft capacity which is unlikely to be narrowed in the short term by passenger traffic growth.

4. Provisions of relevant Air Services Agreements

4.1. The Memorandum of Understanding of 9 December 1992 (1992 MOU) and the Australia - Japan Air Services Agreement of 19 January 1956 provide for the multiple designation of Australian carriers. The 1992 MOU also enables the designated airlines of both countries to operate joint passenger, freight and/or mixed services between Japan and Australia subject to the conclusion of a commercial agreement or agreements between the designated airlines of the two countries which have been approved by the respective aeronautical authorities.

4.2. A further Memorandum of Understanding was agreed on 20 December 1996 (1996 MOU) which increased the total capacity entitlement of each country to 77.0 units from 30 March 1997, increasing to 79.0 units from 26 October 1997. One unit equates to the operation of one B767-200 each way per week.

4.3. Qantas currently has an allocation of 60.0 units of capacity and Ansett International 14.0 units, leaving 5.0 units unallocated. On the Japanese side JAL is utilising 42.0 units and ANA 7.2, units leaving 29.8 units unutilised.

4.4. The 1996 MOU also restricts the portion of the total capacity entitlement that may be used by each country between Australia and Kansai airport at Osaka to 21.2 units and 14 frequencies per week. That entitlement is nearly fully utilised by both Australia (Qantas is operating 6.6 units/6 frequencies and Ansett International 14.0 units/7 frequencies) and Japan (JAL is utilising 14.0 units/7 frequencies and ANA 7.2 units/6 frequencies).

4.5. While references to joint services in the Australia – Japan air services arrangements are limited to noting that such services are allowed, the Department of Transport and Regional Development has advised in relation to the Qantas proposal that each code share flight, regardless of the number of seats involved, should be seen as utilising one B767-200 unit of capacity and one frequency. This means that Qantas will require seven units of Kansai capacity and seven Kansai frequencies to implement its code share proposal. It currently has an allocation of 7.2 units of such capacity and six frequencies.

5. Applicant's proposal and claims

5.1. Qantas is seeking a variation of the Determinations to enable it to operate services jointly with JAL between Australia and Osaka over the period 1 November 1998 to 31 March 2000. Under the proposal, Qantas would withdraw its three B767 flights per week between Australia and Osaka and market 130 seats on each of seven JAL operated B747 flights.

5.2. Qantas states that it is seeking the variation because it cannot profitably operate its own flights between Osaka and Australia in the face of declines in the Japan outbound market, including from Osaka, and insufficient demand between Osaka and Australia to support the current level of services.

5.3. Qantas describes its code share proposal as a temporary measure, imposed by poor market conditions, which will enable Qantas to maintain a presence on the Osaka – Australia route and increase its services on the route from 6 days per week to a daily frequency.

5.4. Qantas has stated that it will be assessing market developments and its longer term operating plans for the Osaka route over the period of the code share.

6. Other submissions

6.1. A submission was received from the Australian and International Pilots Association (AIPA) which supported the Qantas application, but considered that Qantas should be required to give an indication as to what market level would trigger a return to full Qantas operation in the market. The AIPA suggested a review of arrangements be conducted one year after the approval date.

6.2. On 18 September 1998, the Commission issued Draft Decision IASC/DDEC/9801, proposing to approve the application. Comments

were invited on the Draft Decision by 7 October 1998. Submissions were received from Tropic Isle Retail Stores Pty Ltd (Tropic Isle), the Queensland Government and the Australian Tourist Commission (ATC).

6.3. The Commission noted that Tropic Isle has a significant commercial interest in the viability and development of Australia – Japan tourism and trade, particularly in relation to its impact on central and north Queensland.

6.4. Tropic Isle submitted that access to Kansai was critical to any airline seeking to initiate any service between Australia and Japan. The Tropic Isle submission raised a number of concerns about the Qantas proposal, including:

- the effective removal of seven frequencies per week from Australia to Kansai;
- the surrender of valuable Australian slots at Kansai which may not be able to be retrieved; and
- allowing Qantas to retain the allocation but not operate the capacity would be a breach of section 3 and 6(3)(b) of the Act.

6.5. Nevertheless, Tropic Isle stated that “The commercial reality is that Qantas knows its own business best and should be given the opportunity to extend its code share agreement for the period requested.” Tropic Isle supported the AIPA submission and suggested that Qantas should declare its intention to the IASC within one year of the approval date. If it was unable at that time to indicate that it would discard the code share, the IASC should require the surrender of the capacity and frequency and advertise its availability.

6.6. The Queensland Government argued that allowing Qantas to maintain its presence through code sharing while it was unable to operate the Osaka-Australia route profitably would be of benefit to Australia on this potentially lucrative route for Australian tourism. It would also enable Qantas to reallocate the aircraft off the route to a more profitable area, with the tourism and other benefits that this would bring, and leave it better placed to resume services in its own right when the market returned.

6.7. The ATC said Qantas was a significant investor and strategic partner in the ATC’s marketing activities in Japan and that in the Kansai region it invested significantly in ATC brand activities. Qantas was also a major tactical partner with the ATC, investing in marketing campaigns in magazines and newspapers in the Kansai region. The ATC thought that if the code share were not approved, Qantas might reduce its investment in ATC marketing activities. The ATC said that the

Qantas investment in its activities extended the airtime of its TV advertisements and built on the long term positioning of Australia as a tourist destination, which was essential in such a competitive market place.

7. Legislative framework

7.1. The legislative framework for varying determinations made under the *International Air Services Commission Act 1992* (the Act) is set out in Attachment A.

7.2. Carriers to whom a determination allocates capacity may, at any time, apply to the Commission, under section 21 of the Act, for the determination to be varied. Under section 24(1), the Commission must make a decision either confirming the determination or varying the determination as requested in the application.

7.3. Under section 24(2), the Commission must not make a decision varying the determination in a way that varies, or has the effect of varying, an allocation of capacity unless the Commission is satisfied that the allocation, as so varied, would be of benefit to the public.

7.4. In exercising its powers, the Commission must take account of the objects of the Act as set out in section 3 and of the requirement of section 6(3)(b) that the Commission have regard to Australia's international obligations concerning the operation of international air services.

7.5. Section 6(3)(a) also requires the Commission to comply with policy statements made by the Minister under section 11. The current Policy Statement dated 23 April 1997 includes criteria to be applied by the Commission in assessing the benefit to the public of allocations of capacity and of variations to existing determinations.

8. Commission's assessment

8.1. A carrier cannot use allocated capacity by providing services jointly with any other carrier without the prior approval of the Commission. For this purpose, the Commission has previously decided that the provision of services jointly includes *inter alia* code-sharing, seat exchanges, block space arrangements and revenue pooling.

8.2. The Commission will normally determine whether or not an application to code share should be approved utilising the public benefit criteria contained in paragraph 5 of the Policy Statement. This is consistent with the objects set out in section 3 of the Act.

8.3. The Commission's task is to determine whether the Determinations, as varied, would be of benefit to the public. This means that the Commission should decide whether, following the proposed variations, there would at least be the same level of public benefits as before the variations. If not then the application should be rejected. The Commission does not see this as requiring a finding that the variations themselves result in increased benefits.

8.4. However, the Commission must make its assessment having regard to the practical realities of the market in which the applicant is operating and the state of the market at the time that it is making its decision.

8.5. This means that in this case the Commission must compare the position as it exists without approval of this application with the position if the application were approved. As Qantas has decided to discontinue own aircraft services, the Commission must compare the situation when Qantas has capacity on the route, but does not operate any services, against the position where it operates only code share services.

8.6. Although the task of the Commission is to determine the overall effect of the proposal in terms of public benefit, it is convenient to set out the Commission's consideration of public benefit using the structure of paragraph 5 of the Policy Statement. In practice, each element of public benefit impacts on the others and cannot be neatly compartmentalised.

Public benefits

Tourism Benefits

*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).*

8.7. In its application Qantas stated that:

- (i) If the code share is approved, Qantas will be actively promoting and selling on-line daily services between Australia and Osaka. Without the daily code share there would be minimal incentive for Qantas to direct funds and resources to promoting Australia

in the Osaka market. Without the Qantas promotion there would be potentially less Japanese visitor traffic from Osaka.

- (ii) There is no evidence that the current level of Osaka – Australia traffic will increase over the next few years. Accordingly, the capacity on the Osaka route from November 1998 will be able to accommodate anticipated tourism demand.
- (iii) The Qantas aircraft released from the Osaka market will be used in domestic operations and contribute to the carriage of international tourism traffic within Australia.

8.8. The Commission notes the ATC's advice that Qantas provides substantial financial support to the efforts of the ATC to promote Australia as a tourism destination in the Kansai (Osaka) region. The Commission accepts that if Qantas is not present in a market at all, there is little reason for it to promote that market and this could impact negatively on tourism. If the code share were not approved, there is every possibility that the present level of Qantas' financial support for tourism promotion in the Osaka region would not be maintained.

8.9. By moving to code share arrangements, rather than withdrawing completely, Qantas may be more able to respond to the development of the Osaka market through resumption of full services in the event that economic conditions improve in the future. By retaining its own customer base, a marketing role on the route and market intelligence about future prospects, Qantas will be able to better time its resumption of own aircraft operations. The Commission notes that the Queensland Government has expressed a similar view in its submission.

8.10. The Commission takes the view that the proposal is unlikely to deliver any enduring tourism benefits in the form of reduced prices on the route, although Qantas has assured the Commission that the airlines will price and market their services separately.

8.11. The Commission's conclusion, in terms of tourism benefit, is that the level of public benefit if the variation were approved is greater than if it were rejected.

8.12. The position may have been different had there been a submission from another airline expressing an interest in utilising the capacity.

Consumer Benefits

*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).*

8.13. Qantas claims that the code share will enable it to maintain a service for its Australian passengers who will benefit from a daily as against the previous 6 day per week service. Qantas claims that the total amount of capacity operating on the route will be able to accommodate all passengers wishing to travel on the route including the Australian origin market.

8.14. The Commission accepts that there will be some benefit arising from the code share for consumers who wish to fly with Qantas to Osaka (eg frequent fliers) and would not have this opportunity if the code share was not approved.

8.15. The Commission concludes that, in relation to consumer benefit, the level of public benefit if the variation were approved would not be less than if it were rejected, but that the benefit is, in any event, marginal.

Trade Benefits

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.*

8.16. Acknowledging that there will be less direct freight capacity and frequency between Australia and Osaka if Qantas does not resume services with its own aircraft from November 1998, Qantas raises the following points in support of a trade benefit resulting from the proposal:

- (i) Qantas has not been experiencing high cargo load factors on the route;**
- (ii) Qantas customers can tranship freight through Nagoya using Qantas freight services to that city; and**

- (iii) there is ample capacity on other carriers' flights to Osaka to accommodate any increase in the freight market.

8.17. The Commission considers that regardless of the level of cargo involved, Qantas' existing freight customers will be inconvenienced by the Qantas proposals and it cannot be assumed that trans-shipment through Nagoya will prove a practical or economic alternative, especially for fresh produce.

8.18. The Commission notes that even after the proposed withdrawal of the Qantas services there would still be sufficient freight capacity available to meet the anticipated demand.

8.19. As Qantas is, in any event, withdrawing own aircraft services, the Commission concludes that there is no material trade benefit or disbenefit.

Competition Benefits

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.*
- *the extent to which applications are proposing to provide capacity on aircraft they will operate themselves as, in the long term, operation of capacity on own aircraft is likely to result in more competitive outcomes;*
- *the provisions of any commercial agreement between an applicant and another airline affecting services on the route but only to the extent of determining comparative competition benefit between competing proposals;*
- *any determinations made by the Australian Competition and Consumer Commission or the Australian Competition Tribunal in relation to a carrier operating or proposing to operate on all or part of the route; and*
- *any decisions on notifications made by the Australian Competition and Consumer Commission in relation to a carrier operating or proposing to operate on all or part of the route.*

8.20. As the Commission acknowledged in IASC/DEC/9801, the Australian Competition and Consumer Commission (ACCC) is the organisation with primary responsibility for addressing anti-competitive activity. However, the Act makes it clear that fostering competition between international airlines is an important aspect of public benefit and is a matter for this Commission. Furthermore, the nature and the extent of competition impacts directly on consumer benefits, tourism benefits, trade benefits and industry benefits as well as being an important issue in its own right under the Minister's Policy Statement.

8.21. In accordance with the Memorandum of Understanding between the Commission and the ACCC, implemented to minimise duplication between the two bodies, the Commission sought the ACCC's view on the code share proposal. The ACCC made no adverse comment about the proposal.

8.22. As required by the Policy Statement, the Commission has considered whether there are any decisions of the ACCC or the Australian Competition Tribunal in relation to Qantas and JAL. There are no such decisions.

8.23. As stated by the Commission in paragraph 8.30 of IASC/DEC/9801, it is for the ACCC, and not this Commission, to determine whether any commercial arrangements breach the *Trade Practices Act 1974*. It is for this Commission to assess whether commercial arrangements between airlines are likely to increase or reduce public benefit in terms of the *International Air Services Commission Act 1992*.

8.24. One of the Commission's primary obligations under the Act is to consider the extent to which any proposal would contribute to the development of a competitive environment for the provision of international air services. This obligation is reinforced by section 15(2)(e) of the Act.

8.25. It is the Commission's view, as previously stated at paragraph 8.35 in IASC/DEC/9801, that:

- close linkages exist between fostering a competitive environment and achieving the public benefits to which the Act refers;
- competition plays an important role in determining whether public benefits in terms of consumer benefits, tourism benefits, trade benefits and industry benefits, accrue from a commercial agreement for the joint use of capacity;
- the Commission is required by section 15(2)(e) of the Act to include in its determinations a condition stating the extent (if

any) to which carriers may use allocated capacity by providing international air services jointly with another Australian carrier or any other person; and

- the criteria by which the Commission should determine any such conditions are those public benefit criteria to which the Act and Policy Statement make reference.

8.26. Qantas has claimed in relation to competition benefits that:

- the code share will enable Qantas to maintain a presence on the route and exert a competitive influence;
- in the absence of the code share it would be more difficult for Qantas to re-establish its own plane operations to Osaka in the future;
- Ansett International's share of the total seats on the route will increase; and
- the Qantas/Ansett International seat share will increase as a result of the proposal and the two Australian carriers will continue to offer between them the majority of seats on the Osaka route.

8.27. The Commission notes that Qantas and JAL together currently account for 83% of the direct capacity between Australia and Japan compared to the 5% and 12% of ANA and Ansett respectively.

8.28. The significant presence of Qantas and JAL is most pronounced between Narita and Australia where, following the withdrawal of ANA in July this year, they are the only direct carriers. Under the 1996 MOU no further flights may be introduced by Australian carriers to Narita, Japan's main gateway. Qantas and JAL already code share from Brisbane and Cairns to Narita under Decision IASC/DEC/9608.

8.29. The combined market share of Qantas and JAL is less pronounced on the Osaka route where there are four carriers. Together they currently hold 47% of the capacity to and from Osaka, which will decline to 40% following the withdrawal of Qantas operated services from 1 November 1998.

8.30. It would be difficult to interpret the proposed code share as anything but a strengthening of the relationship between the two largest carriers on the Australia - Japan route.

8.31. In IASC/DEC/9801 the Commission stated (at paragraph 8.44) that there must always be concerns, in terms of the potential effect on competition and therefore the development of a competitive

environment, when two major airlines on a route seek to code share. The Commission considered in that case, that because the proposal was of limited duration, the potential longer term effects on competition were of less concern. The code share arrangements between Qantas and JAL have been expanding in terms of both time and capacity and, accordingly, there must be increased concern about the potential impact of this proposal on the competitive environment.

8.32. At the same time the Commission notes that no submission opposing this application on competition grounds has been made by the other Australian airline operating on the route, or any other interested party.

8.33. A particular concern in relation to code share arrangements is that the carriers involved might not price or sell their capacity independently, or might pool revenue. As the Commission stated in Decision IASC/DEC/9608 the Commission would be unlikely to approve a code share agreement where either of those factors were present (absent ACCC authorisation) as the Commission believes that this would inhibit competition. In this case, however, Qantas has assured the Commission that the carriers will not pool revenue and that the code share participants will price and sell their capacity independently. The Commission has noted provisions to this effect in the proposed code share agreement.

8.34. The Commission considers that while the proposal is unlikely to enhance competition, the code share between Qantas and JAL, at a time of poor market outlook for the Osaka route, retains an additional competitor in the short term who has expressed an intention to withdraw completely in the absence of approval of the code share proposal.

Industry Structure

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

8.35. Qantas claims in relation to benefits for the Australian aviation industry that:

- (i) the capacity used by Qantas for the code share would not otherwise be used, i.e. no Australian carrier is being denied access to the capacity;
- (ii) there will be improvements in Qantas' financial performance from the code share proposal; and

- (iii) the proposal can be expected to result in higher seat factors for all carriers operating on the Osaka route, including Ansett International.

8.36. Whether or not any other carrier would express interest in the capacity being used by Qantas could strictly only be tested through inviting expressions of interest in the capacity. Such invitations are not sought in response to an application for a variation to a determination as in this case, although the decision process enables interested parties to foreshadow their interest. No other Australian airline or potential applicant has opposed the application.

8.37. The Commission agrees with Qantas that the proposed code share would commercially benefit Qantas through revenue from the sale of code share seats and reduced costs.

8.38. The Commission does not have sufficient information available to it to come to any conclusions about the possible impact of the proposal on other carriers on the route, including whether it would result in higher seat factors for Ansett International, as claimed by Qantas.

8.39. The Commission agrees with the view expressed in the AIPA submission that there is no benefit to the Australian aviation industry in requiring an Australian airline to operate on a route which is not profitable. Similar views have been expressed by the Queensland Government. Given Qantas' stated decision to withdraw its aircraft from the Osaka route, whether or not the code share is approved, there is no suggestion that Qantas could be required to maintain unprofitable operations.

8.40. On balance the Commission concludes that, in terms of its impact on the Australian aviation industry, approval of the proposal would be likely to impact positively due to the increased flexibility of operations it would provide to Qantas in the current difficult marketing conditions. Industry benefits would not be reduced by approving the application.

Conclusion

8.41. The Commission concludes that, on balance, it should approve the Qantas proposal.

9. Role of the ACCC

9.1. Nothing in the Commission's decision should be taken as indicating either approval or disapproval by the ACCC. The

Commission's decision is made without prejudicing, in any way, possible future consideration by the ACCC of the code share agreement or operations under it.

10. Other issues

Non – compliance with Act

10.1. Tropic Isle submitted that allowing Qantas to retain the allocation but not operate the capacity would be a breach of sections 3 and 6(3)(b) of the Act. Section 3 sets out the objectives which the Commission seeks to achieve in allocating capacity. Section 6(3)(b) requires the Commission to have regard to Australia's international obligations concerning the operation of international air services.

10.2. As the Commission understands it, Tropic Isle is concerned that, if the application were approved, seven Australian frequencies at Kansai would only be used in a theoretical sense because Qantas would no longer be actually operating services. Although the Commission shares Tropic Isle's concern to ensure that Australia's capacity entitlements are used to the best practical effect, it rejects the submission that approval of this application amounts to a breach of the Act. Further, the concern expressed by Tropic Isle is not an overwhelming reason for rejecting this application.

Slots

10.3. Tropic Isle submitted that, once surrendered, valuable Australian slots at Kansai may not be able to be retrieved. This submission does not take account of the fact that Qantas has decided to withdraw services regardless of the outcome of this application. The slots would be lost whether or not this application is approved.

Frequencies

10.4. Under the Australia – Japan air services arrangements Qantas requires seven frequencies per week at Kansai to implement code shares on daily JAL operated services, but only currently has an allocation of six frequencies (six under IASC/DET/9804 and none under IASC/DET/9404).

10.5. Qantas has sought a variation of IASC/DET/9404 to provide one Kansai frequency per week. Paragraph 6.3 of the Policy Statement allows the Commission to provide minor increases in capacity by way of a variation to a determination. The Commission will make this minor allocation of capacity to enable Qantas to implement its code share with

JAL.

10.6. Qantas has also sought a variation to IASC/DET9404 to remove a condition that Qantas must:

- *operate the capacity allocated by this determination on the basis that the total number of frequencies operated by Qantas from Australia to Kansai does not exceed 6 per week (being the number specified in Determination IASC/DET/9309);*

10.7. Without the removal of this condition Qantas would not be able to offer seven services per week on JAL flights. The Commission will remove this condition from IASC/DET/9404.

10.8. The Commission notes that IASC/DET/9404 expires on 5 December 1999.

Duration of the code share arrangement

10.9. Qantas has sought approval for the code share to be approved for the period from 1 November 1998 to 31 March 2000. Such an approval would involve three Northern season scheduling periods.

10.10. The Commission is concerned at the potential impact of the proposed joint services between two major players on the Japan route over an extended period, given the uncertainties in this market over an extended period and the impact that developments such as the withdrawal of additional capacity or carriers could have on the competitive environment in that market.

10.11. The Commission considered whether it should approve the code share for the 1998/99 Northern Winter scheduling period (from 1 November 1998 to 31 March 1999) by varying the Determinations, and providing for subsequent scheduling periods up to 31 March 2000 to be approved on a scheduling period by scheduling period basis.

10.12. The Commission also considered the proposal by Tropic Isle that Qantas be required to declare its intention within one year of the approval and that if it could not indicate that it would discontinue the code share, the Commission should require the surrender of the capacity and advertise its availability.

10.13. The Commission has decided, on balance, that it will not take either of the proposed courses. If Qantas does not fully utilise the capacity, the allocations will be subject to review. Otherwise, Qantas will need the Commission's approval to extend the code share in relation to capacity covered by IASC/DET/9404 beyond 5 December 1999 because that determination expires on that date. This will provide ample opportunity for the Commission to consider the position.

The code share agreement

10.14. Qantas previously provided the Commission, on a confidential basis, with a code share agreement between Qantas and JAL dated 20 March 1998 covering the route between Australia and Osaka for the period 31 March 1998 to 31 October 1998. On 19 August 1998 Qantas provided the Commission with amendments to that agreement which cover the extension of the term of the agreement, the additional code share frequencies and new seat blocks to apply from 1 November 1998.

10.15. The Commission notes that many elements of the amended agreement relate to operational matters (eg. method of payment) and have no impact on public benefit issues with which the Commission is concerned. The Commission does not wish to restrict the flexibility of the airlines to amend the agreement by stating that every amendment must be approved by the Commission. However, there should be conditions to ensure that the airlines:

- do not pool revenues;
 - price and sell their services on the route independently;
- and
- advise passengers at the time of ticket reservation of the carrier who will actually be operating the flight.

10.16. The Commission notes that while the amended code share agreement is to operate from 1 November 1998 to 31 March 2000, Determination IASC/DET/9404 which is being varied by this decision expires on 5 December 1999. Qantas has requested that the determination renewing IASC/DET/9404 approve the operation of the code share arrangement as requested. The Commission will address this request when it processes the renewal application.

11. Decision (IASC/DEC/9816)

11.1. The Commission, in accordance with section 24(3) of the Act, varies Determination IASC/DET/9404 by:

permitting Qantas to operate services jointly with JAL between Australia and Japan for the period 1 November 1998 to 5 December 1999 as follows:

- 1.0 B767-200 unit of the capacity and one frequency per week at Kansai may be used by Qantas to provide services jointly with Japan Airlines over the period 1 November 1998 to 5

December 1999 in accordance with the code share agreement of 20 March 1998 and amendments to that agreement forwarded to the Commission on 19 August 1998, subject to the following conditions:

- Qantas must price and sell its services on the route independently;
- Qantas must not share or pool revenues; and
- Qantas must take all reasonable steps to ensure that passengers are informed at the time of seat reservation, of the carrier actually operating the flight.

deleting the following condition from paragraph 9.3:

- *operate the capacity allocated by this determination on the basis that the total number of frequencies operated by Qantas from Australia to Kansai does not exceed 6 per week (being the number specified in Determination IASC/DET/9309);*

11.2. In accordance with section 24(3) of the Act, the Commission varied Determination IASC/DET/9804 by:

permitting Qantas to operate services jointly with JAL between Australia and Japan for the period 1 November 1998 to 31 March 2000 as follows:

- 6.0 B767-200 units of the capacity and six frequencies per week at Kansai may be used by Qantas to provide services jointly with Japan Airlines over the period 1 November 1998 to 31 March 2000 in accordance with the code share agreement of 20 March 1998 and amendments to that agreement forwarded to the Commission on 19 August 1998, subject to the following conditions:
 - Qantas must price and sell its services on the route independently;
 - Qantas must not share or pool revenues; and
 - Qantas must take all reasonable steps to ensure that passengers are informed at the time of seat reservation, of the carrier actually operating the flight.

Dated: 16 October 1998

Russell V Miller
Lonergan
Chairman

Michael L Lawriwsky
Member

Stephen
Member

A. Legislative framework

1. Under section 21 of the *International Air Services Commission Act 1992* (the Act) an Australian carrier to whom a determination allocates capacity may at any time apply to the Commission for the determination to be varied.

2. Section 10(2) of the Act requires the Commission to conduct a review of a determination if the Australian carrier to whom the determination allocates capacity applies to the Commission under section 21 for the determination to be varied. Before conducting a review under section 10 the Commission must, by notice, invite submissions about the review of the determination (subsection 22(1)).

3. Section 24 of the Act relates to decisions on applications for variations. Under subsection 24(1), subject to this section, the Commission must, having conducted a review to decide an application for a determination to be varied, make a decision:

(a) confirming the determination; or

(b) varying the determination in a way that gives effect to the variation requested in the application.

4. Section 24(2) of the Act states the Commission must not make a decision varying the determination in a way that varies, or has effect of varying, an allocation of capacity unless the Commission is satisfied that the allocation, as so varied, would be of benefit to the public.

5. In exercising its powers, the Commission must take account of the objects of the Act as set out in section 3 and of the requirement of section 6(3)(b) that the Commission have regard to Australia's international obligations concerning the operation of international air services.

6. Section 6(3)(a) also requires the Commission to comply with policy statements made by the Minister under section 11.

7. The section 11 Policy Statement dated 23 April 1997 includes criteria to be applied by the Commission in assessing the benefit to the public of allocations of capacity.