



23 October 2012

Ms Marlene Tucker  
A/g Executive Director  
International Air Services Commission  
GPO Box 630  
Canberra ACT 2601

Dear Ms Tucker 

### **Application for Renewal - Italy Route**

On 5 October 2012 Virgin Australia lodged a submission to the International Air Services Commission (Commission) in support of their application for an allocation of 300 seats per week on the Italy route.

Qantas submits the following comments in response to Virgin Australia's submission of 5 October 2012 and its claim that the Italy route is in the "start-up phase". In Qantas' view, the "start-up phase" no longer applies to the Italy route. We have therefore not addressed Virgin Australia's claims against the paragraph 7 criteria of the International Air Services Policy Statement dated 19 May 2004 (Policy Statement).

Qantas requests the opportunity to lodge a supplementary submission should our application for renewal be considered on any other basis other than in accordance with paragraph 8.1(b) of the Policy Statement under the provisions which relate to "after the start-up phase on the route".

The "start-up phase" is defined in paragraph 2 of the Policy Statement and refers to the period from which available capacity under a bilateral arrangement may be allocated by the Commission *"until the date on which a determination has been made under the section 7 or 8 of the Act allocating a commercially sustainable level of capacity on the route to a new entrant"*.

The allocation of capacity to Ansett International Limited (Ansett) is in accordance with the Policy Statement's definition of the "start-up phase" in every respect and, as such, the "start-up phase" on the Italy route has expired. Qantas' application to renew Determination [2007] IASC 113 must therefore be considered under paragraph 8.1(b) of the Policy Statement under the provisions which relate to "after the start-up phase on the route".

On 19 June 2001, the Commission issued Determination [2001] IASC 109 allocating 75 seats of third country code share capacity to Ansett on the Italy route to support plans to serve the Italy market on a code share basis with Singapore Airlines. In



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accordance with the definition of the “start-up phase”, the determination was made under section 7 of the *International Air Services Commission Act 1992* (the Act).

This determination was issued to Ansett as an initial new entrant, at a time when Qantas was operating scheduled international services, having not previously held an allocation of capacity on the Italy route. This fulfils the definition of “new entrant” under paragraph 2 of the Policy Statement, which refers to “*an Australian carrier that has not previously been allocated a commercially sustainable level of capacity in relation to that route*”.

The final element of the “start-up phase” definition is that a “commercially sustainable level of capacity” has been allocated on the route. In paragraph 2 of the Policy Statement a “commercially sustainable level of capacity” is defined as “*the minimum capacity necessary to permit the development of efficient commercially sustainable operations on a route*” (emphasis added). There is sufficient evidence to demonstrate that the allocation of capacity to Ansett is representative of the minimum level of capacity necessary to develop operations on the Italy route.

Virgin Australia’s submission notes that “*on routes where code share capacity is limited under the relevant bilateral, the commercial sustainability of code share services will depend on whether an airline is able to secure an allocation of an amount of capacity sufficient to facilitate the development of efficient and commercially sustainable operations on a route*” (page 7). In June 2001, 1,000 seats of third party code share capacity were available for allocation to Australian carriers under the Australia-Italy air services arrangements. As Ansett was able to request an allocation of more than ten times the amount of capacity it applied for, we can conclude that 75 seats per week represented a “commercially sustainable level of capacity”.

Further supporting that Ansett was allocated a “commercially sustainable level of capacity”, Ansett’s offering was comparable with the frequencies operated by Qantas at the time. Ansett proposed to code share with Singapore Airlines on three weekly services between Singapore and Rome from August 2001 while Qantas was operating four services per week between Australia and Italy, via Bangkok, having increased its service offering to Italy from three weekly frequencies in the prior year.

The existing code share relationship between Ansett and Singapore Airlines enhanced Ansett’s offering on the Italy route, fulfilling the definition of a “commercially sustainable level of capacity”. At the time, Qantas operated services from Sydney and Melbourne to Bangkok and four weekly services between Bangkok and Rome. Ansett, under its Code Share Agreement with Singapore Airlines, was able to offer connectivity from Sydney, Melbourne, Perth and Brisbane to Singapore Airlines’ Rome flights in both directions. At the time, Ansett was code sharing on around 65 Singapore Airlines’ flights per week between Australia and Singapore.

The allocation of 75 seats per week on the Italy route was consistent with Ansett’s offering on another route, further supporting that it represented a “commercially sustainable level of capacity”. In October 2000, Ansett was allocated 75 seats per week on the United Kingdom route by Decision [2000] IASC 215 to enable it to market seats on three weekly Singapore Airlines’ services between Singapore and Manchester. Similar to Ansett’s plans for the Italy route, these three weekly services to Manchester provided connectivity at Singapore from Sydney, Melbourne, Perth and Brisbane.

Virgin Australia submits that assessments of whether an allocation of capacity is commercially sustainable “*can only be properly undertaken after services utilising the capacity have been implemented and operated for a period of time*” (page 3-4). The

definitions of the “start-up phase” and “commercially sustainable level of capacity” under paragraph 2 of the Policy Statement make no reference to the implementation of the capacity, rather, the consideration is regarding the allocation of capacity.

Virgin Australia argues that at the time Ansett was issued a determination on the Italy route, the two references to code share operations in the Policy Statement (paragraphs 3.3 and 3.6) were not present in the previous Minister’s Policy Statement (no. 3 of April 1997) and that *“it may not have been the case in 2001 that a commercially sustainable operation encompassed free sale code share operations”* (page 8). The “start-up phase” refers to an allocation of a “commercially sustainable level of capacity” and “capacity” is defined under the Act as *“an amount of space (however worked out or described) for the carriage of passengers or freight (or both)...permitted under a bilateral arrangement”*. This definition applied in 2001 when Ansett was issued a determination on the Italy route and, as it refers to any amount of space for the carriage of passengers, includes code share capacity irrespective of the particular arrangement. It should also be noted that “code sharing” and “joint international air services” are also defined under the Act and were applicable at the time Ansett was issued Determination [2001] IASC 109.

While we do not intend to address Virgin Australia’s claims against the paragraph 7 criteria of the Policy Statement, we would like to briefly respond to the discussion on the relevance of code share services in 2001 in relation to the application of the “start-up phase”. The relevance of code share services at the time is immaterial to the Commission’s consideration of Qantas’ application for renewal and application of the “start-up phase” however, it is clear that the practice of cooperative marketing was prevalent in the airline industry prior to 2001.

As an example, in addition to its bilateral code share agreements, Ansett had been granted authorisation by the Australian Competition and Consumer Commission (ACCC) in 1998 for an Alliance Agreement with Singapore Airlines and Air New Zealand to provide for the coordination of various aspects of their airline services. In its Determination, the ACCC observed that *“an increasingly popular method for controlling costs and improving profitability is to enter into alliance agreements”* and references statistics from *Airline Business* which *“estimated that there were 502 alliances worldwide involving 196 airlines, including 121 alliances which were established during 1997-98”* (page 16). Further, the three major global airline alliances – oneworld, Star Alliance and SkyTeam – had been established by 2001, having been founded between 1997 and 2000.

Virgin Australia’s submission refers to Qantas’ code share proposition with Cathay Pacific as comprising flights to Milan and Rome however, Qantas currently code shares on Cathay Pacific’s services to Rome only.

We would be pleased to provide any further information the Commission may require in support of this application.

Yours sincerely



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