

ARGYLL AIR SERVICES

1.0 SUMMARY

- 1.1.** This paper provides an update on progress with Argyll Air Services with regard to the development of a sustainable Business Plan, associated Implementation Plan and the procurement of future PSO flights and airport management and operations.
- 1.2.** The Council awarded the PSO flight contract to Hebridean Air Services on 16 May 2011. The PSO Contract Model is designed to incentivise the Operator to maximise scheduled timetable delivery and passenger numbers.
- 1.3.** The Council and the Argyll Aero Club signed a Joint Minute of Agreement on 27 April 2011 which resolved all matters between both parties. The Council has resumed the disputed safety area adjacent to the runway and has ensured that no structures, trees or any other objects can be erected, placed or grown in the area of land leased to the AAC which could affect the future operation or licensing of Oban Airport. The resolution of matters between the Council and Argyll Aero Club has allowed the perimeter fence to be removed, which will allow the airport to operate at Category Two (with remission to Category Three).
- 1.4.** On 27th April the Civil Aviation Authority (CAA) confirmed that the Council's proposals for restructuring to meet business needs were acceptable and that the CAA would review the operation of Oban Airport in November 2011.
- 1.5.** On 2nd June 2011, the Council's Executive agreed the following recommendations:

 - The strategic aims and priorities approved by the Council's Executive on 4 November 2010 have been achieved to date. The sustainable financial business model which has been developed following the successful re-tender process, the achievement of mainstream funding within the finance settlement and the revised staffing structure, provides the foundation to achieve the strategic aims and priorities in the future.
 - The Executive agrees to cease successive monthly reporting of Argyll Air Services to the Executive.
- 1.5** On 24 October, responsibility for the management of the Council's Marine and Air Services transferred to Economic Development and Strategic Transportation. The management resource devoted to developing Argyll Air

Services has been augmented and is focussed upon progressing the Council's Strategic Objectives in a more commercially focussed manner.

- 1.6** On 25 November, the CAA concluded its Licensing & Safety Audit. No Category 1 or 2 Non Compliance issues were found for Oban, Coll or Colonsay; a number Category 3 items were identified which have the potential to affect safety which should be considered for remedial action. Overall the CAA Audit Team commented that their audit had found that there had been no reduction in the Council's commitment to air safety over the last 12 months and that they would be recommending to the CAA that Argyll Air Services be now removed from the "Special Attention" designation. The next programmed CAA audit is scheduled for February 2013.

2.0 RECOMMENDATION

- 2.1 The Audit Committee is recommended to note the content of this paper and the progress made over the last 12 months in the management of Argyll Air Services.

3.0 BACKGROUND

- 3.1 The strategic aims and priorities for Argyll Air Services are:-
- Safety in all operations
 - Limit (and over time reduce) the Council's net financial subsidy to the PSO service and the management and operation of the Council's associated airports
 - Increase the utilisation of the Council's airport to generate more income and maximise the socio-economic benefit accruing to our communities from an increase in PSO passenger numbers and General Aviation

4.0 FINANCIAL

- 4.1 The Council's original priority was to ensure that Oban Airport could support the operation of the PSO flights safely at Category One Fire Cover and in accordance with licensing requirements. With the removal of the Argyll Aero Club's perimeter fence, the Council has, with the CAA's approval, restored its capability to utilise the full runway length to accommodate larger aircraft landings (which can generate increased landing fee income and an increase in General Aviation traffic). The competitive tender returns generated from the revised PSO Tender offering allowed the Council to put in place a sustainable staffing structure which can provide Category Two Fire Cover within budget.
- 4.2 The Financial Business Plan is summarised at Appendix 1. The Business Plan estimates a conservative income projection of approximately 5 large aircraft landings per week in 2011/12, rising to approximately 9 large aircraft landings per week in 2013/14. The Business Plan projects a financial surplus over the 3 year duration of the PSO contract. The Airport will require to increase income generation over time to remain sustainable; however, given that the restriction on aircraft size has now been removed, it is not unreasonable to consider that airport income can be increased significantly through a focus upon the development of a coherent marketing and business development plan.

- 4.3 The initial plan to achieve reductions in staffing costs was founded on reducing the staff complement and staffing costs through redundancy. Through liaison with staff and Trade Unions, the saving in staff costs has been realised through managerial redundancy, the part funding of reception staff by the PSO provider, and changes to staff contracts which have reduced working hours in line with budget; rather than through staff redundancy. This can be regarded as a positive outcome for both airport staff and for the Council's operation as the new staffing model preserves the Council's operational staffing capability and capacity and could allow for expansion in due course.
- 4.4 The implementation of these savings was not however completed until later than was first planned (being complete by the end of the 1st Quarter of 2011/12), and consequently, a series of management actions have been put in place to recover this "one off" projected overspend position reported in August. Progress with reducing the projected overspend is reviewed and reported on monthly basis in line with Budget Monitoring, with actions now well in hand to minimise to risk of a Year End Overspend position.

5.0 DEVELOPMENT & INFRASTRUCTURE – RESTRUCTURE OF MARINE & AIRPORTS

- 5.1 The primary focus for Argyll and Bute Council when considering its Marine & Air Services is safety. A further outcome of the Marine & Harbours Service Review conducted in 2011, has been the recognition of the importance its Marine & Air infrastructure assets in terms of supporting communities and the local economy and the requirement to develop a greater depth of management capacity, knowledge and operational resilience than has historically been provided for these services.
- 5.2 On 24 October 2011, line management responsibility for Marine & Air Services transferred from the direct line management by the Executive Director for Development & Infrastructure to the Head of Economic Development Services, who has responsibility for Strategic Transportation. The Council's Strategic Transportation Manager adopted direct line management of Argyll Air Services and will work alongside the Marine Services Manager within a strengthened management structure which provides greater depth of management capacity, knowledge and operational resilience; to both Marine & Air Services.
- 5.3 This change confirms the Council's commitment to resource the development potential of Oban Airport, Coll and Colonsay within the context of achieving its Strategic Objectives and the wider economic development opportunities which are emerging on the West Coast through aquaculture, marine sciences, offshore renewable and marine and air tourism.

6.0 BUSINESS DEVELOPMENT

6.1 Scope for Procurement of Airport Operation/Management – Position

The Council approved the development of tender documentation for the operation/management of its airports in January 2011 on the condition that the Head of Strategic Finance and the Executive Director of Customer Services,

through Legal Services and the Procurement Team, should scrutinise the proposed provision and form of Contract to ensure that the Council's future interests are safeguarded.

It was agreed that this process would follow the completion of the PSO Flight operations procurement process. Until such times as the Council is in a position to appoint a competent external management operator, the Council must ensure that it can continue to operate Oban Airport and the PSO flight service safely, and in accordance with licensing requirements.

The CAA wrote to the Council on 27 April 2011 to confirm that following discussions regarding the Council's restructuring proposals with the Senior Inspectors:-

"It was agreed that the proposals for the restructuring to meet the business needs were acceptable and that we would review the operation at the forthcoming audit in November 2011.

This will give approximately 6 months settling down time and you will be much more aware of how the restructuring is performing.

As you are aware Oban Airport is currently under the 'CAA airports requiring special attention' process and this will remain in place until the review of the operation at the forthcoming audit."

Given the history of Oban airport to date, the CAA wished to be reassured that the Council would continue to manage a safe licensed airport, and therefore a period of time to allow the new arrangements to "settle in" was considered to be prudent, prior to advancing any further changes to airport management and operation.

As part of a soft market testing process undertaken in December 2010, operators indicated a potential interest in an outsourced Airport Management operation on the basis of a joint procurement exercise in conjunction with the PSO. As European "State Aid" provisions prohibited such a procurement approach, following the award of the PSO operation contract, subsequent soft market testing discussions with potentially interested parties has however indicated that there is no interest from competent parties in the external management of the Council's licenced airport operations at this time. The most significant barriers which have been identified are:- the economies of scale, set up costs, limited short-to-medium term income generation potential, TUPE transfer issues, airport licensing and the uncertainty associated with the Airport's recent history and record of inter-party disputes.

As set out within the Executive paper of 10 March 2011, in developing a Procurement Strategy, it is evident, that the historical difficulties which have existed between the Council and Total Logistics Concepts (TLC) are pertinent factors for Third Parties when considering the scope for, and perceived barriers to the viability of an external management operation. While Development & infrastructure Services is committed to systematically resolving all outstanding matters with and between Stakeholders at Oban Airport, in the short to medium term, it is committed to Manage and Operate Argyll Air Services in accordance with the management structure at Section 5.0 at this time.

6.2 Development Actions

In the short term the Service is focussed on developing a Marketing Strategy & Plan which seeks to work with Stakeholders who have a common economic interest in the development of Air Services at Oban in particular and the wider West Coast in general. The Council has held initial tri-partite discussions between the Council, Hebridean Air Services and TLC, to improve lines of communication and with a view to identifying and implementing mutually agreeable improvements to its operation and the perception of Oban as an Airport destination.

An example of the developing working relationship with Hebridean Air Services is the joint application submitted in November 2011 for European funding from the GNSS agency for satellite navigation infrastructure for both Hebridean's Islander PSO aeroplanes and the Council's aerodromes, which has the potential to achieve enhanced reliability of service delivery and improved safety margins for those scheduled service operations between Oban, Coll, and Colonsay Airports in often changeable and challenging weather conditions. This satellite navigation system is fitted to new generation aircraft and is likely to provide an additional marketing feature for visiting aircraft.

In terms of passenger numbers, the new Contract Model that came into being in May 2011 incentivises the PSO operator to maximise the delivery of scheduled services and income from ticket sales (all of which is retained by the operator). This has led to a 12% increase in passengers in comparison to the same 6 month period (May to October) last year. This change in contract structure appears at this early stage to be progressing well with the passenger figures up to October 2011 already surpassing the total passengers carried during 2010 in its entirety.

6.3 Glenforsa Airport

As part of the income review for Argyll Air Services, and in support of the strategic aim of increasing the wider socio-economic benefits which will accrue from increased and more inter-connective air traffic on the West Coast, a tender is currently being prepared for the outsourcing of the management and operation of the Council's "unlicensed" Glenforsa airfield. Air safety is at the heart of this tender however a further objective is the successful procurement of an airfield operator who on a risk and reward basis can successfully increase the number of aircraft movements at Glenforsa and promote Glenforsa either as a destination or as a strategic transport facility which can integrate with the future development of aircraft connectivity on the West Coast of Scotland.

6.4 Marketing Strategy

A marketing strategy for Argyll Air Services has been progressed which identifies three key priorities:-

- Airport Business
 - attract additional activity/business to Oban, Coll & Colonsay airport

- Air Services
 - attract passengers
 - solidify existing service

- pursue new air services
- maximise wider socio-economic benefit
- Perception, Advocacy & Support
- engender improved perception, advocacy & support for Air Services
- inform the community, other stakeholders, funding agencies

Work will continue to be undertaken with key stakeholders to progress the strategy to implementation.

6.5 Marine & Air Services - Future Commercial Management Capability

The following extracts are taken from the Marine Services Service Review 2011 and are equally relevant to Argyll Air Services:-

.....it is intended that due to the unique operation of Argyll Marines Services (income of +£4M) as a business operation, that is highly susceptible to changes in the market place, that Future Challenges Reports are continually reviewed and revised as required on a quarterly basis throughout the year to allow for modifications in the way the Business Development Plan is driven forward.

In line with Marine Services, Argyll Air Services and the associated portfolio of operations and assets, has a strategic role in supporting economic development and growth within Argyll & Bute. There is a requirement to develop new skills and capability within the Service in support of a more commercially driven structure and culture; which will be required to support the Council's wider strategic, economic development and transportation objectives.

In furtherance to the changes to management responsibilities implemented in October 2011, and to progress the ongoing development & delivery of the Business Plan, the Head of Economic Development will undertake a separate Business Development Review Process within 2012-13, which will consider options for further developing the current operating model, staffing resource and commercial growth capability as they apply to both the Council's Marine and Air Services.

7.0 IMPLICATIONS

<i>Policy</i>	<i>As per detail</i>
<i>Finance</i>	<i>As per Detail</i>
<i>Personnel</i>	<i>As per Detail</i>
<i>Legal</i>	<i>As per Detail</i>
<i>Equal Opportunities</i>	<i>As per Detail</i>

8.0 APPENDICES

Appendix 1	Summary Financial Business Plan
Appendix 2	Argyll Air Services Passenger Figures

For further information and clarification contact Executive Director Sandy Mactaggart 01546 604141

Appendix 1

	2011-12 £000s	2012-13 £000s	2013-14 £000s	Total £000s
<i>Original Budget</i>				
Staffing Costs	608	611	623	1,842
Operating Costs	397	397	397	1,191
PSO Costs	515	515	515	1,545
Total Expenditure	1,520	1,523	1,535	4,578
Income	84	87	90	261
Net Expenditure	1,436	1,436	1,445	4,317
<i>Revised Budget</i>				
Manpower Costs	339	341	348	1,028
Operating Costs	356	356	356	1,068
PSO Costs	707	778	800	2,285
Total Expenditure	1,402	1,475	1,504	4,381
Income	25	35	45	105
Net Expenditure	1,377	1,440	1,459	4,276
Difference	59	(4)	(14)	41

Appendix 2 -Argyll Air Services Passenger Figures

Passenger Figures (excluding scholar flights)

Month	2008	2009	2010*	2011**	**The number of passengers utilising the Oban-Islay/Islay-Oban or Colonsay-Islay/Islay-Colonsay flight which is not covered by the PSO (**2011)
January	-	200	100	173	(21)**
February	-	168	145	249	(38)**
March	-	233	-	244	(46)**
April	-	181	86	131	(22)**
May	-	181	88	147	(36)**
June	137	223	189	251	(18)* (53)**
July	137	207	210	212	(51)* (54)**
August	197	206	246	201	(76)* (44)**
September	153	227	221	216	(52)* (51)**
October	189	133	151	210	(24)* (36)**
November	159	137	239		(41)*
December	151	195	151		(21)*
Total	1,123	2,291	1,826	2,034	(283)*