

Air New Zealand Limited

Submission to the Ministry of Economic Development
regarding changes to
the Commerce Act and airport regulation



AIR NEW ZEALAND

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Executive Summary

Air New Zealand (**Air NZ**) welcomes the Government's recently announced commitment to improving the Commerce Act and the quality of the regulatory regime specifically in relation to airports in New Zealand. It is encouraging progress towards a fair, credible regime able to deliver tangible benefits to New Zealand consumers.

While the thrust of the reforms is in the right direction, Air NZ encourages Ministers to bring forward implementation timeframes. The initial timeframes proposed mean consumers will not benefit from the reforms until 2012 at the earliest. There are, however, simple ways that legislation could achieve consumer benefits and investment certainty much sooner.

Current investor interest in Auckland Airport adds an element of urgency to the implementation of the Government's initiatives. It is in everybody's best interests to give effect to the proposed regulatory changes as soon as practicable.

The amending legislation will need to ensure that all markets in which airports have market power are subject to the new information disclosure and price monitoring regimes underpinned by key input methodologies. In this context, historical arbitrary boundaries such as 'aeronautical' and 'non-aeronautical' are unhelpful starting positions as an airport's market power extends across many business operations.

Air NZ has some specific suggestions for legislative drafting that will immediately strengthen the regime proposed for airports. These suggestions include proposals around:

- the threshold for amending the form of control applicable to a controlled company;
- removal of the statutory right for all airports to "set charges as they think fit"; and
- providing greater clarity around the consequences should a controlled airport fail to adhere to the prescribed input methodologies.

The proposed major review of airport regulation in New Zealand is also a welcomed initiative. Because the study is in substitution for a full Commerce Commission inquiry, it may be beneficial for the Commerce Commission to oversee the study. It will also be important that the study's recommendations are able to be acted on in full as if they were the product of a Commission inquiry.

Introduction

1. Air NZ is grateful to Ministers for this opportunity to submit some preliminary comments on the two recently released Cabinet Papers entitled 'Review of Parts 4 and 4A of the Commerce Act' (the **Commerce Act cabinet paper**) and 'Commerce Act Review: Airports' (the **airport cabinet paper**).
2. Air NZ understands that Ministers are interested in submissions on the design details in Appendix B of the Commerce Act cabinet paper which sets out the detailed specifications for an amended Parts 4, 4A and 5 of the Commerce Act (including the four alternative forms of regulatory control).
3. Of particular relevance to Air NZ is the new information disclosure and price monitoring regulatory form of control under the Commerce Act which the Government is proposing to introduce over Auckland, Wellington and Christchurch airports (the **controlled airports**).
4. Air NZ also has an interest in the design details of the negotiate/arbitrate form of regulatory control given that it would appear the most logical alternative form of control which could apply to airports.
5. The airport cabinet paper identifies the potential harm that uncertainty around pricing principles and new regulatory regimes can create, particularly given current overseas investor interest in Auckland Airport. Therefore, Air NZ considers that it is in everybody's best interests to give effect to the proposed regulatory changes as soon as practicable.

Submission Outline

6. In this submission, Air NZ makes the following key points:

I. Implementation timetable

There are clear benefits for all parties (airports, airlines and consumers) in accelerating the implementation timetable. These benefits could be realised at least three years earlier by the amending legislation providing that either airports or airlines could call for negotiations on charges as soon as input methodologies and pricing principles have been finalised.

II. Regulatory Purpose Statement in the Commerce Act

The new proposed wording of a regulatory specific purpose statement remains critical. Ministers ought to be careful to avoid creating additional issues of statutory interpretation able to be exploited by controlled companies to delay the application of regulatory control.

III. Scope of information disclosure and pricing monitoring remains vital

To limit the ability of airports to undermine price monitoring and information disclosure as a new form of control, it will be critical that the amending legislation ensures that all markets where an airport possesses market power are subject to control. The most logical way to do this is to have controlled airports disclose information across all of their business operations with appropriate confidentiality arrangements. In time, the exclusion of some specific markets where competitive forces are shown to exist may become obvious.

IV. Specific legislative drafting issues

Air NZ has identified several issues that may assist in the drafting of amending legislation:

- Information disclosure and price monitoring can be made even more effective by establishing the consequences of a controlled airport failing to apply prescribed input methodologies. In particular, the Commission needs to have the ability to quickly apply a stronger form of control where monopoly pricing is observed and to do so in a way that bypasses the normal thresholds and timeframes.
- For the same reasons that Ministers now accept the need to remove the right for specified airport companies to set charges “as they think fit”, there is an urgent need to remove this reference from the Airport Authorities Act completely.
- In providing for new, but generic, information disclosure and price monitoring obligation powers under the Commerce Act, Ministers will need to ensure that airport-specific issues are adequately provided for.
- Finally, Air NZ provides a preliminary assessment of those consequential amendments needing to be made to the Airport Authorities Act.

V. Further studies into Airport Regulation

Air NZ welcomes the announcement of a major airport study to be conducted by independent consultants. Ministers will need to be careful to ensure such a study is not used by controlled airports to re-litigate cabinet decisions that have now been made in relation to changing the regulatory environment.

Air NZ would encourage Ministers to ensure that the processes surrounding the study and its ultimate recommendations can be implemented as if the study was a full Commission inquiry.

Such an objective also lends itself to the conclusion that it might be most appropriate for the Commission to both set the terms of reference for the airport study and have responsibility for managing the independent consultant appointed.

I. The legislative amendments proposed for controlled airports need to be effective in 2009, not 2012

7. From the airports cabinet paper, Air NZ currently understands the proposed timetable in relation to airports to be:

Date	Cabinet Paper Proposal (indicative timeline)	Air NZ Comments
2008		
Q1	MED to commission an independent consultant study into review of airport regulation	The Commerce Commission's previous sector experience from the 2002 airport inquiry means that it is well placed to establish the terms of reference and brief a suitably independent and experienced consultant to complete the study.
Q2		
Q3	Amending legislation expected to be passed into law (mid-2008) ComCom to commence development of and consultation on airport input methodologies and pricing principles.	The Commission's 2002 Airports Inquiry provides a basis upon which the Commission could immediately begin consultation. Alternatively, the previous experiences of the Commission's 2002 airports inquiry ought to allow for a relatively quick development and codification of input methodologies and pricing principles relevant to airports
Q4	Consultant review into airport regulation due for completion	By concluding the study by the end of 2008, there is time allowed for further legislative refinement in 2009.
2009		
Q1		
Q2	June 2009- Ministry of Transport due to report on study into regulatory issues specific to smaller airports June 2009- Ministers due to report back to Economic Development Committee with recommended changes and outcome of consultant review of airport regulation	These dates could be accelerated to at least Q1 if the consultant study is concluded by the end of 2008.
Q3		
Q4	December 2009 ComCom obliged to have published input methodologies ready and pricing principles to apply to controlled airport Commission to have specified the information	Given the well worn path of pricing methodologies applicable to efficient airport pricing, Air NZ believes this timeframe could easily be

	disclosure requirements and for the information disclosure requirements to take effect immediately.	brought forward into Q1 of 2009.
2010		
Q1		
Q2	30 June 2010 – Wellington Airport due to provide first information disclosure to ComCom	The first reporting dates for the controlled airports could be brought forward 12 months by the Commission publishing disclosure obligations in Q1 of 2009
Q3	30 September 2010- Auckland and Christchurch Airports provide first information disclosure to ComCom	
Q4		
2011		
Q1		
Q2	Wellington Airport second information disclosure	
Q3	Auckland and Christchurch Airports second information disclosure	
Q4		
2012		
Q1		
Q2		
Q3	July 2012 – Auckland and Wellington Airports obliged to have consulted on charges under the current Airport Authorities Act.	Consumers will have waited a further five years to obtain cost reflective pricing.
Q4	Commission undertakes first review after controlled airports set charges as to whether the controlled airports have complied with pricing principles;	To the extent that controlled airports are monopoly pricing, this allows them to continue to charge monopoly prices for 5 years from today.
2013		
Q1		
Q2		
Q3	July 2013 – Christchurch Airport obliged to have consulted on charges under the current Airport Authorities Act.	Consumers will have waited a further six years to obtain cost reflective pricing.
Q4		

8. The most striking feature of the above timetable, is the significant delay between the time the Commerce Commission (**Commission**) is due to have published the input methodologies, pricing principles and information disclosure obligations applicable to the controlled airports and when such innovations may come to impact actual airport pricing. The additional delay of some three years (2009-2012) until when the controlled airports are obliged to re-consult on charges (mid-2012) and/or when the Commission investigates whether a price reset by a controlled airport is in accordance with the input methodologies (late 2012) appears unnecessary and undermines the benefits.
9. Aside from simply prolonging an ineffective regime over some of New Zealand's most important airports, delay in implementation risks sending a message that Ministers are not serious in their intent to resolve to improve the current regime for the benefit of consumers. Delay may also encourage airports to attempt to re-litigate the clear intentions of Ministers as provided in the recently released cabinet papers.
10. There are four key reasons why it is in the interests of all parties (including airports) that the dynamics that such input methodologies and pricing principles can have on airport pricing not be artificially constrained once finalised in 2009:
 - a delay will amount to a further significant transfer of monopoly rent from consumers to controlled airports;
 - a three-year hiatus period over future airport pricing will do little to improve investor certainty and clarity in respect of current investor activity surrounding Auckland Airport;
 - delay drives uncertainty and this benefits nobody. Furthermore, it risks airports being overly cautious in relation to investment during the period; and
 - The 2012, five-yearly reset of airport charges is merely a creature of statute (Airport Authorities Act) that provides a statutory maximum timeframe. The five year cycle in no way amounts to contractual rights which the amending legislation would be overriding.
11. Air NZ encourages Ministers to not artificially constrain the positive effect the new input methodologies and pricing principles promise to bring to consumers by way of efficient airport charges.

Delay until 2012 unnecessarily denies consumers the benefit of pressures able to promote outcomes consistent with a workably competitive market

12. In its earlier submissions, Air NZ identified the real risk of excessive returns by, for example, Auckland Airport. Until such time as the input methodologies and pricing principles apply to airport pricing, consumers can have little confidence that the controlled airports are not making excess monopoly profits. Where excess returns are present, a delay of three years represents a further substantial legislative transfer of economic rent from consumers to the controlled airports.
13. The controlled airports will deny this to be the case, and therefore ought to be confident of their ability to justify airport charges on the basis of both the input methodologies and the pricing principles the Commission will be tasked with

developing. Therefore, there would appear very little to lose, and all to gain, in exposing airport pricing at the first opportunity to the positive initiatives now being proposed by Government.

14. The precedent value of an early application of the input methodologies and pricing principles is also likely to be important and deliver wider consumer benefits. One of the key objectives of developing input methodologies is to guide all parties (both controlled and non-controlled airports) to reach commercial and efficient outcomes.
15. Of course, the greatest guidance can be expected once clarity can be achieved around precisely how the Commission and/or the airports/airlines themselves have applied the methodologies to reach resolution. The earlier such clarity can be achieved, the sooner Air NZ believes all airports (including non-controlled airports) will understand the means to develop efficient pricing. Early clarity, particularly around the asset valuation input methodology (which importantly needs to also expressly address optimisation and the treatment of asset revaluations as part of the input methodology) will also act to limit any further “rush to revalue” by airports.
16. An analogy can be drawn with recent developments in Australia. Ministers may be aware that earlier this year the Australian Government adopted a “line in the sand” approach to airport asset valuation and fixed airport valuations for the purposes of price monitoring. It is no coincidence that within a few months of such an approach being adopted, airlines (both BARA and Qantas) have successfully concluded a commercial agreement for landing charges for Sydney airport.
17. Such an example illustrates the power of a “circuit breaker” approach to long-standing disputes. The earlier definitive statements can deliver certainty and predictability on the most contentious areas of airport pricing, the quicker commercial resolution is likely to follow.

Uncertainty benefits nobody

18. A delay of over three years from the time input methodologies and pricing principles are defined to when they may impact on airport charges will also create considerable uncertainty.
19. An extended period of uncertainty around factors such as asset valuation and how an airport’s regulatory asset base might be optimised for the purpose of applying input methodologies, may mean that airports could be overly cautious in their investment decisions during this period, with potential harm to consumers.

Airport Investor Certainty

20. An extended period of uncertainty is also likely to be unwelcome by any new or potential investors in Auckland Airport. The earlier binding input methodologies can be applied to Auckland Airport’s pricing, the earlier investors can have certainty about what the Commission-developed input methodologies and pricing principles will mean for airport charges at controlled airports. To do otherwise, is to continue to place New Zealand’s reputation as an international investment market at risk.

Five-year cycle breakable

21. Air NZ encourages Ministers to rethink the rationale behind wishing to wait until 2012 to expose controlled airport pricing to more cost reflective disciplines. The 2012 date is simply the product of an arbitrary five year cycle currently embodied in the Airports Authorities Act (**AAA**). There is no magic around such a statutory period. It is simply a maximum period within which particular airports are obliged to consult airline users. It is also a time period that provides considerable scope for forecast figures that are challenging in a cyclical industry.
22. While prices may be “set” for a period of five years, the unilateral declaration by airports in setting prices in no way amounts to a five year contract entered into by airlines. Air NZ would understand the Minister’s reluctance to interfere with contractual relations if airports and airlines had entered into a five year contract. Factually, there are no formal contracts between controlled airport and airlines in respect to pricing, capital programmes and operating expenditures.

There are several ways the amending legislation could seek to apply the input methodologies to airport pricing from 2009, not 2012.

23. For all of the reasons set out above, the earlier the recently announced initiatives can be made relevant to airport pricing the better. It is only once the input methodologies are applicable to the pricing of controlled airports that the regulatory framework can provide pressures able to mimic a workably competitive market.
24. Air NZ has identified three possible ways the amending legislation could provide for input methodologies and pricing principles to apply from 2009:
 - a) upon finalisation of the input methodologies and pricing principles, either party (airports or airlines) could be entitled to call for charges at a controlled airport to be re-consulted on and/or justified in accordance with the applicable methodologies and principles. A statutory timetable of, for example, six months could provide a time limit by when such consultations ought to have been completed. An even shorter timeframe would seem achievable, particularly given that all parties concerned will have already had the opportunity to be involved in the Commission’s work on developing the input methodologies and pricing principles.
 - b) The Commission could be obliged to conduct a study within six months of finalising input methodologies to determine whether current airport pricing complies with the prescribed input methodologies. Again, such a “reality check” would seem entirely appropriate upon the commencement of a new regulatory regime. Where excess pricing was established, this could trigger an obligation similar to (a) above and/or the Commission could provide a pricing range that it believed would be in accordance with the input methodologies and pricing principles.
 - c) The Commission, taking account of the independent study on airports to be completed by the end of 2008, could determine whether it is appropriate for controlled airports to be obliged to re-consult on their charges and make such a determination in conjunction with publishing the final input methodologies and pricing principles.

25. Of these options, Air NZ favours option (a). This option would provide the most certainty for all parties and would seem to involve the quickest possible means to achieve the Government's goal of implementing an effective regulatory oversight regime for controlled airports. It would also be entirely consistent with the Government's objective of encouraging all parties toward commercial and economically efficient outcomes.
26. Finally, it should not be overlooked that what is now being proposed in respect of controlled airports represents the lowest cost form of control. The proposals are unlikely to represent any additional costs as compared with the prolonged consultation exercise that airports and airlines already participate in. In fact, it is likely to result in cost savings as there ought to be considerably less need to litigate disputed factors that will have been addressed upfront as part of the input methodologies.

II. Part 4 Purpose Statement and threshold test

27. Air NZ welcomes the Government's proposal to introduce a purpose statement specifically for Part 4 of the Commerce Act but makes the following comments and suggestions for improvement:

- *Reconciling protection of consumers with economic efficiency:* while both efficiency and consumer protection are included in the purpose statement, it will be for the courts to attempt to rank or reconcile these two factors in particular. Air NZ is concerned that there will continue to exist a high litigation risk over how objectives of economic efficiency and the protection of consumers will be reconciled in the context of regulatory control under the Commerce Act.
- *Incentives to invest:* sub-paragraph (a) of the proposed purpose statement refers to "incentives to innovate and invest". However, in the context of regulatory control, Air NZ submits that it is important that such an objective be expressly linked to the incentives that would exist in a workably competitive market or investment which is efficient. Clearly both under and over investment can be inefficient, so it is important that incentives to invest are explicitly tied to levels reflective of consumer demand.

Test for regulation

28. Air NZ considers that reference to the subjective words "substantial" ("*substantial scope for the exercise of market power*") and "clearly" ("*benefits of regulation ... clearly exceed the costs and risks of regulation*") in the test for whether regulation may be imposed simply detracts from the intent of the test. They are statutory expressions that will be used by regulated companies to challenge decisions of the Commission in an attempt to delay implementation of regulatory regimes. As such, Air NZ would encourage Ministers to remove them from the test for regulation.
29. Similarly, the proposed statement that "*any regulation should be the least intrusive necessary to meet the objectives of the purpose statement*" appears unhelpful and inviting of litigation. In the context of the proposed regime where four alternative forms of control will be permitted, inclusion of such a statement will provide yet another basis for legal challenge to a Commission decision to regulate under Part 5 of the Commerce Act.

III. Input methodologies, information disclosure and price monitoring need to apply to the entire operations of controlled airports

30. In the case of airports, there remains a question as to the appropriate scope of an airport's operations that should be made the subject of the new price monitoring and information disclosure obligations under the Commerce Act.

31. The airport cabinet paper identifies the solution to the threshold question as those markets in which a controlled airport has a "high degree of market power":

"the Commerce Commission monitors airports having regard to the principles it develops and the prices of services supplied in markets where the airports have high degrees of market power"(paragraph 42)

32. Air NZ welcomes this approach. It is a much needed departure from the artificial distinctions previously drawn between "aeronautical" and "non-aeronautical" in respect of an airport's business.

33. Airports possess high degrees of market power in numerous markets across an airport. In fact, airports possess high degrees of market power in all but a few markets in which they operate. There is widespread international acceptance of airports' market power in operations such as carparking, retail space in the terminal, and taxi access to airports. In appendix A, Air NZ sets out those markets in relation to which overseas independent authorities have previously recognised the high degrees of market power that airports possess.

34. Air NZ's earlier submissions attached analysis by PWC that evidenced excess returns across Auckland Airport's business. Returns of approximately 30% on capital would appear strong prima facie evidence of the high market power Auckland Airport possesses over many of its non-aeronautical activities.

35. There exist alternatives in how the various markets an airport operates in could be made the subject of the proposed price monitoring and information disclosure obligations. For example, the amending legislation could provide that price monitoring and information disclosure obligations apply, at least initially, to the entire operations of an airport.¹ This approach has the following advantages:

- It avoids the potential for legal challenge of each individual market definition and assessment of market power (and the clear opportunities for orchestrated delay).
- The Commission will gain an understanding of the controlled airports business operations including the significant economies of scale and scope that exist across an airport's business. It also allows the Commission's work in developing the information disclosure and price monitoring regime to be completed with knowledge of which markets the regime will apply.

¹ Such an "all in" approach could be supplemented with an obligation on the Commission to periodically review the individual markets and, where satisfied of competitive pressures, carve out such markets from future monitoring and disclosure obligations. In such circumstances, it would seem appropriate that the Commission retain the right to re-introduce the price monitoring and information disclosure obligations of these markets should subsequent inappropriate pricing behaviour be detected.

- It avoids the need for an arbitrary distinction to be drawn between parts of an airport's business.
- It avoids the need at the outset to undertake arbitrary cost allocation of common costs (of which there are many in an airport business).
- It would make the task of reconciling financial reported accounts with regulatory accounts simpler.²
- It would eliminate the concern overseas regulators have had regarding the ability of an airport to disguise revenue streams in a regime of price monitoring only parts of a controlled company's business. In Australia, for example, airport operators are reported as having sought to introduce charges for access to aeronautical services and facilities but classified those charges as "non-aeronautical" revenue, thereby concealing this new revenue stream from reporting in the ACCC price monitoring reports.

36. Alternatively, the amending legislation could provide the power for the Commission to examine individual airport markets and determine in which markets airports possess high market power. However, aside from adding to the high workload of the Commission during 2008, Air NZ's main concern with such an alternative is the risk that controlled airports will use the process of individual market analysis by the Commission as a source of delay through legal challenges to what ought to be considered an appropriate market definition and whether an airport possesses substantial market power in that individual market. It is for this reason that Air NZ strongly favours the "all in" option.

² Where issues of confidentiality of information arise and/or where public disclosure of detailed financial information would be problematic for a controlled company, information provided to the Commission could be made the subject of a confidentiality order.

IV. Specific suggestions for legislative drafting able to strengthen the regulatory regime now proposed for airports

37. Air NZ has some specific suggestions for legislative drafting able to strengthen the price monitoring and information disclosure regime now proposed for airports. These suggestions focus on:

- the need for greater clarity around the consequences in the event a controlled airport fails to adhere to the prescribed input methodologies (including the applicable threshold for amending the form of control applicable to a price monitored company);
- removal of the statutory right for any airport to set charges “as they think fit”; and
- appropriately addressing airport specific issues in the context of generic information disclosure and price monitoring obligation powers under the Commerce Act.

Clarity around the consequences of failing to apply input methodologies

38. Air NZ welcomes the acceptance by Ministers that defining binding input methodologies will assist all parties to reach commercial and economically efficient outcomes.

39. The Commerce Act cabinet paper notes that all input methodologies will be “binding”. However, Air NZ is unclear precisely how this is to be given effect and the cabinet appear appears to be silent on specific proposals to ensure that controlled airports will be held to account and apply such input methodologies. As the airport cabinet paper correctly highlights, anything less than binding would merely equate to the situation at present where some controlled airports have repeatedly and openly dismissed the application of methodologies previously applied by the Commerce Commission (including in the most recent pricing reset by the controlled airports).

40. Air NZ considers that the consequences of failing to adhere to input methodologies are critical. To ensure a real threat of stronger control exists, the Commission needs to be provided an ability to efficiently and quickly apply a stronger form of control where monopoly pricing is observed. Analogous to the thresholds regime currently applicable to electricity lines businesses, this ought to bypass the thresholds and timeframes applicable to where control is initially applied to a company.

Time constrained inquiry

41. As Air NZ has previously identified, it is possible for Commission inquiries under Part 4 to be protracted. The process can extend over many years. To avoid such an outcome in circumstances where the Commission’s price monitoring role has revealed the need for an stronger form of control (such as negotiate/arbitrate), Ministers should provide a strict statutory timetable to govern these particular forms of “amending inquiries”.

42. A statutory maximum period, such as 120 days for the Commission to complete such an inquiry, would ensure that the regulatory threat for price monitored businesses remains real.
43. A time limitation of 120 days for a Commission inquiry also seems credible. Unlike inquiries addressing sectors not previously regulated, any inquiry relating to a business that is already the subject of price monitoring, will mean the Commission has access to considerable data and is clearly not required to undertake an all new inquiry.

Reduced Ministerial Discretion

44. Air NZ notes that the Minister of Commerce's involvement in accepting or rejecting a Commission recommendation to amend the form of control exercised over a controlled company is to remain. However, Air NZ considers there to be a case for limiting the exercise of such discretion in circumstances where the Commission is merely recommending a change to the form of control over an already controlled business, rather than implementing control of any kind for the first time.
45. Air NZ notes with interest that there is to be a regime provided to allow the Commission to recommend that trust-owned electricity lines businesses (which will be subject to the new price monitoring and information disclosure regime similar to airports) have the new 'default/customised price-quality path' regime imposed. Air NZ similarly encourages Ministers to provide a parallel ability for the Commission to impose the 'negotiate/arbitrate' form of control for controlled airports under defined circumstances and in a way that avoids the need for a full commission inquiry.

Minimise opportunities for gaming through delay

46. The Commerce Act cabinet paper proposes a new merits-based appeal for finalised input methodologies. Air NZ submits that it will be important to ensure that such an appeal right is matched by a statutory provision that ensures that input methodologies remain binding and applicable to controlled entities even where such input methodologies are subject to merits-based appeal or judicial review. There are precedents for this in other regulatory regimes (e.g. section 60(3) of the Telecommunications Act) where it has proved successful in serving to remove some of the incentives for parties to appeal simply in order to 'game' the process and delay the full application of the input methodologies to pricing.
47. Similarly, Air NZ submits an important and further disincentive against potential gaming by controlled airports would be an express right for the Commission to backdate charges or factor into future pricing where charges are found to not be in accordance with input methodologies or pricing principles.

Legislative amendments need to categorically remove the statutory right for an airport company to set charges "as it thinks fit"

48. Air NZ understands from the airports cabinet paper that as a consequence of moving the pricing regime for controlled airports from the AAA to the Commerce Act, each controlled airport will lose the statutory right to set charges "as it thinks fit". This is a welcome and much-needed improvement.

49. However, from the airport cabinet paper Air NZ remains unclear whether it is also the intention of Ministers to take the opportunity to remove the reference entirely from the AAA.
50. Air NZ encourages Ministers to take the opportunity to remove this statutory reference from the AAA entirely. As Air NZ has previously set out, such a statutory right is unique in the world with respect to natural monopolies and it works to fundamentally undermine the airport charging regime for New Zealand airports. Until such time as the recommendations from the proposed review of airport regulation are implemented, such a provision could be replaced with an obligation on airports to determine and demonstrate cost-based pricing.

There is a need to ensure that generic information disclosure and price monitoring obligations adequately address airport issues

51. Air NZ notes that the price monitoring and information disclosure obligations will initially apply to both the controlled airports and trust-owned electricity lines businesses. While Air NZ supports the goal of ensuring cross-industry consistency for this type of control, Air NZ highlights below some issues which Ministers may wish to consider in relation to airports.

Commission monitoring and reporting

52. Air NZ welcomes the proposal in the Commerce Act cabinet paper that a key part of the information disclosure and price monitoring regime for airports will be a requirement on the Commission to monitor compliance and report on whether further regulation is needed.
53. Air NZ notes with interest recent amendments in the Australian airports price monitoring regime whereby the Government must annually make an explicit judgement on whether the conduct of any of the monitored airports warrant further investigation. The Productivity Commission recommended that the responsible Minister, having assessed the monitoring reports and other relevant information, publicly indicate either that no further investigation of conduct is warranted, or alternatively that one or more airports would be asked to 'show cause' why further investigation into their conduct should not take place.
54. While in the case of the proposed New Zealand regime it would be the Commission responsible for annually making such a public statement, there are obvious merits to a similar regime.
55. The Commission's role in reporting on a controlled airport's compliance with the relevant input methodologies and pricing principles is a particularly important aspect of the proposed regime and Air NZ trusts that Ministers will provide rigorous and timely reporting obligations on the Commission.

Asset Management Plan

56. Controlled airports will be obliged, as part of the information they are required to provide to the Commission, to provide an asset management plan.
57. In the context of price monitoring regimes, asset management plans are typically weak. For example, Air NZ understands that the Commission generally does not comment on the substantive merits of an asset management plan provided in other regulatory contexts.

58. The role of asset management plans would also appear to be linked to the type of asset valuation approach ultimately adopted for airports. For example, in the context of depreciated historic cost (where there is no optimisation performed) agreement of proposed capital expenditure plans with users is likely to become more important. In contrast, in the context of Optimised Depreciated Replacement Cost (ODRC), an asset management plan is likely to be of limited use given that the question of asset optimisation would be specifically addressed on a periodic basis.

59. It would be a valuable development if somehow the requirement on a controlled airport to file an asset management plan could provide the context to require airports to demonstrate user agreement with the planned capital expenditure.

Information to be provided is relevant both before and after airport consultations on charging

60. In the case of airport/airline negotiations, information disclosure and the price monitoring reports to be published by the Commission will clearly be relevant both before and after schedule price consultations. The price monitoring reports of the Commission will obviously assist fully informed negotiations.

61. It should not be assumed that airports will only seek to consult on prices once every five years. Such a timeframe is a maximum timeframe specified in the AAA and market conditions or industry developments may well prompt consultations at intermediate periods, underscoring the importance of regular monitoring and disclosure obligations.

Monitoring of airport service quality

62. The airport cabinet paper is silent on the role of service quality monitoring at airports under the proposed price monitoring and information disclosure form of control. Service quality remains important to airline users of airports, particularly in the absence of progress by the controlled airports to agree service level agreements of the type regarded as commonplace in other industries.

63. The ACCC, as part of its monitoring of major Australia airports, monitors service level qualities. The purpose of this monitoring is to ensure economic efficiency. The ACCC considers that the process and its outcomes act as an important complement to price monitoring. It provides transparency and consistency, and in doing so benefits consumers, airlines, the government and the airports themselves.

64. The ACCC focuses on those facilities and services provided by, or could be influenced by, the airport operator, including: airside facilities such as runways, taxiways and aprons; terminal facilities; carparking; and taxi and bus pick-up and drop-off points. The ACCC draws on information from a variety of sources, including airport operators, airline passengers, airlines and the Australian Customs Service. Some of the key indicators for the ACCC regime include:

- Efficiency in aircraft movement areas
- Terminal crowding
- Waiting times in passenger processing

- Baggage handling areas.
65. We also set out in Appendix B an example of the service quality matters that the UK airport regulator monitors and factors into its regulatory regime.
66. Complying with the service quality monitoring regimes would require the controlled airports to provide data to the Commission. Much of the information to be submitted by the controlled airports is likely to already be collected in the normal course of business – including for internal management purposes, [or for meeting agreed information disclosure obligations to airlines]. While there may be some additional costs around reporting some items in different formats and auditing the information submitted to the Commission, such costs are likely to be insignificant compared to overall revenues for the controlled airports. Adopting the ACCC’s practices would be unlikely to lead to an increased workload on the Commission. The ACCC does not set quality standards, merely monitors them. The ACCC also does not gather information itself. Its role is to evaluate the data provided to it by other parties.
67. Finally in relation to airport service quality, Air NZ notes that while most elements of airport service quality are controlled by airports, there are some elements of quality at an airport that is the source of competitive pressure as between airlines (e.g. premium check-in facilities etc). Air NZ submits that, where an airport unreasonably refuses to supply the inputs able to be used by airlines to differentiate airline service quality at an airport, airlines ought to have a right to invest in the airport infrastructure to the extent necessary to deliver the infrastructure required. Such a dynamic would introduce a competitive force on airports in the provision of airport infrastructure that does not presently exist.

Status of judicial review for pricing decisions of controlled airports

68. Airport decisions to set airport charges under the AAA are currently subject to judicial review. As part of moving the price setting powers of controlled airports from the AAA to the Commerce Act, it will be important to clarify whether airline customers will retain the right to judicial review of the pricing decisions of a controlled airport.
69. The right for airlines to seek judicial review of the pricing decisions of controlled airports should only be removed where airline customers have a clear alternative process to challenge the pricing decision of a controlled airport and where it can be established that the airport has not applied relevant binding input methodologies.

Amendments to the Airport Authorities Act 1966

70. As the airport cabinet paper correctly identifies, control of the controlled airports will require a number of consequential amendments to the Airport Authorities Act 1966 (the **AAA**). Below we identify the principal amendments Air NZ considers will be necessary to give effect to the regulatory changes and to effect those changes proposed elsewhere in this submission:

Definition of a controlled airport

- A controlled airport will need to be defined in the interpretation section (s2). Controlled airports will be a subset of specified airport companies. The

definition could be as simple as referring to those airport companies controlled under Part 5 of the Commerce Act.

Provisions in the AAA that will no longer be applicable to controlled airports

- Provision in the AAA compelling airport companies to disclose current aircraft related charges (s3BA) ought properly to be addressed in the information disclosure regime for controlled airports under the Commerce Act.
- Section 4(1), which relates to the powers of airport authorities in relation to airports and associated operations, ought to be modified to reflect the proposed use of Asset Management Plans under the Commerce Act for controlled airports (and offers the potential to increase transparency, consistency and an enhanced ability for controlled airports to be required to agree proposed capital expenditure plans with airline users).
- Section 4A, which provides the ability for airports to set charges as they think fit. The repeal of this section would remove a long-standing anomaly in New Zealand's airport charging regime. Air NZ acknowledges and welcomes the airport cabinet paper's intention to remove this ability for controlled airports, but encourages the complete repeal of section 4A (i.e. in relation to all airports). A failure to repeal across all airports has the potential to create regional impacts and implications for the level of services available at non-controlled airports.
- Section 4B, which sets out the consultative requirements concerning charges, will need to be brought under the Commerce Act
- Section 4C, which sets out the consultative requirements concerning capital expenditure, will similarly either need to be brought under the Commerce Act or remain in the AAA and applicable to controlled airports. Were such a consultation obligation to remain within the AAA, consideration will need to be given as to how such a requirement ought to reconcile with obligations on a controlled airport to provide an asset management plan under the new information disclosure and price monitoring form of control.
- Section 9A, which allows the Governor General to require information disclosure, should exclude controlled airports. As the Commerce Act will include a complete framework for information disclosure, keeping section 9A in relation to controlled airports would appear unnecessary.
- Finally, there may be limited value in continuing to have section 9C applicable to controlled airports. Section 9C compels airports subject to regulations to disclose information to the Secretary of Transport. Although under the proposed changes controlled airports will not be subject to regulations made under section 9A, there may still be significant benefits from carrying over to the Commerce Act, the obligation of a controlled airport to similarly provide disclosed information to the Secretary of Transport.

V. Independent Airport Study

71. Air NZ welcomes the proposed commissioning by the Ministry of Economic Development of a major independent review of airports in New Zealand, specifically to consider whether:
- I. Additional airports to Auckland, Wellington and Christchurch should be subject to regulation under the Commerce Act; and
 - II. Other forms of regulation should apply to regulated airport companies under the Commerce Act.

Statutory recognition required for independent airport study

72. Air NZ notes that the airport study is in substitution for a full Commerce Commission inquiry into airports (an alternative discounted by Ministers due to resource constraints on the Commission during 2008). As such, it will be important that the completed study is recognised in the amending legislation so as to ensure that its recommendations are comparable to that of a Commission inquiry. In particular:
- On the basis of the conclusions of the independent airport study, the Commission should be able to make a recommendation to the Minister in relation to the extent and scope of airport regulation (and without the need for a further and separate Commission inquiry which would otherwise be required under the Commerce Act).
 - Opportunities, comparable to those that interested parties would enjoy within a Commission inquiry, must be provided for industry engagement. This should include the opportunity for interested parties to submit, cross-submit and share confidential information with the consultant under confidentiality arrangements analogous to a Commission inquiry.

The importance of independence and industry experience

73. The challenge in commissioning such a study will be in finding an independent expert that is knowledgeable in airport regulation with the necessary wide industry background and familiarity. Ideally, the consultant ought to be able to demonstrate prior experience with several international airport regimes.
74. The Commission would appear well placed, given its 2002 airports inquiry, to assist Ministers commission and appoint and help to brief the consultant. The Commission's involvement in the study would also ensure that thinking around the regulation of airports benefited from insights gained by the Commission across the various regulated sectors in New Zealand.

The terms of reference for the study will need to allow for the proposed changes to the Commerce Act

75. The airports cabinet paper recognises that had the Commission been undertaking the study into airports, it could commence the study prior to any amending legislation being passed and then simply transfer it to be under the revised Commerce Act (thereby allowing recommendations to be made on alternative forms of regulation).

76. On the same basis, it will be appropriate to ensure that the terms of reference for the independent study into airports take account of all proposed changes to the Commerce Act. Of particular relevance will be considerations concerning the proposed new purpose statement, emphasis on qualitative rather than quantitative testing, the need to address both 'whether' and 'how' simultaneously, and allowing recommendations to be made on the basis of the proposed alternative forms of regulation.

Need to consider how best to consolidate charging regimes by New Zealand airports

77. Air NZ recommends that the terms of reference for the independent airport study should expressly include a desire to consolidate the different applicable charging regimes for New Zealand airports. With the addition of the new regime proposed for controlled airports under the Commerce Act, four different regimes will govern airport charging in New Zealand (three under the AAA).
78. The need for four separate regimes in a country the size of New Zealand is highly questionable. Air NZ would welcome any move to consolidate and simplify the alternative arrangements and categorisation of airports by virtue of ownership structure.

Timing of MoT study

79. As it is proposed that all airports would be brought under the independent airport consultancy study, Air NZ suggests that it might be preferable for the MoT to follow on from the consultancy study. In this respect, MoT could address any issues peculiar to small regional airports that warrant additional review and comment or which are not appropriately canvassed in the wider study.

Appendix A - Areas of operations where airports possess high market power

<p>Services provided by the supply of aircraft movement facilities and activities, comprising:</p> <ul style="list-style-type: none"> • Airside grounds, runways, gates, taxiways and aprons • Airfield lighting, airside roads and airside lighting • Ground-handling services • Airside safety • Nose-in guidance • Aircraft parking • Visual navigation aids • Aircraft ground-power and air-conditioning • Reticulation 	<p>ACCC accepts that airports possess monopoly power of such a service (see submission to PC, August 2006, page vii)</p>
<p>Passenger processing facilities:</p> <ul style="list-style-type: none"> • Forward airline support area services • Aerobridges and airside buses • Departure lounges and holding lounges (excluding VIP lounges) • Immigration and custom service areas • Public address systems, closed circuit surveillance systems, security systems • Baggage make up, handling, inspections, trolleys and reclaim • Public areas in terminals, public amenities, public lifts, escalators • Flight information display systems • Landside roads, landside lighting, and covered walkways. • Signage 	<p>ACCC accepts that airports possess monopoly power of such a service (see submission to PC, August 2006, page vii)</p>
<ul style="list-style-type: none"> • Aircraft refuelling • Aircraft maintenance sites and buildings • Freight equipment storage sites • Freight facility sites and buildings • Ground support equipment sites • Check-in counters and related facilities • Car parks 	
<p>Landside vehicle facilities (landside passenger access facilities, carparking, taxi facilities etc)</p>	<p>ACCC accepts that airports possess monopoly power of such a service (see submission to PC, August 2006, page vii)</p>
<p>Aircraft refuelling services</p>	<p>Both the ACCC and Productivity Commission have concluded that airport operators have moderate to high market power in imposing charges on aircraft refuelling facilities</p>
<p>Check-in counters and related facilities</p>	<p>Moving all check-in counters off site is neither practical nor commercially viable</p>

Appendix B - UK Airport service quality measures (2006)

Element	Metric	Standard Heathrow	Standard Gatwick
Stands	% time available	98%	98%
Jetties	% time available	97%	97%
Pier service	% passengers pier served	90%	90%
Fixed electrical ground power	% time available	98%	98%
People movers (including escalators, lifts, conveyers).	% time available	98%	98%
Security queues	Waiting time less than 10 minutes	At least 95% occasions checked	At least 95% occasions checked
Arrivals reclaim	% time Baggage Carousels available	98%	98%

Element	Metric	Standard Heathrow	Standard Gatwick
Departure lounge seat availability	Monthly QSM score	3.6	3.6
Cleanliness	Monthly QSM score	3.7	3.8
Way-finding	Monthly QSM score	3.8	3.9
Flight information	Monthly QSM score	4.0	4.0

The passenger elements (i.e. departure lounge seat availability, cleanliness, way-finding and flight information) are based on quality of service monitor (QSM) scores. The QSM scores are tabulated from questionnaires given to passengers with responses based on a 5 point scale.