



Airports Economic Regulatory Authority of India

Consultation Paper No.3 /2010-11

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**PROPOSAL OF AAI TO LEVY USER DEVELOPMENT FEE
(UDF) AT SARDAR VALLABHBHAI PATEL
INTERNATIONAL AIRPORT, AHMEDABAD**

New Delhi: 27th April, 2010

**Rajiv Gandhi Bhawan
Near Safdarjung Airport
New Delhi – 110003**

Subject: PROPOSAL OF AAI TO LEVY USER DEVELOPMENT FEE (UDF) AT SARDAR VALLABHBHAI PATEL INTERNATIONAL AIRPORT, AHMEDABAD

The Airports Authority of India (AAI), is a body constituted under the Airports Authority of India Act, 1994. AAI manages 128 airports including Civil Enclaves. AAI also provides air navigation services over the Indian airspace covering an area of 2.8 million square nautical miles of land mass and the adjoining oceanic area.

2. Sardar Vallabh Bhai Patel International Airport at Ahmedabad, is one of the airports owned and managed by the AAI. The actual annual passenger throughput at this airport during 2008-09 was 28,25,939, which is in excess of 1.5 million passengers per annum (mppa). Hence, Ahmedabad International Airport is a 'major airport' as defined in clause (i) of Section 2 of the Airports Economic Regulatory Authority of India Act, 2008('the Act'). This position has also been stated in the Circular (F.No.AV-24032/03/2009-AAI) dated 12.03.2010 issued by the Ministry of Civil Aviation. As per 2008-09 traffic statistics, the domestic passengers comprised 75.78% of the total passenger throughput. Further, in terms of Sec 13 (1) (b) of the Act, the Authority shall, inter alia, determine the amount of development fees in respect of major airports. Furthermore, Rule 89 of the Aircraft Rules, 1937, provides that the licensee (of an aerodrome) may levy and collect at a major airport the User Development Fee at such rates as may be determined under clause (b) of sub-section (1) of Section 13 of the Act.

3.1 AAI has made an application, on 24.12.2009, to the Authority seeking levy of User Development Fee (UDF), in view of the construction of the New International Terminal Building (NITB), at Ahmedabad Airport. It has been stated that the existing domestic and international terminal buildings have already saturated. With the commissioning of the NITB at Ahmedabad, the peak hour handling capacity would increase from 500 (Arrival 250 & Departure 250) to 1400 (Arrival 600 & Departure 800). The project was approved by the Central Government, at an estimated cost of Rs.290.92 (Phase I Rs.195.92, Phase II Rs.95 crores), vide letter AV.20036/017/2002-AAI dated 09.01.2007 (**Annexure-I**). AAI have stated that the likely completion cost of the project is now estimated at Rs.296.37 crores. It, inter alia, includes the cost of aerobridges, traveller, apron, taxi link, car park and approach road, inter connectivity between the international and domestic terminals etc. AAI had planned that the NITB being constructed under Phase I would be further expanded under Phase II in 2013-14 to meet future traffic growth. However, considering the rapid growth in passenger traffic, the project work under Phase II has been taken up simultaneously with work under Phase I. The NITB will now have an area of 41000 sqmts (Phase I – 27331 sqmts and Phase II – 13669 sqmts) which is an increase of 33616 sqmts as compared to existing international terminal building. AAI have stated that the IRR of the project at the time of approval was 6.2% post tax. Final submissions in respect of the proposal containing requisite details and clarifications were made vide AAI's letters no. AAI/CHQ/REV/AERA/09 dated 12.04.2010 and no. AAI/CHQ/ REV/AERA/UDF/2010 dated 19.04.2010 (**Annexure-II & III**).

3.2 AAI has submitted that the NITB is likely to be commissioned during the month of May,2010 and in order to make the project viable and to attain a reasonable rate of return the levy of UDF is imperative. AAI has proposed to levy and collect UDF @ Rs.270/-per embarking domestic passenger and @ Rs. 1000/- per embarking international passenger for a period of 10 years. Alternately, AAI has proposed a UDF levy @ Rs.150/- per embarking domestic passenger and @ Rs. 755/- per embarking international passenger for a 15 year period.

3.3 It has been clarified that the existing international and domestic terminal buildings are of 7384 sq. mtrs. and 29422 sq. mtrs. area respectively, i.e.; the total terminal floor area works out to 36806 sq. mtrs. After the commissioning of NITB admeasuring 41000 sq. mtrs., the total terminal floor area would become 77806 sq. mtrs., which represents an increase of 111% over the existing terminal area.

4.1 The Authority is, presently, in the process of finalizing its regulatory philosophy and approach in economic regulation of airports and air navigation services. In this connection, a Consultation paper (No.03/2009-10) has been issued on 26.02.2010 wherein the Authority has set out its tentative positions on various issues before it, including in respect of levy of UDF.

4.2 Rule 89 of the Aircraft Rules, 1937 reads as under:
User Development Fee – The licensee may

(a) Levy and collect at a major airport the User Development Fees at such rate as may be determined under clause (b) of sub-section (1) of section 13 of the Airports Economic Regulatory Authority of India Act, 2008;

(b) levy and collect at any other airport the User Development Fees at such rate as the Central Government may specify.

However, no methodology has been prescribed in the Aircraft Rules for determining the UDF. The Concession Agreements for Bangalore International Airport Ltd (BIAL) and Hyderabad International Airport Ltd (HIAL) provide for levy of UDF “from embarking domestic and international passengers, for the provision of passenger amenities, services and facilities” and for the UDF to be “used for the development, management, maintenance, operation and expansion of the facilities at the Airport”. The draft guidelines issued by the Ministry of Civil Aviation noted that levy of UDF was to be considered only in cases and years where the target revenue of a major airport was projected to fall short of the admissible expenditure. Hon’ble High Court of Kerala, in its judgement in the case of Commissioner of Central Excise Vs. Cochin International Airport Ltd. [2009 (16) S.T.R. 401 (Ker.)], has noted that the purpose of UDF “is to augment revenue”. Thus, UDF may be taken as a revenue enhancing measure to ensure economic viability of the airport operations.

5. It is noted that:

(a) The project has an IRR of 6.2%, which is below the benchmark rate of 12% for the public projects.

- (b) The project, including the project cost estimate, has been approved by the Central Government after due consideration.
- (c) The NITB is expected to be commissioned by May'2010. Therefore, a decision regarding levy of UDF needs to be taken immediately.
- (d) The Authority has not yet taken a final position in respect of economic regulation of airports. Therefore, the tariff determination in respect of the Ahmedabad International Airport would take time. In the interim, the revenue enhancement through UDF could be considered, on an ad-hoc basis, as proposed by AAI. In case this is not considered, the target revenue and the loss to be recouped would be higher at the time of tariff determination.

6.1 In the light of the position noted in para 5 above, the submissions made by AAI along with the workings have been examined by the Authority.

6.2 **Return** - AAI have calculated the UDF rate such that the Net Present Value (NPV) of the profit after tax from aeronautical revenues equals the NPV of the expected post tax return on the capital employed. The Targeted Revenue (TR) has been computed as: $TR = (EA + NA) * 12\%$

EA= Value of the existing assets at Ahmedabad Airport

NA= Value of the New Asset

UDF = TR- Projected Revenue.

This appears to be reasonable

6.3 **Regulated Asset Base (RAB)** - For the purpose of arriving at the RAB, the book value of the assets at Ahmedabad Airport as on 31.03.2009 (Rs.130.02 crores) and value of the NITB (Rs.296.37 crores), totaling to Rs. 426.39 crores has been considered.

6.4 **Traffic Projections** – Following traffic projections have been made in respect of passenger traffic and aircraft movements:

Passenger	Domestic	10% in 2010-11 to 2016-17 & 12% thereafter
	International	10% in 2010-11 to 2011-12, 12% in 2012-13 to 2016-17 and 14% thereafter
Aircraft	5.5% in 2010-11	
	8.4% in 2011-12 to 2016-17	
	10.4 % thereafter	

It is noted that the passenger traffic projections are, broadly, in line with the past national trends viz. domestic traffic grew at a CAGR of 13% over the last 8 years; international traffic @ 13.9 % over the last 8 years. The aircraft movement projections are significantly different from the past trend of growth @ 16.5 % over the 8 year period from 2001-02 to 2008-09. Upon a specific query from the Authority, AAI have confirmed that the traffic forecast for Ahmedabad airport has been made based on econometric analysis, regression analysis and trend analysis. Main reasons for difference in projected growth rate in passenger traffic vis-à-vis the aircraft movements have been stated to be as under:

- (i) Historically the growth in aircraft movement has always been lesser than the growth in passenger movements.
- (ii) During the period from April 2009 to January, 2010 all India growth in passenger movement is around 12.9% whereas the growth in aircraft movement is only 1.1%.
- (iii) Because of increasing level of the traffic, the average size of the aircraft will increase whereby more passengers will be accommodated in lesser number of aircrafts.
- (iv) At Ahmedabad airport, 75% of the traffic is domestic. Because of the economic slow down, the capacity utilization of domestic aircrafts in the last year was low and therefore, the increase in the passenger traffic is accommodated partly by increase in the load factor of the existing fleet.

Since the present determination is proposed to be made on an ad-hoc basis, the projections made by AAI are being accepted for the time being subject to review at the final determination stage.

6.5 Revenue

6.5.1 Aeronautical Revenue - The growth rate of aeronautical revenues (landing, housing & parking) and Passenger Service Fee (PSF) are in line with their traffic projections for aircraft and passenger growth. However, no increase in rates of these charges has been contemplated. AAI have not considered any revenue from the Security Component of PSF and have correspondingly excluded the security expenses of the airport from the purview of UDF determination.

6.5.2 No revenues from Route Navigation Facility Charge (RNFC) and Terminal Navigation Landing Charge (TNLC), for incoming flights at Ahmedabad, have been considered and the corresponding expenses attributed to RNFC & TNLC have also been excluded.

6.6 Non-Aeronautical Revenue

6.6.1 Based on the increase in the terminal floor space due to the addition of the NITB, AAI has projected its non-aero revenue from trading concessions, rent and services to be up by nearly 80% in the first year of commissioning, i.e., 2010-11. Thereafter, taking in to account the built-in escalation clauses in its commercial agreements, taking a long term view, 10% growth rate has been considered. For non-aeronautical revenues like car parking, admission tickets, portorage, ground handling etc AAI has assumed a 10% increase over the previous year income while for Cargo revenue the growth rate assumed is 5%. Growth in Throughput Charges have been maintained at the same level as that of aircraft movements growth (i.e., 5.5% in 2010-11, 8.4% in 2011-12 to 2016.17 and 10.4% thereafter. Authority will go deeper into these projections at the time of final tariff determination and based upon its final position in this regard.

6.6.2 However, AAI has not considered any revenue from City Side development at Ahmedabad Airport. It has been stated that *“Ahmedabad airport is among the first lot of 10 airports where city side development has been planned, however no concrete plan has been firmed up and no time frame is available for accrual of revenue on this account. Hence no revenue from it has been considered in the calculations.”*

6.7 Expenditure

6.7.1 **Pay and Allowances** – An increase of 25% in pay & allowances has been assumed in 2010-2011, 8% p.a from FY 2011-2012 to FY 2019-2020, excepting in FY 2017-2018 where the increase is assumed @ 30%. It has been stated that the effect of increments, increase in DA and promotions works out to approximately 8% and increase in staff expenses on commission of new terminal building by 25% takes care of the regular increase as also deployment of manpower commensurate with size and operation of the NITB. The 30% increase in FY 2017-2018 is estimated due to likely revision of pay scales w.e.f. 2017. It is reasonable to assume that the manpower requirement for managing the much bigger NITB would be on a higher side. The quantum of one time increase would require detailed examination at the tariff determination stage. However, the same are being accepted for the time being as AAI have projected an increase of 25% only when the total terminal area has increased by 111%. Other assumptions also appear to be, prima-facie, reasonable.

6.7.2 **Repairs and Maintenance (R&M)** - A 75% increase in R&M expenses in the year of commissioning (over the previous year actual) has been assumed and thereafter at a regular growth rate of 10% pa. AAI have assumed a higher initial expenditure due to increase in terminal building area by 33616 sqmts involving larger area for upkeep, more civil & electrical repairs and inclusion of new equipments & systems under R&M. The projected increase, therefore, appears to be, prima-facie, reasonable subject to detailed examination at the tariff determination stage.

6.7.3 **Electricity & Water Charges** - AAI have assumed an increase of 70% in the electricity and Water charges (based on actual of previous year) in the year of commissioning and thereafter an increase at a flat growth rate of 10% pa. The higher initial expenditure estimated by AAI is due to increase in terminal building area and consequently the increase in air-conditioning expenses, lighting and electrical & electronic equipments. The projected increase, therefore, appears to be, prima-facie, reasonable subject to detailed examination at the tariff determination stage.

6.7.4 **Interest on Borrowings** – AAI have assumed an interest rate of 9% on a loan of Rs.55 crores (in 2009-10) and Rs.10 crores (in 2010-11) with 25% repayment from the financial year 2013-14 onwards. However, the same is only based on the action plan of AAI and the actual amount of loan and the interest rate may vary. In view of this uncertainty, the cost of debt cannot be determined. Hence, the same is not being provisioned for the present.

6.7.5 Other miscellaneous expenditure - AAI have not given any break-up of the miscellaneous expenditure. They have assumed an increase of 25% in the miscellaneous expenditure in the year of commissioning (over the previous year actual) and thereafter at a regular growth rate of 10% pa. Considering the large increase in the size of the NITB, these assumptions appear to be, prima-facie, acceptable subject to detailed examination at a later stage.

6.7.6 Apportionment of Corporate Head Quarters (CHQ)/Regional Head Quarters RHQ Expenses - AAI have assumed a uniform growth rate of 7.5% pa except in 2017-18 where a rate of 12% is considered. The expenses of CHQ & RHQ have been apportioned over the airports based on the number of employees, which is as per the existing accounting policy of AAI.

6.7.7 Depreciation – The depreciation rate applied by AAI is as per AAI's approved accounting policy considering the useful life of the assets. However, in the instant proposal, AAI has considered depreciation on straight line method at weighted average rate of 10% on the entire RAB (, i.e., existing + new assets) and has claimed depreciation from 2009-10 on the new asset in their calculations. In the Consultation paper (No.03/2009-10) the Authority has stated that it will adopt a capitalised financing approach, which will ensure that users do not have to pay for assets until they have been commissioned and are in use. Hence, the UDF needs to be reworked to capture depreciation from FY 2010-11 onwards for the new asset, i.e., the NITB.

6.8 Weighted Average Cost of Capital (WACC) - AAI have assumed a post-tax nominal WACC of 12% which is the bench mark rate for public projects. Authority at this stage refrains from commenting on this benchmark rate since this exercise is for ad-hoc determination of UDF. Tentative position of the Authority in regard to fair rate of return and determination of WACC is put forth in the Consultation Paper dated 26.02.2010 referred to above.

6.9 Till – AAI have assumed hybrid till with 30% non aeronautical revenue being considered for the UDF determination. However, the Authority in its Consultation paper (No.03/2009-10, issued on 26.02.2010) has tentatively decided to adopt “Single Till” approach. Thus, the “Single Till” approach is being adopted in the present case.

6.10 Corporate Tax – AAI have considered corporate tax rate @ 33.99%, i.e., standard rate.

6.11 Discount rate – AAI have adopted a discount @ 12% to determine the NPV of Target Revenue. Considering that the WACC is being taken @ 12%, the Authority may, for the present, take the discount at the same rate as the WACC rate.

6.12 Service Tax – AAI have considered the levy of Service Tax on the UDF and have proposed the rates inclusive of Service Tax. Authority is conscious of the fact that in the case of Commissioner of Central Excise Vs. Cochin International Airport Ltd. (Supra), the Honble High Court of Kerala has held that Service Tax is not leviable on UDF. However, this is an issue to be decided by the relevant tax

authorities based upon the laws of the land. Therefore, UDF rates have been worked out exclusive of Service Tax. In case the same is held to be leviable, the incidence of such tax would be a pass through.

6.13 AAI have stated that the new international terminal is nearing completion and is now expected to be commissioned during the month of May, 2010. They have submitted that the new terminal was envisaged to be used as International terminal building. However, it is now proposed to be used as Domestic Terminal and the existing domestic terminal would be used as International Terminal. The usage of existing international terminal after commissioning of new terminal building has not yet been firmed up.

6.14 To Summarise:

- (i) AAI's projections in respect of traffic (passenger & Aircraft movements), aeronautical revenue, expenditure (except interest on borrowings) are proposed to be accepted, for the present, subject to detailed examination at the final determination stage.
- (ii) The cost of borrowings is not being considered for the time being for reasons explained in para 6.7.4 above.
- (iii) AAI has assumed a WACC of 12%, which is the same as benchmark rate for public projects. Discount rate is proposed at the same rate as the WACC.
- (iv) Single Till is being adopted as against the 30% hybrid till proposed by AAI.
- (v) Corporate tax is considered at the standard rate. Further, UDF rates are calculated net of Service Tax, if any.

7.1 Keeping in view the position explained above, the proposal has been reworked for a 10 year period and 15 year period, respectively, as under **(Annexure-IV & V)**:

UDF per embarking Passenger	Domestic	International
Net for 10 year period (Rs)	Rs 111/- (say Rs.110/-)	Rs 411/- (say Rs.415/-)
Net for 15 year period (Rs)	Rs40/-	Rs199/-

7.2.1 It is observed that in terms of Section 13 (2) of the Act, the tariff determination is to be made on a quinquennial basis. Therefore, it is for consideration whether UDF determination could be made for a 10 year or 15 year period.

7.2.2 In a similar proposal relating to levy of UDF at the Trivandrum International Airport, the Authority had observed that:

- (a) UDF is considered a measure of revenue enhancement. From this perspective, the UDF may be determined for a five year time,

recognizing the fact that in the second tariff cycle, UDF will need to be reworked based on the experience of first regulatory cycle and future projections/forecasts for the subsequent ones.

- (b) Balancing the interest of passengers (i.e., keeping the charges as low as possible) and the viability of the project, the UDF rates could be considered on the basis of figures for 10 years period.

The Consultation Paper No. 05/2009-10 issued by the Authority on 26.03.2010 refers, in this regard.

8. In view of the above, the Authority proposes to approve the levy of UDF at the SVP International Airport, Ahmedabad @ Rs. 110/- per embarking domestic passenger and @ Rs. 415/- per embarking international passenger (exclusive of statutory levies, if any) purely on ad-hoc basis, with effect from the date of commissioning of the New Terminal Building, based on the figures for a period of 10 years. This ad-hoc determination would be reviewed at the stage of tariff determination for the first cycle and thereafter at such intervals as the Authority may decide.

9. The Authority solicits feedback, comments and suggestions from stakeholders on the proposal contained in para 8 above. Comments/submissions may please be furnished to the Authority, **latest by Tuesday, the 11th May, 2010** at the following address:

Shri Sandeep Prakash,
Secretary,
Airports Economic Regulatory Authority of India,
Room No. 58, Rajiv Gandhi Bhawan,
New Delhi.
Tel: 011-24616025
Fax: 011-24656214
Email: sandeep.moca@nic.in
sandeep.prakash@aera.gov.in

Yashwant S. Bhave
Chairperson