

APPLYING SPECTRUM PRICING TO THE AERONAUTICAL SECTOR

DRAFT #3

INTRODUCTION

1.0. It is disappointing that you have decided to consult once again on applying AIP to aeronautical spectrum. Because it was so complicated and potentially damaging to aviation we had to expend considerable resources on dealing with the previous consultation. It was clear then that AIP would not improve efficiency and it would have been outside your authority to impose. This consultation is equally complex, introducing as it does additional report material and setting out a somewhat different logic. Nonetheless many of the issues we raised last time still stand.

1.2. The fundamental proposition you put forward now is that there is excess demand for aeronautical VHF spectrum and AIP will cause it to be managed more effectively by allocating it to those who value it most thereby maximising the benefit to society. For AIP to be relevant there must be excess demand and an alternative use; the spectrum must be managed more effectively as a result and value to society must be maximised. Our response is built around these propositions looking in turn at excess demand, alternative use, effective management and value to society. We then examine some of your data before summarising our position but we begin by considering the overarching requirement for safety in aviation.

SAFETY

2.0. Before we examine your proposition it is important to understand the safety issues which you acknowledge but either argue or dismiss in the consultation. Aviation safety is not a single definable product which can be shown to be present or absent, rather it is made up of many small components of which communications is but one. However, communication is an enabling factor in the majority of safety areas and is therefore very important, particularly in commercial operations. When proposing to change something in aviation, we need to carry out a cost and safety benefit analysis and consider if safety will be maintained, improved or reduced and at what price. Generally, Society will not tolerate a change which trades safety for revenue and this is recognised in the historic way we have managed aviation regulation: if a proposed change cannot be shown to increase safety or at least be safety neutral, it is not taken forward. This conservative approach has served the Industry well for many years and as VHF com is the key to safety and regularity in civil aviation, Society will demand that any change that may be made to spectrum management should not reduce safety. You now propose to force a change that would increase revenue for the benefit of Society (which Society as individuals would have to pay for) but which had the potential to make flying less safe to the extent that you expect the CAA to introduce secondary legislation to stop any changes that result. This does not appear to a sound safety case which Society should support.

2.1. You open the consultation with the example of the emergency services which pay AIP to use business radio and liken them to aviation implying that it too should pay. However this comparison is not valid as the safety considerations are fundamentally different:

2.2.1. If an ambulance is dispatched without access to radio communications it may not be able to carry out its function as effectively but the ambulance itself is no less safe as it travels through the busy streets of a city.

2.2.2. However an aircraft travelling through similarly busy airspace over that same city but unable to use its radio is, of itself, an increased risk to life and property; indeed to society.

There are circumstances where aeronautical radio communications are appropriate and the CAA manages that to ensure a proper balance of safety throughout aviation. But your AIP proposal would remove that safety management function from the CAA and give it up to market forces because that "will have a beneficial impact on the economy". We do not find that argument at all persuasive.

SUPPLY AND DEMAND

3.0. You note that in para 7.67 that where the supply of spectrum is sufficient to meet demand, there is little to be gained in efficiency terms from setting fees other than to recover some or all of your relevant administrative costs. Throughout your document you refer to existing excess demand and a shortage of aeronautical spectrum leading to opportunity costs (eg para 1.9). By frequent repetition this statement seems to gain some authority but nowhere, either in your document, in its supporting reports or in previous studies such as the Cave reports, is this excess demand quantified. You say in referring to those reports (5.28) that "the preceding evidence demonstrates excess demand" but it does no such thing. Cave merely says that congestion exists and this mantra is repeated down the chain. Your sub-contractor Indepen says for example, that the twice yearly regional planning meeting is evidence of congestion when it is actually evidence of complexity not congestion.

3.1. To address this properly we asked the CAA how many unfulfilled VHF assignment requests currently existed in the UK and they said there were none. We are certain you know this already. At the time of writing there is, de facto, no excess demand whatsoever.

3.2. When we put this to you at a meeting between Ofcom and the LAA, you said that you rely on the Helios report, which includes a map representing what it calls the density of UK assignments by area (page 20) to demonstrate excess demand and congestion. First of all, Helios is not an independent analyst, it is your subcontractor employed to support your proposals and you must bear the responsibility for anything you draw from its report. Their approach demonstrates a fundamental misunderstanding about aeronautical spectrum distribution or if it is not misunderstood then it is misrepresented. Because of the absolute need to prevent interference there are rules for repeat assignment which you explain and which Helios lists. The map actually represents areas

where frequencies cannot be reused because of these rules and it is most dense in the south-east of the UK due to assignments in mainland Europe. It is in no way connected with demand in the UK which is the whole basis of your proposition. If European assignments are removed from this depiction then it becomes clear that UK use of aeronautical spectrum is very modest. It cannot be called congested and there is clearly no excess demand. What Helios depicts and you use as the basis for this proposal is an illustration of the impact on the UK of spectrum use in Europe but that is not what you propose to address. This is a contrived methodology to provide you with basis for your proposal to introduce AIP but it is fatally flawed.

3.4. We agree that because of the way Europe manages its air traffic systems there is significant spectrum use there which, by international agreement, leaves but part of the spectrum available for use in the UK. As we shall demonstrate, applying a control on spectrum use in the UK merely transfers allocation back to Europe which will have no impact on the density depicted on the map and will gain us nothing. In fact it would cause a net loss of spectrum to the UK.

3.5. You make specific mention of aeronautical band congestion and Professor Cave used the same term but it is being misused by both of you in the aviation context. Congestion is something that arises when the level of communications traffic prevents or delays messages being passed. You have used the term congestion to describe the situation where almost all the channels available in the band are taken up and you aver that this is unsatisfactory. In fact aeronautical channels have very low utilisation (and therefore low congestion) and the whole band has an overall very low utilisation over time; congestion is very rare indeed. Because failure to pass a message can be a significant safety risk for aircraft, Industry and the Regulator seek to minimise congestion and this is done by utilising as many available channels as possible to separate functions. Thus your objective of reducing what you call congestion would have the reverse effect and a reduced number of channels would increase the risk of congestion with the concomitant increase in risk to the travelling public and to citizens generally.

3.6. Further, at your meeting with the LAA you introduced your concept of "hidden excess demand" to show that there is excess demand even though we could not find any unfulfilled assignments. You explained that potential new users might not declare their requirement publicly because they know there is no availability and you drew on experience with seat pricing and load factors in airline ticket sales in the Far East to evidence that concept. Translated to the current proposition, this suggests that service providers are currently limiting their business aspirations but AIP would somehow resolve that and expose new demand. However, aviation infrastructure is well defined and there are no "new potential users" who may suddenly come into the market with new airports or new air routes. Airports are not built speculatively and the air route structure is not open to competition. Moreover the number of VHF channels required for aviation is very stable and does not respond directly to changes in public demand. The number of channels needed at an airport is largely set by the configuration of the airport and even very significant changes in passenger numbers and aircraft movements do not change that requirement. For example, if a new runway is built for London, it will need a tower frequency and a ground frequency; a modest change in spectrum requirement for an enormous uplift in

capacity. But such changes happen in the very long term and the CAA have told us that such assignments can be dealt with in concert with Europe. Similar considerations also apply to the route structure. Overall we did not find your concept of hidden demand to be at all persuasive; it seems to be an import from a quite different economic situation that is used to try to bolster what is very weak case.

ALTERNATIVE USE

4.0. In the last consultation we argued that international agreements applying to aeronautical spectrum prevented alternate use, the second key requirement for AIP, and therefore AIP should not be applied. It appears that you accepted this at least in part by now proposing that alternative use by other aeronautical users is possible and should be considered. Your paragraph 4.157 recognised this point. However throughout the document you refer to other alternative uses “at the margins” and “in the longer term” when you know that is not a realistic possibility. In the impact assessment (A.8) your consultants say that not applying AIP to the users of aeronautical spectrum will deny its use to other valuable services such as mobile broadband. Of course this is nonsense as you well know that such alternative use will never be allowed by the rest of the World and for the safety of aviation should not be contemplated by you. If, as you argue and some believe, aviation will grow, the spectrum assigned to aviation may well be extended further so reallocation to alternative uses is unrealistic. Moreover, your suggestion that new technologies will enable aviation to forego spectrum for alternative use in the longer term is also flawed because if new technologies reach aviation, which is very slow to move because of worldwide conservative regulation, they will have certainly reached those alternative uses earlier and removed demand there first. Therefore we still maintain that there is no prospect whatever that that AIP will in any way cause spectrum to be released for alternative uses outside aviation and your earlier response appears to accept this.

4.1. We now turn to your statement (4.157) “that it is possible within the existing spectrum use for assignments to be distributed differently if users reduce their requirements”. This sets the new test of alternate use that is necessary before AIP can be applied. It is instructive to consider 2 examples of how such alternative use might be achieved:

4.1.1. In the first assume that a UK approach or upper sector frequency is given up in response to AIP. That frequency does not belong to the UK to reassign because of the interference issue – it belongs to Europe and if the requirement for it is removed it must be given back and may be reassigned to a user in another country. It is true that the UK could bid for it on behalf of a potential UK aeronautical user on the same basis as other nations but there are many more of them than there are of us so the probability of it coming back to the UK is much less than one. So in this example AIP causes the spectrum available to the UK to reduce to the disbenefit of UK society. This is an excellent illustration of a fundamental flaw in your proposal on applying AIP to aeronautical spectrum. The World and Europe allocates spectrum through regulation and the UK is an integral and subordinate part of that. There is no UK spectrum market and if you create an artificial one by introducing AIP, there will still be no

market forces because you cannot isolate the traded product from the direct regulation of Europe without withdrawing from international agreements. There can be no UK internal market for this spectrum as it cannot be reassigned in the UK but has to be given back to the European regulatory system. AIP applied as you propose would cause UK society to lose the value it obtains from spectrum.

4.1.2. In a second example, assume that a tower, AFIS or A/G frequency is given up. These frequencies are given to the UK to manage and are used in several places separated by the appropriate protection distance. In all cases the only place that a frequency can be reused is very close to the original site and for its original purpose. Given the quite static nature of UK aviation infrastructure that we described earlier and because of stringent planning restrictions, new airfields do not spring up next to and in competition with existing airfields. So there is a very high probability that any of these frequencies that are given up will remain unused. If there was a potential user for a frequency for the same use, it is extremely unlikely that they could be allocated the available frequency. Therefore there is a significant probability that it would then remain unused in the UK or be reallocated within Europe as part of a general reassignment. This is an example of the second fundamental flaw in your proposal. If you create an artificial market by introducing AIP, there will be no market forces because even where the traded product is under UK control it cannot generally pass from one user to another. Again, UK society will lose the value it obtains from this spectrum.

Returning to paragraph 4.157 in the consultation you assert that “there is scope for assignments to be differently distributed between users and potentially for more assignments to be accommodated if existing users reduce their spectrum requirements”. We have shown that this theory, on which the whole of your proposal appears to be based, does not stand scrutiny. There can be no direct distribution between users. If existing users reduce their spectrum requirements, the number of assignments available to UK society will not increase but will reduce.

EFFECTIVE MANAGEMENT OF AERONAUTICAL SPECTRUM

5.0. Your proposal would move the responsibility for spectrum assignment from the regulator to the end users and in para 1.22 you propose that they are much better informed than the CAA and are also better at assessing safety needs although you offer absolutely no evidence or supporting material to justify your astonishing assertion. We do not subscribe to your view at all. Clearly an end user makes their assessment and judgement based on their own commercial situation and aspirations. They have no knowledge of the needs of others users and even if they did their directors are obliged to act in the best interest of their shareholders. Your desire to move to a capitalist model for spectrum management appears to come from a desire to wrest control from the aviation regulator rather than to ensure that society gains most benefit from aeronautical spectrum. We do not believe that is appropriate behaviour for a public body.

5.1. At the top end of the sector, your studies show an AIP charge of less than a penny per passenger for airlines using main airports so there will be no price

issue for the user to face and even if there was they would be able to pass it down to the passenger. Because of the volume of end charge payers frequencies could be held or additional frequencies taken up with no meaningful penalty to the service provider. Your consultants recognise this in their report concluding the cost in this area would be insignificant so it is clear that AIP would be ineffective in this part of the aviation sector.

5.2. Unlike airlines where some 100 passengers share the per-flight cost of AIP for public transport operations at the sporting, recreational and training end of the sector the pilot is the sole end fee payer. For non-public transport operations a pilot is prevented by law from charging fees to passengers and on average there is only one passenger per flight. AIP charges here will be significant and have a detrimental impact on SMEs which rely on general aviation for their business. Some service providers will have to forego VHF com assignments for compelling business reasons notwithstanding that their operations will be less efficient and less safe. Your consultants propose that the correct policy response to this is for the CAA to enact secondary legislation to force the user to maintain the frequency and pay the AIP fee. Such pre-planned intervention in the market will prevent it operating and cause AIP to be ineffective.

5.3. It is clear that applying market forces will not make spectrum management more effective than management by the Regulator and we can find no evidence in your consultation to support your assertion that it would. However, if AIP were to operate as you intend and spectrum allocations did change to follow market forces, safety would reduce where frequency allocations are given up contrary to the expectations of society. If the CAA legislates to prevent this, no frequency allocations will occur and the charges set will become a tax which is contrary to the law. Society will not benefit in any way from this exercise.

5.4. Quite extraordinarily, you suggest that the UK should lead the World working towards releasing aeronautical spectrum for other uses when the UK has little influence on the World stage and safety and our own national interest demands it should do no such thing.

VALUE TO SOCIETY

6.0. You propose in para 1.7 that AIP would improve the value obtained by society from this spectrum. You go on in 1.8 to say that where a frequency allocation is transferred as a result of AIP "it is reasonable to conclude that the value derived by society is increased". You do not explain how you draw that conclusion and nowhere in the consultation do you define what that value actually comprises. However, in our comments under the heading of Alternative Use we were able to show that transfers of aeronautical spectrum result in a clear net loss to society. So we assert that your unsupported statement is false.

6.1. In para 1.8 you equate the value to society of spectrum to the opportunity cost. As AIP is to be set to reflect that opportunity cost, the value to society which accrues from AIP is therefore the revenue stream. However in para 3.9 you note that in setting AIP you do not take into account the effect of the revenue raised. This is a significant contradiction in your policy as the objective

of AIP is to maximise value obtained and therefore revenue but you cannot take account of it. There is a clear conflict of interest here.

6.2. We then considered what other benefit (or disbenefit) might arise. The total revenue stream is not quantified in the consultation but appears to be in the order of £4 to £7m however you must take no account of that. Beyond revenue, spectrum does not provide any direct value to society; it is the service that is enabled by the use of spectrum that may provide that. In the case of aviation the service that is so enabled and does provides benefit for society is the safety and regularity of aviation in the UK. We discussed that earlier in our response and it applies not only to passengers but also to other airspace users and all citizens in the UK any of whom may suffer the consequences of a safety failure. That this service is applied adequately across all airspace users is a function of the safety oversight and management by the CAA but if you proceed as you propose, that task will be passed to market forces. To be effective, AIP must tend to cause movement in spectrum assignment but you acknowledge that this may have negative safety consequences which would be a disbenefit to society and you suggest that the CAA would need to legislate to prevent that. Putting this into a financial context, current compensation claims for death in aircraft accidents are in the order of £1M to £5M per person so it would only take a very small accident to overtake the £4 to £7m revenues achieved. Once Ofcom overheads are deducted the revenues reaching the Treasury would not exceed the value of a single life.

6.3. You note that you would expect any safety issues to be resolved by the CAA using legislative powers. It was not possible for us to accurately cost such legislative action but it seemed likely that it would be of a similar order to the values described above.

6.4. Having searched your proposal we cannot identify a valid benefit to society. AIP would cause the amount of spectrum available to the UK to reduce and the direct cost of safety disbenefits is likely to exceed revenues.

DATA

7.0 We reviewed the data presented by your contractor and noted a number of anomalies. For example, they appear to have used the published airfield aeronautical information as the source of frequency assignments but have failed to understand its significance. Lasham, a gliding site, requires visiting aircraft to contact the adjacent Farnborough approach but because this frequency is listed by Lasham your contractors have assigned it that approach frequency. RAF Northolt, a busy VIP and business aerodrome has 5 assigned frequencies but your contractors put its total AIP charge as £350. Although we were unable to analyse all the data, there appears to be at least some questionable entries.

OPERATIONS AND MANAGEMENT FREQUENCIES

8.0. Within the aeronautical spectrum, some frequencies are not used for the safety management of aircraft but for commercial messaging through operations rooms and handling agents at airports. You propose to charge these at the lowest rate but these are clearly equivalent to business radio in the way they are used. They are in the aeronautical band for largely historic reasons. In times

past VHF or HF coms were the only means of communicating with aircraft but increasingly other carriers are used. In particular the demise of HF with the closure of Portishead and BA stations has left Stockholm as the only HF ground station close to the UK and driven the change. Similarly an exodus from VHF com for these services could be hastened by AIP and provide benefit to society. There appears to be existing alternative channels for this traffic and it seems reasonable for AIP to be applied to them.

CONCLUSION

9.0. Safety in aviation is an overriding concern of Society and it demands that regulatory changes should not be made unless safety can be shown to be improved or be at least neutral as a result. Your concern is solely with the management of aeronautical spectrum and you have done no safety analysis whatsoever. You say you expect the CAA to regulate to prevent any safety disbenefits but we do not believe Ofcom or its directors can avoid personal liability for the safety consequences of its actions.

9.1 You state that excess demand exists but adduce no evidence to demonstrate this. In fact there is currently no unsatisfied demand for aeronautical spectrum in the UK. Aeronautical spectrum has low utilisation for safety reasons and it cannot be said to be congested. Repetition of a mantra that there is congestion and excess demand does not make it so and is an inadequate basis for the proposal. Your methodology for illustrating the geographic density of assignments in the UK is flawed as it actually shows the impact on the UK of assignments made in Europe but you do not intend to address that issue at all. The UK is assigned only a modest amount of spectrum but nowhere do you illustrate that, perhaps because it is European not the UK use that is the problem. Applying an effective market control on UK spectrum would merely transfer it back to Europe, increasing their share, reducing ours and making no change to your illustration. Your concept of "hidden excess demand" is not valid because spectrum is not a consumer product and there are no ranks of potential users waiting for AIP to be introduced before building new airports or opening new air routes. Thus, the first required test for AIP that there be excess demand fails.

9.4. Your position on alternative use is untenable. There is no possibility that AIP will tend to cause aeronautical spectrum to be released for other purposes such as the mobile broadband you propose. This spectrum is governed by World agreements and standards which you cannot influence effectively. There is also no possibility that alternative use can be made by other aeronautical users because of the way this spectrum is regulated internationally. Spectrum is allocated to the UK sufficient for its requirement and anything given up must be returned to the European pool for reassignment. Where a frequency is managed nationally, it can only be used in its existing location for its existing purpose so the concept of valid alternative use is fictitious. If AIP did cause frequencies to be given up they would be reassigned by Europe or left unused so the benefit to UK Society would be reduced. Thus, the second required test for AIP that there be an alternative use also fails.

9.5 Your assertion that users can manage spectrum better than the regulator is nonsense because users must act in their own interest. This suggests the proposal is based more on wresting control from the CAA than from benefiting Society.

9.6. You recognise that the impact on the airline passenger would be negligible but you do not recognise that this means that AIP would have no impact and be ineffective. You do recognise that the impact in the sport, recreation and training sectors would be very significant but you fail to address the impact on users and SMEs in particular. Where an airfield needs to react to AIP by giving up VHF com you propose that safety should be maintained by the CAA legislating to prevent the change. That would remove any supposed market and make AIP a tax. We therefore conclude that contrary to the requirement for its imposition, AIP set by Ofcom would be less effective at aeronautical spectrum management than the current arrangement implemented by the CAA.

9.7. The value obtained by society from aeronautical spectrum is the safety and regularity of aviation. Spectrum itself has no direct value save the revenue which you propose to raise from AIP. As presented this is a relatively small sum in relation to the value of life. AIP would give remove that element of safety management from the CAA and give it up to market forces driven by the commercial requirements of certain service providers. Such loss of safety would be unacceptable to Society.

9.8. We have found errors in the base data you use to build your proposition.

9.9. We consider that AIP is appropriate for those frequencies used for management purposes by handling agents, airline operations and the like but you have priced these at the minimum scale. We support the proposal to apply AIP to those uses of aeronautical spectrum and believe these should be charged at the full opportunity cost.

10.0. We oppose the remainder of your proposal on the basis that the UK use of aeronautical spectrum is not congested and there is no excess demand. AIP would not release spectrum because surpluses would be taken up by Europe and the density of use over the UK would be unchanged. Use of this spectrum outside aviation is not tenable because of international agreement. As there is no excess demand and no alternative use, the 2 required tests to validate AIP fail. Moreover, the other characteristics required of AIP, that it improves spectrum management and increases the value obtained by Society are also absent in this proposal. We conclude that any charges made by Ofcom for the use of aeronautical spectrum beyond licensing costs would amount to a tax.

LAA

24 Feb 2010