



**CIVIL AVIATION BILL - EXPOSURE DRAFT:
SUBMISSION TO THE MINISTRY OF TRANSPORT**

22 July 2019

PUBLIC VERSION

**[Commercially sensitive information has been redacted – indicated in
green square brackets]**

Overview of submission

1. Auckland International Airport Limited (“**Auckland Airport**”) welcomes the release of the exposure draft of the Bill and the opportunity to provide a submission. This is appropriate given the extensive gestation period for the Bill and because it includes material proposals which were not contemplated at the time of original submissions in 2014.
2. Auckland Airport supports efforts to provide fit-for-purpose and modern legislation that facilitates a thriving, safe and secure aviation sector. The draft Civil Aviation Bill makes some useful progress towards this goal. However, certain proposals go further than “modernising” New Zealand’s aviation framework, as was originally intended by the review of the Airport Authorities Act 1996 (“**AAA**”) and Civil Aviation Act 1990. We are concerned that these proposals – particularly the proposed removal of airports’ current ability to set prices – will have material consequences and disrupt an established, effective regulatory regime where there is clear evidence that this regime is working well today.
3. We are particularly concerned about these changes given the unprecedented investment programme at Auckland Airport. We are underway with a multi-billion dollar aeronautical infrastructure development plan that will deliver nationally significant, “once-in-a-generation” investment projects including a new domestic jet facility, and a second runway, along with other major aeronautical infrastructure across our terminals, airfield, cargo facilities and ground transport network. The current airport pricing and regulatory framework provides us with confidence that we can make these investment decisions following consultation with our airline customers, and that we will be able to recover the cost of these investments and earn a reasonable return on the investments made. If the proposed changes are adopted, this confidence and certainty will be materially undermined. This will likely delay and may curtail elements of our long-term infrastructure investment plan that don’t have unanimous airline support (because of airlines’ different service offerings and preferred infrastructure) while we seek bilateral agreement from each of those airlines to ensure that they will pay to use these multi-billion dollar aeronautical assets and that we can repay our lenders.
4. Auckland Airport endorses the submission made by the NZ Airports Association (“**NZ Airports**”) in its entirety, and the points made by NZ Airports should be treated as part of Auckland Airport’s submission. In the sections below, we provide additional feedback on the following key points:

- a. **Auckland Airport strongly opposes the proposed repeal of section 4(A) of the AAA.**
The ability for airports to set charges is a fundamental part of the current pricing and economic regulatory regime, working together with Part 4 of the Commerce Act as part of a cohesive whole, which is overseen by the Commerce Commission and regarded as working well. It must be maintained. We are very concerned and disappointed at the proposed removal of section 4A when there was never any intention to use this review to change the regulatory regime applying to major airports, and there is clear evidence the current regime is working well. There is no evidence of a problem that needs to be fixed, especially when changes to maintain and strengthen the effectiveness of the current economic regulatory framework were made by Parliament just last year.

This is not about the *level* of our charges. It is about the *process* of charge-setting, airports’ ability to recover charges once set, and the necessary stability of regulatory settings at a time of material investment decision-making. In any event, Auckland Airport’s current international charges will fall by 2.5% per year on average over the current five-year pricing period, with average domestic charges reducing by 0.1% per year over that time – at the same time as we are forecast to spend \$1.8 billion on aeronautical infrastructure investment. Our average domestic charges are among the lowest in Australasia, and our international charges benchmark in approximately the middle of the pack compared to a sample of 26 peer airports. This is hardly evidence of an unfettered ability to price however we like or a problem that requires fixing – rather, it shows that Part 4 and section 4A of the AAA are working well together to generate outcomes that are good for consumers.

However, if the Government is minded to make changes to section 4A despite the material concerns outlined by NZ Airports and Auckland Airport, we support the alternative proposal

put forward by NZ Airports (which would retain the ability for airports to set prices while removing the words “from time to time as it sees fit”). This change would reflect the reality that regulated airports do not set charges ‘as they see fit’ today, particularly given the material constraints introduced by the Part 4 regulatory regime and its influence on our pricing decisions. This refinement would have the effect of removing any perceived ambiguity about the interaction between the pricing power and the regulatory regime under Part 4 of the Commerce Act, and removing any perceived impression that section 4A gives airports greater discretion than they actually have.

- b. **The approval regime for airline alliance arrangements should be changed to align with New Zealand wide best practice.** The Commerce Commission (“Commission”) is the expert competition regulatory authority in New Zealand and should be tasked with the assessment of airline alliances in accordance with the competition tests established in the Commerce Act 1986.
 - c. **Auckland Airport opposes the proposed repeal of parts of section 6 of the AAA, which provide for the ability to terminate leases for airport purposes and an exemption from other statutory requirements for long-term airport leases.** These sections continue to serve very important purposes and are not obsolete or redundant. In particular, retaining the ability for airports to terminate leases for airport purposes provides a vital backstop that helps to ensure the safe, secure and efficient operation of the airport in the face of changing market conditions and regulatory requirements.
 - d. **We agree the current capex consultation thresholds are outdated and consider that any new consultation threshold should be measured by reference to the value of an airport’s non-land assets.** We recognise the value of consultation in delivering key infrastructure projects that are aligned with the needs of our customers, and in practice we already consult with airlines much more widely than strictly required by the AAA. Percentage-based thresholds that reference non-land asset values are appropriate as they adjust with the changing scale of investment at airports and provide an accurate reflection of the materiality of present and future projects in proportion to existing infrastructure.
5. At a technical level, we have also noticed there appears to be a gap in the proposed legislation relating to the disposal of dangerous goods and have suggested a minor amendment to the legislation to support clear allocation of responsibilities and powers in this area.

The power for airports to set charges must be maintained

6. We are concerned that the draft Bill proposes to remove the section of the AAA that provides airports with the power to set charges. This power is a key part of the economic regulatory regime that applies to airports, and the original review of the AAA clearly stated that there was no intention to change that regime through the review process. The original consultation paper did not propose to make any changes to this section for major airports subject to Part 4 of the Commerce Act.
7. However, the draft Bill now proposes to remove this section because it is seen as “redundant”, apparently because airports have the powers of ordinary companies. MOT’s commentary document suggests that section 4A risks signalling that airports have greater discretion when setting charges than they would otherwise have and “overlaps” with the Commerce Amendment Act changes made in 2018. Cabinet papers also suggest the removal of the power is intended to promote “better negotiations” between airports and airlines.
8. NZ Airports has clearly articulated why these explanations are unsound and why the removal of section 4A will be extremely problematic for major airports and smaller airports alike. As set out in the NZ Airports submission, section 4A is not redundant or obsolete. Its removal is a fundamental, material and disruptive change to the economic regulation framework for airports – when the evidence and commentary from the Commission, MBIE and Parliament shows the regime is working and there is no problem to be solved.

9. In addition to the points made by NZ Airports, Auckland Airport emphasises that:

- a. The statutory ability for airports to set prices under the AAA controls the *process* by which prices are set. The *level* of prices is supervised and strongly constrained by the regulatory regime under Part 4 of the Commerce Act. As the Commission has recognised, the two statutory regimes co-exist and operate for distinct purposes. There is no overlap or inconsistency – rather, the two pieces of legislation work together to provide a cohesive regulatory regime for major airports.
- b. We recognise it is important that Auckland Airport's aeronautical services are subject to scrutiny by an independent regulator (in addition to the intense scrutiny from airlines during pricing consultations). Among other things, it is appropriate to check that we are operating and investing efficiently and that our prices are fair and reasonable. The combination of information disclosure regulation and price-setting under the AAA meets these objectives.
- c. Airport pricing decisions are inherently linked to airport investment decisions. Removing the power to set prices following consultation will effectively require airports to reach agreement with all airlines on the size and nature of the investment plan at the time prices are set. In practice, although we are often successful in reaching a high degree of alignment and broad support for investment at Auckland Airport, it is not possible to reach 100% agreement with all airlines on the forecast investment plan given that different airlines have unique business models, operating horizons and investment priorities. The current power to set prices allows Auckland Airport to navigate a pathway through different feedback from all airlines operating at the airport, and set prices reflecting the investment required to meet the needs of current and future airport users – including those users who do not pay airport charges directly but who have a strong interest in good quality airport infrastructure (such as passengers and government agencies operating at the airport).
- d. These issues are material in practice, particularly right now. Auckland Airport has a multi-billion dollar plan for aeronautical infrastructure investment over the next decade. Our confidence and ability to deliver this infrastructure plan relies on our ability to set prices and recover those charges from our airlines. It would be irresponsible for Auckland Airport to proceed with our planned multi-billion dollar aeronautical infrastructure build programme under this accidental new regulatory regime knowing that key airlines are likely to dispute the resultant aeronautical charges and protracted court proceedings will be needed to determine the ultimate returns on that investment. In the meantime, Auckland Airport will have no power to prohibit non-paying airlines from using and benefitting financially from that new infrastructure.
- e. Although airlines claim that change is required to promote commercial discussions and negotiations, airport pricing consultations are currently lengthy and robust processes where airlines are provided with extensive information and multiple opportunities to provide input and influence airport decisions. The Commission invites feedback from airlines on the process used by airports to set prices when it reviews those pricing decisions, and both airlines and the Commission have provided regular endorsement of the thorough and meaningful consultation undertaken by airports.
- f. Section 4A is a core part of an established, effective, working regulatory regime. Our first-hand experience is that this regime imposes material constraints on our ability to set prices, as seen earlier this year when Auckland Airport reduced its prices in response to concerns from the Commission that our aeronautical charges “may” have been too high. The Commission acknowledged Auckland Airport’s willingness to engage and respond positively to its final report, stating that Auckland Airport’s decision to revise our prices was a good result for consumers and showed the benefits of the current information disclosure regulations that are applied to New Zealand’s major airports. In short, we are not able to set prices “as we see fit”. This is supported by clear evidence from the Commission and policy officials that the regulatory regime is working.

10. We expand on these points below.

How airport pricing works in practice

11. Auckland Airport typically sets prices under section 4A for what we call “common use” assets and operating costs – facilities and services provided by the airport that are available for any passenger and any airline, including any new airlines that may start operating at Auckland Airport in the future. We call these prices “standard charges”.
12. Revenue from standard charges is used to operate and maintain the airport, and to support investment in new common use assets – like terminal expansions and upgrades, aircraft gates and stands, new taxiways, and runway extensions – which improve the quality of our services for today’s passengers and provide additional capacity for future growth.
13. Our pricing process uses a “building blocks” model where asset values, operating costs, forecast capital investment, depreciation, tax and a target return are used to generate a forecast of the revenue needed by the airport to operate and invest over a five-year period. We then use a forecast of demand over the period along with economic principles to allocate that forecast revenue to different services and different airport users in a way that best reflects the cost associated with the services used. Auckland Airport consults thoroughly on each of these elements, along with other important factors such as service quality (which directly impacts the level of forecast operating costs and investment).
14. The ability to set and enforce prices under section 4A following consultation is vital to this process. This is because:
 - a. **The airport is a complicated system and a common-use approach to pricing reflects this reality.** The majority of airport charges recover the fixed costs of common use airport infrastructure, which is used in an overlapping and interchangeable way by passengers, airlines and government agencies. Section 4A allows us to adopt a clear, transparent and robust cost-based method to recover those fixed costs from all airlines in a fair, reasonable and equitable manner. Auckland Airport remains open to individual agreements with airline users, although these typically work best where an airline wishes to pay for dedicated facilities or exclusive use of terminal or airfield space. For common use infrastructure with high fixed costs, section 4A provides a clear process for us to set standard charges for standard services without requiring mandatory agreements with all airlines. Customers have assurance that the price for those services is then reviewed and assessed by the Commerce Commission.
 - b. **Section 4A gives us the ability to set charges that provide a level playing field for all airlines.** We set a standard charge that applies to any airline that wants to use our airport facilities. For example, any passenger on any airline is charged the same price to use Auckland Airport’s international terminal. Any airline flying the same type of aircraft pays the same price to use the runway. This is the best way to make it easy for new airlines to start flying to New Zealand, and we have been able to quickly accommodate over 18 new airlines over the past four years under this model. A standard price for common use infrastructure means that these new airlines pay the same price to use the same infrastructure and facilities as existing airlines, with no barriers to entry. In this way, our investment and pricing approach promotes open access and competition between airlines, which has a hugely beneficial impact on airfares as well as increasing the number of available destinations and frequency of services to those destinations. This has a massive benefit for New Zealand and the travelling public.
 - c. **Requiring agreement on prices would require agreement on investment decisions.** For a regulated business, it is not possible to separate investment and price. Our prices reflect the value of the airport’s current assets and investments, as well as those which are forecast to be built over the pricing period in question – an area where airlines frequently have different views to each other. For example, when we set prices in 2017, the investment plan embedded in our pricing decision was supported by airlines representing

over 80% of passengers at Auckland Airport. This gave us good confidence our investment plan was reasonable. The current pricing regime allowed us to make a decision on that base investment plan, set prices, and get on with the next stages of planning and delivery with confidence that we would be able to recover the cost of our investment programme from all users – not just from 80% of them.

We are constantly talking to our airline customers about what we are building and we try to deliver to their requirements where we can – but if we had to reach agreement on the investment plan with all airlines before we set prices, there's a good chance we would still be negotiating today. Similarly, if we set charges on the expectation that we would likely need to pursue some airlines in court to pay those charges, that would have a substantial chilling effect on our confidence to continue with the investment plan underpinned by those prices.

- d. **More generally, different airlines have different views on a number of building block inputs.** International airlines want to pay a lower proportion of shared infrastructure costs than domestic airlines, and vice versa. Different airlines have different service quality aspirations and therefore value investment and operating process changes differently. Airlines have different growth aspirations and therefore different views on likely future demand at an airport and the required infrastructure. The ability to set prices following consultation allows Auckland Airport to navigate a way through the airline feedback that has been provided and seek to strike the right balance for all consumers for the long term.
- e. **Charges set under section 4A have a key role to play in sending price signals that encourage efficient behaviour and discourage inefficient behaviour** – maximising the overall efficiency of the airport system and minimising total cost through unnecessary investment. As the Commission has previously recognised, the prices set by Auckland Airport through its pricing methodology have an important role to play in improving efficiency. Consistent with outcomes observed in workably competitive markets, the prices set by Auckland Airport for each charged service should help ensure the efficient allocation of its aeronautical services and therefore its resources and provide signals of where innovation and investment is needed at Auckland Airport to meet consumer demands.

Efficient pricing involves ensuring that prices are subsidy-free, scarce goods and services are consumed by those that value it the most, prices allow consumers to make price-quality trade-offs, and the development of prices is transparent and promotes price stability. In practice, this involves concepts like allocating shared costs between domestic and international users, and efficient pricing tools like peak pricing (which the Commission has specifically encouraged Auckland Airport to consider in the future). However, our ability to implement these efficient pricing mechanisms relies on our ability to set prices under section 4A. Rational commercial airlines would not readily agree to pay prices that are designed to change their behaviour, even where this does not impact the overall level of revenue earned by an airport and may be the most efficient solution for the overall airport system.

- f. **Section 4A allows airports to consider the needs and interests of airport users other than airlines when making pricing and investment decisions.** Ultimately, airports must set prices that provide for investment in the core infrastructure that will give New Zealand the capacity it needs to grow and succeed – which means taking a long-term view that balances the views of all airlines, government agencies operating at the airport, other businesses operating here, and current and future passengers. Auckland Airport's charges set under section 4A recover the cost of infrastructure investments, with that cost determined by the design, layout, and spatial requirements of the infrastructure that will be built. Those requirements – and therefore the ultimate cost of the infrastructure and the level of prices that result – are influenced by a very wide group of stakeholder needs. Although airlines are a very important part of that stakeholder set, they are not the only party who has relevant views. The fact that airports have the power to set standard charges

gives us the ability to directly consider and include requirements of these other airport users when making decisions about what we build and how we operate which flow through to charges to airlines – even where this might differ from the shorter-term priorities and commercial motives of airlines currently operating at Auckland Airport at any given time.

Airline consultation at Auckland Airport is robust, effective, and commended by airlines

15. We anticipate that policy makers – influenced by airlines – may be of the view that removing section 4A will help to ensure better commercial discussions take place about airport pricing and that airports have regard to the views of their customers when setting prices. The reality is that the current regulatory and pricing regime is already promoting robust commercial conversations between airports and airlines about prices and investment.
16. Pricing consultations at Auckland Airport involve a thorough and extensive process. Under the AAA, consultation has evolved to become a rigorous process of information gathering and robust discussion that imposes significant pricing pressure. Our substantial airline customers are knowledgeable, well-resourced, and involved in pricing discussions worldwide. They are experienced participants in pricing consultations and are able to bring considerable scrutiny to the process.
17. This creates an environment where we are genuinely interested in learning about our customers and their needs. In addition, we learn a lot from our airline customers about international best-practice approaches. As we learn more about and from our customers, consultations become more effective and lead to better outcomes for all parties.
18. To provide an example of how this process operates in practice, the table below shows the key milestones from the most recent pricing consultation at Auckland Airport:

Milestone	Date
Consultation overview – initial briefing	9 June 2016
Info Pack #1 released: Pricing approach	2 Sept 2016
Meetings with customers on Information Pack #1	16 Sept 2016
Airline written responses to Information Pack #1 due	30 Sept 2016
Info Pack #2 released: Investment outlook	30 Sept 2016
Meetings with customers on Information Pack #2	7 Oct 2016
Airline written responses to Information Pack #2 due	28 Oct 2016
Info Pack #3 released: Cost drivers, forecasts and allocations	31 Oct 2016
Meetings with customers on Information Pack #3	11 Nov 2016
Airline written responses to Information Pack #3 due	25 Nov 2016
DRAFT PROPOSAL RELEASED	15 Dec 2016
Meetings with customers on Draft Proposal	2 Feb 2017
Written responses to Draft Proposal	22 Feb 2017
REVISED PROPOSAL	24 March 2017
Meetings with customers on Revised Proposal	29 March 2017
Written responses to Revised Proposal	20 April 2017
Substantial Customers meet with Board sub-committee	3 May 2017
FINAL PRICING DECISION	8 June 2017
NEW STANDARD CHARGES OPERATIVE (UNLESS EXPRESSLY IDENTIFIED AS DELAYED IMPLEMENTATION)	1 July 2017

19. As shown above, during consultation Auckland Airport publishes a series of information packs and discussion papers to explore different pricing elements, before preparing a draft proposal, revised proposal, and final decision. Auckland Airport prepares and shares hundreds of pages of information, expert evidence, and supporting explanations for the decisions that have been made – including carefully setting out and responding to airline feedback. Airline feedback is sought and valued at every step of the process through a combination of joint meetings, individual meetings with airlines, written feedback, and informal discussions throughout. Airlines are provided with an opportunity to present directly to the Aeronautical Pricing Committee of Auckland Airport's Board. This is rigorous, robust, commercially focused engagement that aims to test and balance past practice, current circumstances, economic evidence, regulatory guidance, passenger interests and airline feedback to strike the best long-term outcomes.
20. Airlines and the Commission have recognised the constructive approach to consultation adopted by Auckland Airport. For example, comments from BARNZ and Air New Zealand near the conclusion of Auckland Airport's 2012 pricing consultation and through the subsequent Commission review illustrated that on the whole, both parties believed the quality of our consultation process was high. While the airlines did have some remaining substantive concerns at the conclusion of the process, these were largely restricted to narrow, detailed points of difference on technical matters. In particular:
- a. BARNZ explicitly noted in feedback to Auckland Airport's Board prior to the final pricing decision that it considered Auckland Airport's consultation process had been constructive and had enabled good dialogue between the parties.¹
 - b. Air New Zealand acknowledged that it had come a long way with Auckland Airport in working together for the benefit of their mutual customers.² Air New Zealand also recognised that (setting aside the level of charges), changes to Auckland Airport's pricing in 2012 reflected efficient pricing principles, and created a stronger link between the facilities that are used and the charges and revenues associated with those facilities.³
 - c. BARNZ and Air New Zealand's positive comments about Auckland Airport's consultation philosophy extended to our approach to capital expenditure consultation, which was positively endorsed by BARNZ,⁴ and described as "robust, transparent and inclusive" by Air New Zealand.⁵ In particular, BARNZ noted Auckland Airport's changed approach to capital expenditure in its 2012 price setting consultation, stating that "in the more than 10 consultations over the resetting of charges under the AAA which BARNZ staff have been involved with, this is the first occasion on which an airport has included airline priorities as a fundamental initial step in capital expenditure planning".⁶
21. We built on this positive foundation when setting prices for our most recent pricing decision in 2017. Again, the quality of our consultation was praised:
- a. Near the end of the pricing consultation process substantial customers were provided with an opportunity to present to a sub-committee of Auckland Airport's Board. Airlines took this opportunity to draw attention to the substantive issues that mattered to them the most ahead of the final pricing decision. As part of the meetings, airlines were also asked if they had any feedback on Auckland Airport's consultation process. BARNZ confirmed that that the pricing consultation process had worked well, that there had been good exchanges, and that Auckland Airport had been very professional in the material that had been provided to BARNZ. BARNZ also noted that it appreciated the interaction with Auckland Airport on capital consultation, that it understood capital planning was complex, and that it hoped to keep the good dialogue going throughout the pricing period.⁷

¹ Auckland Airport, Final Price Setting Disclosure, Aeronautical Pricing Consultation, 2 August 2012, at page 36.

² As recorded in Auckland Airport, Final Price Setting Disclosure, Aeronautical Pricing Consultation, 2 August 2012, page 36-37.

³ Air New Zealand Submission on Section 56G Review of Auckland Airport, page 19.

⁴ BARNZ Response to Section 56G Issues Paper Relating to Auckland Airport, page 30.

⁵ Air New Zealand Submission on Section 56G Review of Auckland Airport, page 16.

⁶ BARNZ Response to Section 56G Issues Paper Relating to Auckland Airport, page 30.

⁷ As recorded in Auckland Airport, Section 53B review of Auckland Airport's price setting disclosure for PSE3: cross-submission on process and issues paper, 19 December 2017 at page 24.

- b. Air New Zealand also stated that it was happy with the pricing and capital consultation processes. Air New Zealand executives noted that the capex consultation process had been very collaborative, and that it was producing very good results such as Pier B. Air New Zealand said that it valued discussion of the wider context which had helped broaden understanding, and that the terminal consultation process had been better and richer as a result.⁸
 - c. When providing its views to the Commission as part of the review of Auckland Airport's pricing decision, BARNZ noted that the price development process at Auckland Airport is transparent to substantial customers, and that Auckland Airport consults extensively on its prices with substantial customers and provides descriptions and explanations of its proposals.⁹
 - d. BARNZ also acknowledged the impact of airline feedback and information disclosure regulation on Auckland Airport's 2017 pricing decision – noting that Auckland Airport reduced its target return in response to submissions and also provided a substantial amount of justification for its target.¹⁰
22. We appreciate that consultation is still seen as a valuable part of the regulatory framework, and that airports' consultation obligations have been retained in the draft Bill.
 23. However, section 4A currently empowers Auckland Airport to make the final decision on prices after consultation is complete. This reflects the reality that pricing discussions involve a variety of airlines with different interests and priorities. Different customers have unique (and sometimes competing) service and investment priorities. Consultation allows Auckland Airport to balance these views and reach an outcome that reflects our diverse base of intermediate customers and which delivers the best outcome for the ultimate consumers — passengers. Having consulted extensively, our prices are set and enforceable – and then subject to review and scrutiny by the Commission, which judges whether they are reasonable and efficient.
 24. If section 4A is removed, we could follow the same extensive and rigorous consultation process that we do today – but with no confidence that we will have clear and enforceable prices at the end of that process. No matter how well we consult, how robust the process, how much information we share, how much time we spend listening to our airline customers and seeking to understand their views, there is no guarantee that all airlines will agree to the prices that flow out of that consultation process. There will always be areas where airports and airlines do not agree. There will always be areas where different airlines have competing views. There will always be areas where Auckland Airport is required to look across the long-term interests of all airport users and make a decision. And without agreement, and without section 4A, our prices are not enforceable in statute or in contract law.
 25. Today, if airlines have remaining concerns about airport prices after consultation, their avenue is to raise those concerns with the Commission when it undertakes its review of the prices that have been set by that airport. Airlines directly engage in the Commission's review process and provide their views directly to the regulator.
 26. If section 4A is removed, airlines will have a further option – simply refuse to pay. Or pay less than what is invoiced. This happens regularly in Australia, and airports have no recourse other than to bring legal action to recover unpaid charges. At the moment, Qantas is currently locked in disputes with Perth Airport and two Northern Territories airports over pricing and investment, generating considerable uncertainty and inefficiency.
 27. For Auckland Airport, the idea that we could plan and reach broad alignment on a multi-billion dollar aeronautical infrastructure investment programme, consult to the very best of our ability for a year or more on airport prices, but then not have any confidence on the enforceability of our prices or

⁸ As recorded in Auckland Airport, Section 53B review of Auckland Airport's price setting disclosure for PSE3: cross-submission on process and issues paper, 19 December 2017 at page 24.

⁹ BARNZ Assessment of AIAL's PSE3 Pricing Decision against Part 4 Criteria, 28 November 2017 at page 8.

¹⁰ BARNZ Assessment of AIAL's PSE3 Pricing Decision against Part 4 Criteria, 28 November 2017 at page 12.

our ability to repay our lenders is extremely worrying. As we explain below, we are particularly nervous about the impact of this very disruptive change at a time when we can least afford that uncertainty.

Current regulatory settings are working and producing the right outcomes

28. For New Zealand's three largest airports – Auckland, Christchurch and Wellington – the prices set under section 4A of the AAA are subject to an information disclosure regime that is designed to be active economic regulation, and which mirrors key parts of the way the Commission sets prices for its price-controlled regulated businesses. The Commission designed the airport regulatory framework to promote the same outcomes that would be seen in competitive markets, and to drive investment, quality, efficiency and pricing outcomes which are consistent with the long-term benefit of airlines and passengers. The Commission continues to apply these tests today when it reviews every pricing decision made by the three major international airports.
29. When it comes to prices, the Commission actively measures whether airports are earning a fair, or “normal” profit (called a “normal return” in the regulatory world). It does this by looking at an airport's return on investment – and checking whether that represents a fair and reasonable approach given the individual circumstances of each airport.
30. In other words, the Commission regularly and carefully checks whether airports are earning a normal profit over time. And it can do that because airports are required to publicly disclose a huge range of information about their pricing decisions – including the forecast investment plans and operating costs used to set prices. This is transparent cost-based pricing, scrutinised by a competition and regulatory watchdog – a far cry from common airline claims that airports are free to do whatever they like.
31. And the regime is clearly working. When Auckland Airport set prices in 2012 (referred to as “PSE2”, although this was actually the first exercise of our power to set prices under s4A of the AAA after Part 4 of the Commerce Act came into force), the Commission made a number of important findings about our behaviour and about the regime. At that time, the Commission concluded that Auckland Airport's conduct and behaviour was effectively promoting the long-term benefit of consumers across a wide range of performance areas. In particular, the Commission found that:
 - a. Innovation at Auckland Airport was appropriate (including that we facilitate airline-led innovation) and the airport regulatory framework was effectively promoting incentives in this area.¹¹
 - b. The quality of service at Auckland Airport was very good and met the demands of passengers and airlines.¹² Further, the Commission concluded that information disclosure regulation had not negatively affected existing incentives to provide services at a quality that reflects consumer demands.¹³
 - c. Information disclosure regulation was effectively promoting efficient pricing at Auckland Airport, including improving the efficiency of pricing,¹⁴ that Auckland Airport explicitly considered consumers' demand responsiveness when establishing our pricing

¹¹ Commerce Commission “Final report to the Ministers of Commerce and Transport on how effectively information disclosure regulation is promoting the purpose of Part 4 for Auckland Airport – Section 56G of the Commerce Act 1986” (31 July 2013), paragraph B3.

¹² Commerce Commission “Final report to the Ministers of Commerce and Transport on how effectively information disclosure regulation is promoting the purpose of Part 4 for Auckland Airport – Section 56G of the Commerce Act 1986” (31 July 2013), paragraph C3.

¹³ Commerce Commission “Final report to the Ministers of Commerce and Transport on how effectively information disclosure regulation is promoting the purpose of Part 4 for Auckland Airport – Section 56G of the Commerce Act 1986” (31 July 2013), paragraph C5.

¹⁴ Commerce Commission “Final report to the Ministers of Commerce and Transport on how effectively information disclosure regulation is promoting the purpose of Part 4 for Auckland Airport – Section 56G of the Commerce Act 1986” (31 July 2013), paragraph D5.

methodology,¹⁵ and that Auckland Airport set prices transparently - having regard to price stability and certainty for stakeholders when doing so.¹⁶

- d. Auckland Airport had effectively consulted on forecast capital expenditure with airlines for PSE2, and the consultation process adopted by Auckland Airport had been commended.¹⁷ Parties considered that the level and timing of planned investment for PSE2 was efficient based on the circumstances at the time of pricing,¹⁸ and there was no evidence of planned under or over-investment at Auckland Airport for PSE2.¹⁹
 - e. Importantly, that Auckland Airport was limited in its ability to extract excess profits and had set prices under s4A of the AAA to target returns within an acceptable range.²⁰
32. For our 2017 price setting event under the AAA ("**PSE3**"), the Commission initially had some reservations about whether Auckland Airport's prices may be too high, although it did not make a definitive finding of excess profits. Auckland Airport responded by reducing its charges earlier this year – a move welcomed by the Commission and praised as good for consumers. The Commission acknowledged Auckland Airport's willingness to engage and respond positively to its final report, stating that Auckland Airport's decision to revise our prices was a good result for consumers and showed the benefits of the current information disclosure regulations that are applied to New Zealand's major airports. The Commission was also clear that the incentives from the information disclosure regime have strengthened over time, as targeted returns were significantly lower than when the current regime was introduced.²¹
33. Throughout the review of our 2017 pricing decision, the Commission also made a number of positive findings about Auckland Airport's pricing approach and projected performance. For example:²²
- a. The Commission recognised that Auckland Airport was investing heavily in new infrastructure in response to growth, that planned and actual investment was generally occurring at an appropriate time, that Auckland Airport engages well with its customers on investment, and that a high level of rigour had been applied by Auckland Airport to costing the forecast capex plan. We welcomed the Commission's findings that there was no evidence of planned under-investment, over-investment, bias in capex forecasting, or a strategy to gain from delaying projects at Auckland Airport.
 - b. The Commission reviewed and had no significant concerns about any of Auckland Airport's forecasts, including our forecast asset values, demand projections, operating costs and capital expenditure.
 - c. The Commission found that Auckland Airport had continued to seek improvements to the efficiency of its prices in PSE3 – including introducing differential charges for domestic passengers on trunk and regional routes, differentiated charges for check-in services, and

¹⁵ Commerce Commission "Final report to the Ministers of Commerce and Transport on how effectively information disclosure regulation is promoting the purpose of Part 4 for Auckland Airport – Section 56G of the Commerce Act 1986" (31 July 2013), paragraph D25-26.

¹⁶ Commerce Commission "Final report to the Ministers of Commerce and Transport on how effectively information disclosure regulation is promoting the purpose of Part 4 for Auckland Airport – Section 56G of the Commerce Act 1986" (31 July 2013), paragraph D31.

¹⁷ Commerce Commission "Final report to the Ministers of Commerce and Transport on how effectively information disclosure regulation is promoting the purpose of Part 4 for Auckland Airport – Section 56G of the Commerce Act 1986" (31 July 2013), paragraph H4.2.

¹⁸ Commerce Commission "Final report to the Ministers of Commerce and Transport on how effectively information disclosure regulation is promoting the purpose of Part 4 for Auckland Airport – Section 56G of the Commerce Act 1986" (31 July 2013), paragraph H4.2.

¹⁹ Commerce Commission "Final report to the Ministers of Commerce and Transport on how effectively information disclosure regulation is promoting the purpose of Part 4 for Auckland Airport – Section 56G of the Commerce Act 1986" (31 July 2013), paragraph H17.

²⁰ Commerce Commission "Final report to the Ministers of Commerce and Transport on how effectively information disclosure regulation is promoting the purpose of Part 4 for Auckland Airport – Section 56G of the Commerce Act 1986" (31 July 2013), paragraph E3-E6.

²¹ Commerce Commission media release, 28 March 2019, <https://comcom.govt.nz/news-and-media/bulletin/auckland-airports-pricing-response-welcomed>

²² See Commerce Commission "Review of Auckland International Airport's pricing decisions and expected performance (July 2017 – June 2022): Final report – Summary and analysis under section 53B(2) of the Commerce Act 1986", 1 November 2018 – especially paras 181-185, X47-X48.

parking charges. Although the Commission considered that Auckland Airport could have given greater consideration to whether peak charges were appropriate, it did not consider that this raises any significant efficiency concerns for PSE3. We were pleased that the changes we made to our pricing structure were recognised as contributing to improved efficiency.

34. During the most recent review of Auckland Airport's prices by the Commission, airlines also spoke about Auckland Airport's willingness to engage and work constructively with airlines on a number of important pricing matters:

- a. BARNZ and Air New Zealand generally supported Auckland Airport's approach to consultation and engagement, and were broadly supportive of the airport's investment programme.²³
- b. BARNZ noted that Auckland Airport is generally willing to respond to customer concerns and help partners deliver better and more efficient services and cites as an example that Auckland Airport listened to airline concerns over the bussing product and made changes in response. BARNZ also noted that Auckland Airport has introduced ground power at international gates and stands (which assists aircraft efficiency and lowers costs and greenhouse gas emissions), and has taken steps to resolve reliability issues, such as the reliability of the baggage handling system.²⁴
- c. BARNZ acknowledged that Auckland Airport is willing to work with airlines and agencies to deliver service quality improvements.²⁵ BARNZ also recognised that Auckland Airport seeks to deliver innovative solutions, either to improve passenger experiences or to avoid capex, and that Auckland Airport has introduced innovations where a pressure point has emerged.²⁶
- d. Further, BARNZ acknowledged that Auckland Airport engages well with consumers on operational matters and capital planning.²⁷

35. We have been pleased the Commission has made positive findings about our pricing decisions and performance across the two pricing periods so far under today's economic regulatory regime, and that both the Commission and airlines have recognised Auckland Airport's robust approach to price setting and capital investment planning. These findings show that:

- a. Auckland Airport takes a careful, considered and reasonable approach to setting prices under s4A of the AAA. We seek to anticipate the way that our pricing decision will be assessed by the Commission, and to target a fair and reasonable return that balances our airport-specific circumstances and risks with feedback from our substantial customers and guidance from the regulator.
- b. The power to set prices under section 4A does not allow an airport to set prices at whatever level it likes. The level of airport charges, the reasonableness of airport forecasts, and other important factors like the efficiency, transparency and stability of airport prices, are heavily constrained and checked by the Commission.
- c. There is no danger that airports see section 4A as somehow allowing them to operate without proper regulatory scrutiny. That scrutiny has been demonstrably proven to be effective for all airports. Auckland Airport's prices have ultimately been welcomed as good outcomes for consumers in both price setting events since the introduction of Part 4.

36. In this way, section 4A works together with Part 4 of the Commerce Act as part of a cohesive regulatory regime. Section 4A gives airports the confidence that we can set enforceable prices

²³ Commerce Commission "Review of Auckland International Airport's pricing decisions and expected performance (July 2017 – June 2022): Final report – Summary and analysis under section 53B(2) of the Commerce Act 1986", 1 November 2018 at paragraph 212.

²⁴ BARNZ *Assessment of AIAL's PSE3 Pricing Decision against Part 4 Criteria*, 28 November 2017 at page 18.

²⁵ BARNZ *Review of Auckland and Christchurch Airport's Third Price Setting Events – Appendix*, 28 November 2017, page 19.

²⁶ BARNZ *Review of Auckland and Christchurch Airport's Third Price Setting Events – Appendix*, 28 November 2017, page 19.

²⁷ BARNZ *Assessment of AIAL's PSE3 Pricing Decision against Part 4 Criteria*, 28 November 2017 at page 18.

after thorough consultation and then move forward with what needs to be done. Part 4 gives airlines, passengers, and the public confidence that our prices are carefully scrutinised by an independent regulator who checks that they are in the long-term interest of consumers.

Change creates material risk at a time when our major investment plan requires certainty and stability

37. As will be apparent from this submission, we are very concerned at the proposed removal of section 4A when it is an integral part of the overall airport regulatory regime. This change has been proposed despite the fact that there was never any intention to use this review to change the economic regulatory regime applying to major airports, there is clear evidence the current regime is working well, there is no evidence of a problem that needs to be fixed, and when changes to the regulatory framework for airports were made by Parliament in October 2018. We are disappointed at finding ourselves in a position where we need to continue to defend key statutory provisions that form part of a regulatory regime that was found to be working well by all government agencies and Ministries involved just last year.
38. This is particularly disappointing when it has never been clearly articulated what advantages there might be in removing section 4A:
- a. Consultation under the AAA already provides for robust, commercial, ongoing discussions between airports and airlines about prices and investment, with considerable sharing of information and opportunities for feedback throughout. This process is clearly a material influence on airport decisions.
 - b. Prices for common-use infrastructure, facilities and services are already set using a cost-recovery model that follows the same methodology the Commission uses to set maximum revenues for businesses that are price controlled. This model is designed to recover revenue that covers an airport's efficient operating and investment costs, including providing for a fair return on investment.
 - c. If airlines want exclusive use of dedicated facilities, they are already able to enter into individual agreements with airports for such facilities. Auckland Airport has a number of these types of agreements in place today (e.g. where an airline or other aeronautical user wishes to lease a particular part of the terminal or airfield). Airports also remain open to commercial agreements with airlines more broadly – we just do not consider it is practical for feasible for such agreements to be mandatory.
 - d. Airport prices (both the overall revenue targeted and the efficiency of those prices) are already closely scrutinised by the regulator who assesses whether they are fair, reasonable and in the long-term interest of consumers, and who has the ability to trigger changes to the regulatory regime if that is considered necessary.
 - e. As NZ Airports has clearly explained, and as we have noted above, all evidence shows the current regime for airport pricing and regulation is working well.
39. In contrast, removing section 4A would:
- a. Give airlines in the minority the ability to slow investment progress by refusing to agree to prices that incorporate infrastructure investment they don't agree with.
 - b. Increase barriers to entry for new airlines as incumbent airlines rationally seek pricing and investment arrangements that favour them as existing operators.
 - c. Make it more difficult for airports to adequately provide for the interests of government agencies operating at the airport (such as Avsec, MPI, Customs and Immigration NZ), as the passenger-facing space provided by the airport in which these agencies operate forms part of the asset base used to set airline charges.

- d. Increase tension between domestic and international airlines over the allocation of shared costs between users – their interests are directly opposed here and we consider it will be almost impossible to reach a position that both international and domestic airlines would agree to.
 - e. Lead to inefficient utilisation of assets if airports are unable to introduce pricing mechanisms designed to encourage efficient behaviour (such as peak pricing and other efficient differential charging mechanisms) – which are unlikely to be agreed to by those parties engaging in the behaviour the charges are designed to discourage. In turn, inefficient behaviour would trigger inefficient capital investment that is either larger than needed or required inefficiently early.
 - f. Likely result in smaller airlines having less representation on airport pricing and investment matters than they do today as BARNZ would be at risk of breaching the cartel provisions in the Commerce Act by acting collectively for these airlines in negotiations towards a pricing agreement (explained more fully by the NZ Airports submission).
 - g. Create a real risk of under-recovery where, even in circumstances where the overall revenue targeted by an airport is fair and reasonable and linked to an appropriate investment plan with broad support, individual airlines do not agree to pricing arrangements designed to recover that revenue. This would leave an airport at real doubt about whether it will be able to recover its efficient costs, including its efficient investment costs and repay the lenders that have financed this infrastructure.
 - h. Introduce the very real risk that airlines refuse to pay airport charges they don't agree with, forcing airports to bring court action to recover the cost of the service. This would introduce considerable uncertainty and disruption and frustrate the ability of airports to deliver good quality aeronautical investment in a timely manner. As explained by NZ Airports, this process would effectively ask the court to determine what is a reasonable price to pay for a regulated service – which is essentially what the Commission already does today under current regulatory settings.
40. Even if it were possible to reach agreement with every airline operating at Auckland Airport and avoid the need for costly and wasteful litigation, that process would be extremely time consuming and is likely to involve protracted negotiations. This would result in a multitude of different agreements, entered into at different times, for different lengths, with different terms and different price points – but for the use of the same infrastructure, facilities and services. Aside from the inefficiencies and uncertainties that this process would create, it is not clear at which point during the multiple different contract negotiations with different airlines that an airport would have enough certainty to proceed with major investment projects.
41. Auckland Airport is underway with an unprecedented multi-billion dollar aeronautical infrastructure investment programme to continue to provide quality services to existing customers and to cater for forecast growth. Airlines representing over 80% of passengers at Auckland Airport were supportive of this investment plan at the time we set prices. We cannot afford for investment planning to stall while we attempt to get 100% agreement (extremely unlikely) or work through court proceedings to recover our prices.
42. Soon, Auckland Airport will need to make a decision to start construction of the second runway, a huge milestone for us, Auckland and New Zealand. Removing section 4A creates real uncertainty ahead of such a large investment decision.
43. At the moment, there is a high degree of alignment about the need for a second runway at Auckland Airport. However, we anticipate that setting prices for the second runway will be challenging. Different airlines are likely to have very different views about the best pricing approach given their individual operating models, growth strategies, and their differing commitments to New Zealand. We expect this will continue to be an important discussion topic both before and after the runway is built, and an area where we will need to carefully navigate airline feedback, economic evidence, regulatory guidance and the long-term interests of all current and future customers.

44. On top of this, removing section 4A would open the door for airlines to refuse to pay for the second runway. It would open the door for some airlines to claim they will just continue to use the existing runway and have no need for the second runway – even though the whole airport is a system and the new runway will be required because overall demand is greater than can be handled at a single-runway airport.
45. We are struggling to see how Auckland Airport could have confidence to start such a material investment – and others in our substantial investment plan – without confidence in the stability of the airport pricing and regulatory regime, and without confidence we will be able to recover the cost of that investment and service the debt and equity funding required.

Alternative proposal

46. Auckland Airport's primary position is that the current wording of section 4A should be retained in the Bill. However, if the Government is minded to make changes to section 4A despite the material concerns outlined by NZ Airports and Auckland Airport, we support the alternative proposal put forward by NZ Airports (which would retain the ability for airports to set prices while removing the words "from time to time as it sees fit").
47. This change would reflect the reality that regulated airports do not set charges 'as they see fit' today, particularly given the material constraints introduced by the Part 4 regulatory regime and its influence on our pricing decisions. Auckland Airport's recent pricing reductions for the final three years of its FY18-22 pricing period in response to the Commission's review of our original pricing decision is just one such example.
48. In short, this refinement of the existing provision would have the effect of removing any perceived ambiguity about the interaction between the pricing power and the regulatory regime under Part 4 of the Commerce Act, and removing any perceived impression that section 4A gives airports greater discretion than they actually have, while still preserving the essential ability for airports to set prices for the use of their services and have confidence they can recover those prices.

Approval of airline alliance arrangements should move to the Commission

49. Auckland Airport appreciates the economic pressures that airlines operate under, and generally supports initiatives which aim to alleviate these pressures in order to drive benefits for the travelling public and New Zealand through increased air connectivity to a wider range of international destinations. As such, Auckland Airport supports market structure arrangements that are consistent with fair and balanced competition, and which provide clear benefits for travellers – including arrangements that will deliver increased capacity, choice, and quality of service.
50. However, international air travel is a vital part of the economy of an isolated country such as New Zealand. It is vital to ensure that cooperation arrangements do not have a detrimental impact on the continued promotion of competition in international air services that is so vital to the tourism sector and New Zealand's economic prosperity. For instance, Auckland Airport would be concerned about market structure developments that have the potential to lead to fewer flights, fewer seats, and/or increased prices for travellers – including where this may set a precedent for further reductions in capacity or choice in the future.
51. It is therefore crucial that arrangements for airline cooperation are robustly tested, that benefits are clearly demonstrated at the time of the application for approval and over time, and that the impact on the overall structure of the aviation market is carefully considered.
52. Ultimately, the decision-making Minister must be satisfied that cooperation will deliver benefits to New Zealand consumers, and remain satisfied throughout the duration of the alliance – including through the use of controls such as capacity conditions and the ability to review the arrangement over time in order to safeguard consumer interests.
53. Auckland Airport agrees with NZ Airports that the process for assessing the suitability of airline alliance arrangements should follow established best practice for other sectors in New Zealand and move to the Commerce Act. The Commission should be adopted as the primary assessor, and

airline alliance applications should be reviewed against the established competition guidelines in the Commerce Act, with opportunities for input from MOT where relevant.

54. This would allow the agencies to best utilise their respective areas of expertise to facilitate a thorough assessment of the economic, social and political implications of an airline alliance arrangement and provide the Minister with a complete understanding when deciding the outcome of an application and over time as the effects of that application can be seen in practice.

Current leasing powers are important and must be retained

55. Auckland Airport has grown from several hundred thousand passengers in 1966 to 20.5 million in 2018. We expect this trend to continue and anticipate 40 million passenger movements and 260,000 flights a year in 2040. Auckland Airport has also become New Zealand's second largest cargo port by value with \$12 billion in imports, \$7 billion in exports and 240,000 tonnes of airfreight handled in FY18. To accommodate this growth and support New Zealand's vision to become a global travel destination, continuous infrastructure and development is required.
56. Although airports are long-term infrastructure businesses with long planning horizons and detailed masterplans for future land use and airport development, airports can also change rapidly over a short timeframe. Auckland Airport uses leases across our business to manage these challenging requirements, using our statutory rights and leasing arrangements to strike the right balance – one where we aim to provide lessees with certainty of tenure as much as possible given known information and planning forecasts and to ensure that land marked for aeronautical development is efficiently used in the interim, while maintaining the ability to adapt to changing airport requirements over time (including those outside our control).
57. Auckland Airport has a range of leases that grant an individual customer exclusive possession of space or buildings in the terminal, on the airfield, and in the surrounding airport precinct. Lease rental prices are generally negotiated by agreement, typically with reference to market evidence and commensurate with the level of service or exclusivity of possession required by the customer. This is possible because, unlike the core regulated aeronautical services (i.e. common use airfield and terminal assets), each asset that is subject to a lease is typically used exclusively by one customer.
58. The uniqueness of the airport precinct and our leasing arrangements is highlighted in our airfield and terminal environments. We have approximately 140 leases within the current airfield and terminal boundaries, with another approximately 210 leases in the surrounding areas of the airport.
59. The following table shows the length of Auckland Airport's current leasing arrangements:

Final expiry date of lease	Number of leases expiring that year
[redacted]	[redacted]
[redacted]	[redacted]
[redacted]	[redacted]
[redacted]	[redacted]
[redacted]	[redacted]
[redacted]	[redacted]
[redacted]	[redacted]
[redacted]	[redacted]
[redacted]	[redacted]
[redacted]	[redacted]
[redacted]	[redacted]
[redacted]	[redacted]

Final expiry date of lease	Number of leases expiring that year
[redacted]	[redacted]
[redacted]	[redacted]
[redacted]	[redacted]
[redacted]	[redacted]
[redacted]	[redacted]
[redacted]	[redacted]
[redacted]	[redacted]
[redacted]	[redacted]
[redacted]	[redacted]
[redacted]	[redacted]
[redacted]	[redacted]
[redacted]	[redacted]
[redacted]	[redacted]
[redacted]	[redacted]
[redacted]	[redacted]
[redacted]	[redacted]
[redacted]	[redacted]

60. As can be seen, there are a number of long-term leases in force today at Auckland Airport. In a landscape of ever-changing market conditions, regulatory requirements, safety and security obligations, and a material aeronautical development and construction programme, it is vital that Auckland Airport retains the ultimate ability to control our land and the leasing powers that exist under the AAA today.

Statutory power to terminate leases


61. MOT has proposed removing the current power for airports to terminate leases for airport purposes. It is concerning that the current proposal recommends the removal of this crucial statutory power, particularly when no explanation has been provided to justify its removal.

62. In practice, Auckland Airport takes its masterplanning role across the airport very seriously and seeks to maintain an environment of stability and certainty that supports investment by all parties engaged within the airport precinct. As a result, Auckland Airport rarely, if ever, uses the power in section 6(3) of the AAA. Auckland Airport's approach and longstanding practice to terminating its leasing arrangements is to engage constructively with the relevant party.

63. Despite this practice, the statutory power to terminate leases for airport purposes remains crucial. As submitted by NZ Airports:

- a. No evidence or explanation has been provided for the proposal to remove this power. It is not redundant or obsolete, and continues to have real, practical importance and justification today.
- b. Airports are long-term land owners that often need to react to unexpected regulatory change and shifting market conditions – which requires the flexibility to adjust airport layouts and infrastructure, including at short notice in response to aviation safety and security regulatory developments.
- c. Airports undertake long-term planning that involves leasing land to airport users, often on a long-term basis, for interim commercial purposes where that land is not yet required for

aeronautical use. The ability to terminate these leases when required for airport purposes creates an efficient system where aeronautical land can be used for interim purposes ahead of aeronautical development.

- d. Ultimately, section 6 is necessary to enable the safe and secure provision of airport services in an environment subject to rapid and unforeseen regulatory change, and to promote efficient use of land in that changing airport environment over time.
64. Auckland Airport has negotiated its current lease agreements based on a statutory right to terminate leases when necessary for airport purposes. Our experience is that the statutory right to terminate currently included in s6(3) of the AAA ensures that businesses understand the reality of operating at the airport and appreciate that the configuration of the airport precinct can be subject to change for a number of reasons related to airport purposes – including safety and security requirements, regulatory changes outside of Auckland Airport’s control, changes in aviation, trade and tourism market conditions, and the ability to meet demand and plan for expected growth.
65. Auckland Airport strongly urges MOT to retain the existing statutory power to terminate airport leases. In addition to the points made by NZ Airports, Auckland Airport emphasises that:
- a.  Although we can plan to the best of our ability given known information, and to align lease terms with known and anticipated regulatory changes, aviation regulation is dynamic and can change rapidly. The power in section 6(3) recognises that it is important for airports to have the ability to respond quickly in these types of circumstances, including the power to terminate leases.
 - b. A wide range of lessees operate their businesses in areas that impact on the safety and security of the airport (both aviation security and biosecurity). Auckland Airport works with each of these stakeholders, but we have overarching security and biosecurity responsibilities across the airport. Auckland Airport takes security seriously and has internal management mandates to ensure a culture where security is of paramount importance. Auckland Airport needs to be able to protect the secure environment at the Airport by having the right to terminate the leases of those operating on our land that do not hold safety, aviation security or biosecurity requirements in the same regard as Auckland Airport. Issues of safety and security go above and beyond simple compliance with all relevant legislation and the terms of the leases, and therefore relying on operators merely complying with the law and/or the terms of the lease may not achieve a secure environment. Auckland Airport needs to be able to protect the airside border and the wider Airport precinct from operators who do not have organisational structures and management that have these same mandates.
 - c. Auckland Airport has an unprecedented aeronautical infrastructure development plan underway. Although we do our best to ensure that lease expiry dates align with our anticipated development timeline, circumstances can and do change on a regular basis for a range of legitimate reasons. It is not always possible to perfectly predict when aeronautical development will take place, and the nature, timing and sequence of planned capital expenditure projects can often vary from that originally forecast. Leases are entered into at a range of times and often have lengthy terms – and it is entirely feasible that leases entered into before major market changes (such as the massive increase in passenger numbers at Auckland Airport between 2015 and 2018) did not contemplate that the space in question would be required for airport purposes in the way or at the time that it will be needed. The ability to terminate leases for airport purposes allows airports to appropriately adapt to changing circumstances, timeframes and capital priorities of airport users.

66. Without the statutory ability to terminate leases for airport purposes, Auckland Airport would be left with several untenable realities:

- a. It is entirely realistic that Auckland Airport would be unable to negotiate in an equivalent clause into lease agreements at any price. While counterparties acknowledge that a lawful right to terminate a lease exists, we do not expect that Auckland Airport will be able to negotiate this right in unilaterally. It is likely that lessees would deem a request for a termination right for airport purposes to be a burden on their business and would view the term as unreasonable. Commercial parties do not typically agree to things that could be detrimental to their businesses.

Ultimately, our priority is to ensure that the commercial decisions we make today are for the benefit of the airport tomorrow. Given our responsibility to future-proof the airport, develop infrastructure to cater for demand and growth, and ensure we can respond quickly to protect the safe and secure operation of the airport, we would be extremely reluctant to enter leases that do not give us rights to reclaim that property.

In short, Auckland Airport would be forced to choose between either entering a lease without the ability to terminate that lease if the space is required for airport purposes in the future (likely to be extremely problematic), or not entering that lease (also very problematic where the lease is for an aeronautical purpose that is important to the airport operation and to the travelling public, and where the section 6(3) termination right currently provides Auckland Airport with the necessary leverage to negotiate a relocation provision into the lease agreement).

- b. Even if Auckland Airport was able to get lessees to agree to the concept of a unilateral termination right, such a key term would come at a huge price for Auckland Airport. We expect that lessees would demand terms in relation to such a termination right that would be cost prohibitive to Auckland Airport. We have already experienced negotiations of this nature in relation to other rights in our leases. This would force Auckland Airport to decide whether to permit a lessee onto our land at a huge financial cost that would overly burden our financial stability, or to turn away that lessee. Again, forcing Auckland Airport to make this choice would be inefficient and problematic and we do not consider this to be a sensible proposition – particularly where the lease in question would serve an aeronautical function or otherwise provide benefits to airlines, the travelling public and/or freight operators.
- c. Further, even if it was possible for Auckland Airport to get lessees to agree to termination rights, no two leases would be negotiated on the same terms – even neighbouring leases that would be impacted by the same airport purpose requiring termination. In contrast, the current section 6(3) provides for a consistent termination that gives Auckland Airport the ability (if required) to terminate leases for all tenants impacted by the same airport purpose at the same time and on a consistent basis

67. If the power is removed from legislation despite the strong concerns that we have raised, we note that Auckland Airport would need to renegotiate numerous leases that were entered on the basis that a statutory power to terminate lease in accordance with section 6 existed. [REDACTED]

[REDACTED] There must therefore be a specific provision included in the final legislation that makes it clear airports retain the current statutory right to terminate leases for airport purposes for all leases entered into before the Bill is passed into law.

Subdivision exemption for long-term leases

68. As discussed above, Auckland Airport aims to provide lessees with certainty of tenure as much as possible given known information and planning forecasts (with the ability to rely on our section 6 right to terminate the lease if required for airport purposes).
69. Currently, section 6(8) of the AAA provides an exemption from parts of the Resource Management Act, Local Government Act and Public Works Act that apply to long-term leases. Without this

exemption, leases for a term over 35 years would be deemed to be subdivisions and, among other things, resource consent would be required for these types of leases.

70. We endorse the points made by NZ Airports that the current exemption in section 6(8) is not obsolete and must be retained.
71. As shown by the table above, Auckland Airport has a number of leases with final expiry dates extending well into the future [REDACTED]. These long-term leases are for a range of purposes and include multiple aeronautical leases where one airport user has a lease to exclusively occupy particular space at the airport for a long period of time.
72. Airports are long-term property owners and do not develop land for sale. Long-term leases are a feature of the airport environment and are not subdivisions by any sense of the word. Airports enter into long-term leases because we are long-term businesses and landholders, and because lessees often see value in basing their business at the airport for a lengthy period. The exemptions in section 6(8) continue to be necessary today to avoid triggering problematic requirements applying to subdivisions on a technicality that serves no efficient purpose and could lead to materially inefficient outcomes for lessees and Auckland Airport.

Capital expenditure consultation thresholds

73. Section 4C of the AAA requires Auckland Airport as a “specified airport company” to consult with all of our substantial customers on identified capital expenditure that will exceed 20% of the value of our identified assets. For Auckland Airport this threshold currently sits at \$282 million.
74. Consultation is a valuable tool that allows airports and airlines to work together to understand each other’s infrastructure requirements, so that airports can design and deliver necessary and affordable infrastructure with input from their key customers. As discussed above, Auckland Airport invests considerable time and effort into consultation with airlines and values the feedback and collaboration that takes place in those forums.
75. Auckland Airport is aware of the fundamental importance of our relationships with our airline customers and of the value that worthwhile engagement brings to these relationships. We consider that today’s dynamic aviation environment is best supported by regular and appropriate communication and we strive to achieve this on an ongoing basis with appropriately pitched engagement. For Auckland Airport, the legislated threshold does not inhibit meaningful engagement on a wide range of capital projects that fall below the threshold.
76. At the same time, it is important to ensure that formal consultation obligations do not impose inappropriate cost and operational impact on the participants. Auckland Airport therefore supports consultation thresholds that strike a balance between promoting collaboration on material expenditure and that facilitate the delivery of projects in a timely and cost-effective manner.
77. We anticipate that the \$30 million threshold proposed by MOT for capital expenditure consultations is based on the joint proposal put forward by BARNZ and NZ Airports in 2010. That proposal recommended that MOT amend the capital expenditure thresholds in the AAA using a combination of percentage based and fixed thresholds. At that time, the thresholds proposed were to set capital expenditure consultation at the lower of \$30 million or 20% of the value of an airport’s identified assets. This proposal was not seen as a priority by MOT at the time.
78. Although the \$30 million figure may have been appropriate in the past, we do not consider it to be appropriate today for Auckland Airport or our substantial customers. The construction industry has experienced significant headwinds in the form of suppressed supply of goods and labour since 2010, and our experience is that these factors have led to significant increases in the cost of construction. Similarly, as the size and scale of airports has increased over time, the value of capital expenditure that is considered material for any particular airport has changed too. This illustrates the inherent risks of relying on fixed sum thresholds that are unable to adjust to reflect changes due to inflation and changing construction costs, and which over time are no longer proportionate to the value of existing infrastructure at each airport.

79. At Auckland Airport, we are underway with a prolonged period of unprecedented expenditure that will require efficient and timely decision-making to deliver an ambitious infrastructure programme. Our concern is that if thresholds are maintained at the proposed level set out in the Bill, they will create a greater burden on airports and airlines to constantly consult on immaterial projects and hinder the delivery of timely infrastructure. Although we always strive to consult meaningfully on major capital expenditure, some of our large airline customers often tell us they do not want to be “over consulted” given the resource-intensive nature of ongoing robust consultation and collaboration on investment planning.
80. To safeguard against the threat of fixed sum thresholds failing to keep up with inflation and the cost of construction, and/or ending up materially out of balance with what is actually a substantial investment at individual airports, percentage-based capex consultation thresholds should be adopted. This allows the consultation requirement to remain proportionate to the value of existing infrastructure at all airports over time. We also recommend that the thresholds should be linked to the value of an airport’s non-land assets, as this links capital expenditure most closely to the value of existing aeronautical infrastructure without being impacted by an airport’s land values (which can vary considerably between airports and over time). A percentage threshold, rather than a fixed sum, is also the best way to ensure the thresholds remain proportionate over time and that the legislation is adequately future-proofed.
81. In 2013, Auckland Airport formally confirmed to BARNZ that we would, as a minimum, apply the section 4C consultation obligations to a threshold equating to 10% of the value of our non-land RAB assets (as that term is defined in the information disclosure requirements under Part 4 of the Commerce Act). At that time, this threshold captured projects with forecasted capital expenditure above \$76.2 million.
82. We continue to consider that this threshold – 10% of the value of an airport’s non-land aeronautical assets – is appropriate. For Auckland Airport, this would reduce the statutory consultation threshold from \$282 million to \$108 million.
83. We note that changes to the threshold will not change the constructive approach we have to capital expenditure consultation today, nor our ongoing efforts to promote meaningful and robust consultation on capital expenditure of importance and relevance to our key customers. As we do today, we will continue to recognise that dollar value is not the only measure of airlines’ interest in proposed development at the airport and will continue to meaningfully engage with substantial customers on a wide range of capital projects that fall below the legislated threshold.
84. Section 205(2) of the Civil Aviation Bill should be amended as follows:

205 Airport companies must consult concerning capital expenditure plans

[...]

(2) An airport company with annual passenger movements specified in column 1 of the table must consult with all its substantial customers in respect of identified capital expenditure (and all related capital expenditure) if the amount of the identified capital expenditure (and the amount of any related capital expenditure) will, or is likely to, within the following 5 years exceed an amount which is equal to 10% of the value of the non-land identified assets of that airport company at the commencement of the then current accounting period, specified in relation to those passenger movements specified in column 2 of the table.

Annual passenger movements of airport company	Amount
Less than 1,000,000	\$5,000,000
1,000,000 or more but not more than 3,000,000	\$10,000,000
More than 3,000,000	\$30,000,000

85. Auckland Airport also strongly supports the proposed section 205(3) and 205(4) of the draft Bill.

Aviation Security powers and responsibilities – dangerous goods

86. Auckland Airport is largely supportive of the proposals to improve airport security and create greater operational efficiency. As a general comment, we support legislative and regulatory provisions that involve clear delineation of responsibility for aviation safety and security matters.
87. In that regard, a small amendment is required to properly provide for the handling, temporary storage and disposal of dangerous goods once removed from passengers' bags at an aviation security screening checkpoint.
88. The volume of goods removed from passengers' bags at Auckland Airport is considerable. Avsec installed six new smart lanes throughout FY18 at the Auckland Airport international outbound security screening with each having a capacity to process up to 340 passenger per hour. Dangerous goods that are identified in passengers' bags by Avsec are confiscated. These goods often include spare batteries for power tools, filming equipment power banks, gas struts and camping equipment. The most commonly removed items are portable power banks used to recharge cellphones that are worth less than \$50.
89. The risks of storing, handling and disposing of these dangerous goods led ground handlers, airlines, Avsec and Auckland Airport to begin working together two years ago to develop an agreed best practice process for dealing with the growing volume of dangerous goods confiscated from passengers' bags.
90. After consultation with Dangerous Goods Consultants, four dangerous goods cabinets were installed by Auckland Airport outside each of the level 4 screening locations. Three of these cabinets are used as a managed segregation system for items to be held for 24 hours with the remaining cabinet used to store high value items for up to 48 hours. The following process was agreed to deal with dangerous goods:
 - a. Restricted items are stored in the transitional storage area for a maximum of 72 hours with dangerous goods required to be fully segregated based on class.
 - b. Avsec completes a form for any item removed from a passenger's bags and send a photograph of the item along with the form to the relevant passenger airline.
 - c. Avsec places the removed item (with its associated form) into the appropriate cabinet – either the high value cupboard for any item considered of high value or related to a high value piece of equipment (e.g. filming camera batteries, power tool batteries) or in the appropriate cabinet for the relevant type of dangerous good.
 - d. Airlines are responsible for collecting any items which they deem valuable enough to return to their passengers.
 - e. Auckland Airport staff empty the three segregated cabinets every 24 hours with the removed items passed onto a third-party electronic disposal firm for destruction.
91. During the development of this process the approach of Avsec management was that once they had removed the item from the passenger's bag, they considered that it was no longer their responsibility to ensure that the item was delivered to the relevant storage area. This can lead to inconsistencies in how these dangerous goods are stored and subsequently a break down in the agreed best practice process.
92. We are concerned that the provisions in section 140 of the Bill do not recognise the aerodrome taking on this disposal role. To ensure that the process established for dealing with dangerous goods is clear, Auckland Airport requests that an additional option be added to permit aviation security to deliver the dangerous goods to the aerodrome operator for disposal in instances where they choose not to dispose of the item themselves.

93. We support the drafting proposed by NZ Airports to address this issue, namely that section 140(4)(b) of the draft Bill be expanded to specify that aviation security officers may also deliver the item or substance to an aerodrome for disposal or destruction.
94. In the absence of such a provision, Auckland Airport will need to rely on Avsec to assume responsibility under clause 140(4)(c) for managing the removal and destruction function of the dangerous goods removed from passengers' bags.

Appendix: Summary of Auckland Airport's position on select proposals

Exposure draft proposal	Auckland International Airport's position
Remove section 4A of the AAA and the ability for airports to set charges	Retain the current wording in section 4A or Maintain the current power to set charges but remove words "from time to time as it thinks fit" – as per drafting suggested by NZ Airports.
Airline Alliance approval regime	Support proposed changes but recommend that the Commission assume responsibility for assessing airline alliance arrangements moving forward. Support MOT providing advice in situations requiring political considerations.
Changes to leasing provisions - remove ability to terminate leases under AAA for airport purposes, and remove exemption from subdivision requirements for long-term airport leases	Retain current ability to terminate leases in accordance with existing s6 of the AAA. Retain current exemptions from subdivision requirements.
Change to consultation thresholds of: Annual passenger movements Amount <1,000,000 \$5,000,000 >1,000,000 but <3,000,000 \$10,000,000 >3,000,000 \$30,000,000	Amend consultation thresholds to above 10% of the value of an airport's non-land identified assets.
Aviation Security – dangerous goods powers and responsibilities	Recommend adding requirement in section 140(4) of the Bill that would empower aviation security to deliver dangerous goods to the aerodrome operator for disposal – as per drafting suggested by NZ Airports.