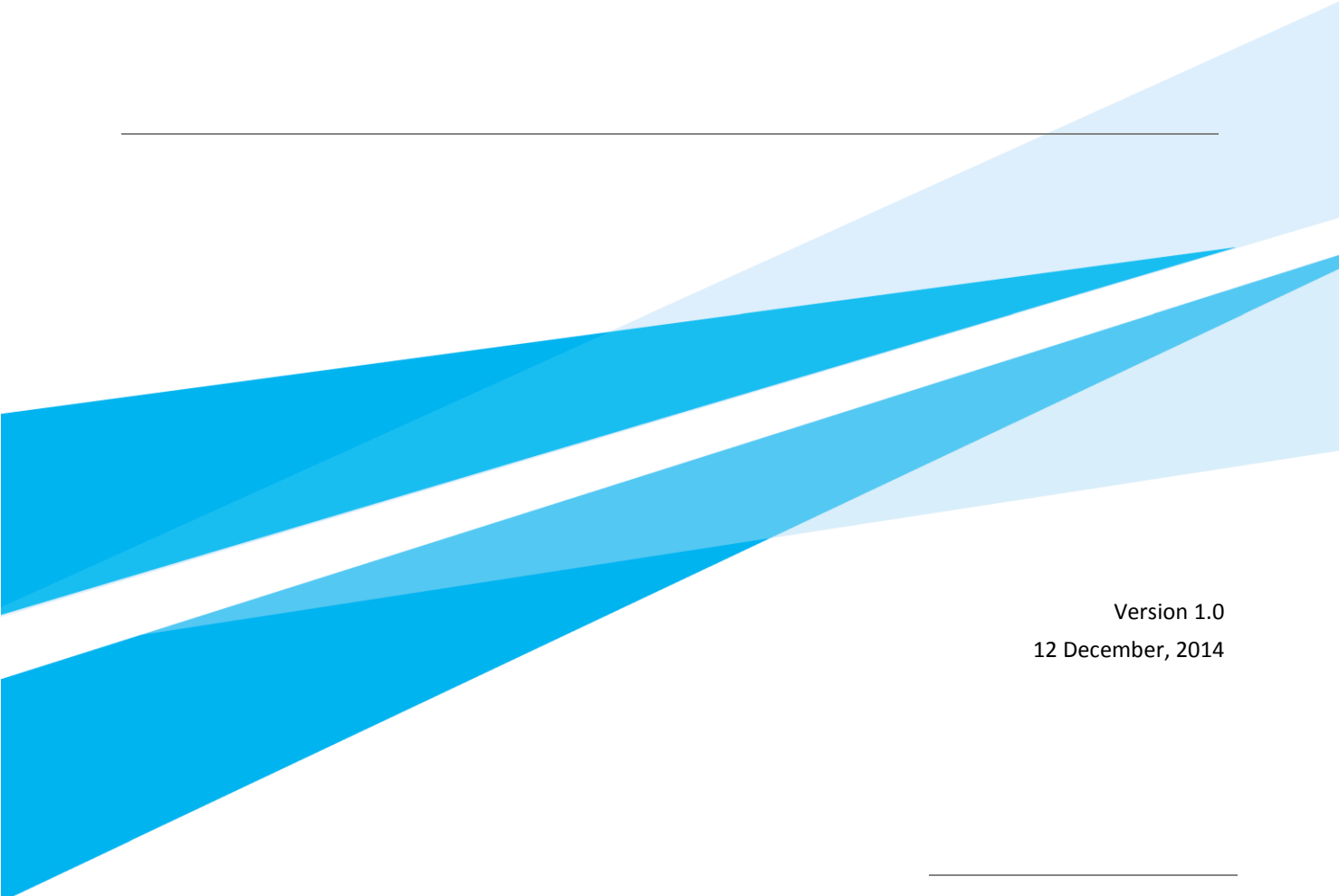

Airways New Zealand Queenstown lights proposal 2014

Public submissions document



Version 1.0
12 December, 2014

Contents

1	Introduction	3
2	Purpose	3
3	Air New Zealand Limited	4
3.1	Proposed changes to Airways' prices at Queenstown Airport	4
3.2	Timing of the price increases	5
3.3	Level of the proposed increase	5
4	BARNZ	7
5	Jetstar	8
5.1	Lighting project	8
5.2	Building upgrades	8
6	Qantas/Jetconnect (received late)	9
6.1	Night operation lighting proposal	9
6.2	Building upgrade proposal	10

1 Introduction

On 29 October 2014 Airways began a formal consultation for a proposed increase to the Queenstown aerodrome price for night operations and building upgrade. The detailed consultation document can be found at www.airways.co.nz

Airways sought feedback on the proposal set out in the document, inviting the public to provide feedback in writing by 3 December, 2014.

A total of four written submissions were received – all from members of the airline sector.

Between now and February 2015, Airways is considering each submission and will finalise its prices for the Queenstown aerodrome.

In early March 2015, Airways will publish a document responding to public submissions.

Any changes to Queenstown aerodrome prices will be announced on 3 March 2015.

2 Purpose

The purpose of this document is to present the four submissions received in a single document to make submissions easy to download, read and cross reference. Sections 3 - 6 of this document present a verbatim record of all submissions received, listed in alphabetical order.

3 Air New Zealand Limited

Queenstown Aerodrome Price Proposal – 29 October 2014

I refer to Airways 29 October 2014 *Queenstown aerodrome price proposal for night operations and building upgrade*.

Airways is proposing to invest \$2.2 million to provide lighting equipment and building space to accommodate additional power and lighting equipment for the lights, and \$4 million to provide additional building space for staff, resolve existing workplace health and safety issues (including asbestos), provide for a backup power service to improve reliability and to increase the structural strength of the building to the required earthquake standard.

Provision for lighting results from the successful safety case developed by airlines and Queenstown Airport to enable commencement of night flights within Queenstown Airport's existing resource consent for operations between 6am and 10pm. Airways is working to enable commencement of night flights from mid-2016.

It is noted that Queenstown Airport will also need to invest to facilitate the commencement of night flights. Airlines will also be required to fund this airport investment. The extent of this investment is not known at this time so it is not possible to get an accurate and complete picture of the additional costs airlines will face as a result of this development.

At the outset, Air New Zealand wishes to express its support for Airways' undertaking the proposed solution as outlined in the proposal. We appreciate that Airways has investigated alternative options to undertake this investment, but has determined that these deliver an inferior operational and financial outcome over the longer term. Air New Zealand agrees with this conclusion.

We do, however, have some concerns about the timing and level of increases proposed to support this investment.

3.1 Proposed changes to Airways' prices at Queenstown Airport

Airways is proposing to fund the investment and additional operating costs through increasing the Aerodrome Service price for all aircraft over 5 tonnes, with charges for aircraft in the 5-30 tonne range increasing 14% and charges for aircraft in excess of 30 tonnes increasing 29%. The difference reflects the fact that costs associated with lighting will only be charged to aircraft above 30 tonnes as aircraft under this weight are not currently equipped to be able to use the lights.

Setting aside the question of the increase in charges, which is discussed below, Air New Zealand supports differentiating between aircraft which are equipped to use the lights and those which are not on the basis of this weight break at this time.

3.2 Timing of the price increases

Airways is proposing that the price increases be implemented from the later of 1 April 2016, or when night operations begin.

Air New Zealand certainly supports any change to charges being implemented from the latter of those options.

However, Air New Zealand questions why Airways would seek to implement an increase from 1 April 2016 when the next price review will take effect from 1 July 2016, only three months later. This is particularly the case when Airways' analysis suggests that Queenstown Aerodrome Service prices will then be reduced from 1 July 2016. It seems illogical to increase prices on 1 April 2016 only to then reduce them 3 months later. Consequently the earliest that any price change should be implemented is 1 July 2016.

Furthermore, given activity growth at Queenstown it is likely that the forecast shortfall associated with the part-year operation (April-June 2016) of approximately \$0.2 million would be offset by a positive EVA outcome for Queenstown Aerodrome and Approach services. It is noted that Airways' FY2014 disclosures indicate that the DCM 2015 Budget outcome for Queenstown Aerodrome and Approach services is a positive EVA of \$0.915 million. Queenstown Aerodrome itself has a budget outcome of positive \$0.143 million.

Deferring the price change until 1 July 2016, when the next price review takes effect, will ensure that all relevant information can be taken into account when setting the charges.

3.3 Level of the proposed increase

Airways is seeking to increase Aerodrome Service prices in order to recover approximately \$1 million additional revenue in FY2017. Airways financial modelling assumes achieving EVA=0 for the building and lights investment each year of the 30 and 20 year (respectively) lives of the assets.

Air New Zealand questions Airways' focus on achieving EVA=0 from day one of the lives of the assets, particularly in the case of long-lived assets such as these. An alternative approach could be to consider mechanisms to achieve EVA=0 over a longer time-period rather than in every single annual period, and to achieve a flatter profile of charges through capitalising on activity growth.

As noted above, Air New Zealand also questions the extent of the increase proposed when Airways' own Budget forecast for Queenstown Aerodrome and Approach services suggests that the positive EVA generated by those activities in 2015 will be sufficient to fund the lighting and building investment. It is also noted that Airways' FY14 result was ahead of forecast – driven largely by activity being higher than forecast – delivering a positive EVA outcome across the "Domestic" business. It is appropriate for this positive return to be re-invested in the business in the form of contributing to investment such as that proposed at Queenstown.

Air New Zealand notes also that Airways' current EVA reporting framework states that "Airways has set its capital charge rate at the 75th percentile which is consistent with the Commerce Commissions [sic] Input Methodologies." Airways will be aware that the Commission has recently reviewed its approach to establishing the point estimate of the WACC and concluded for gas pipeline and electricity distribution businesses that the appropriate point estimate is the 67th percentile. The Commission has also indicated its intention to undertake further work in relation to the appropriate point estimate for airports subject to the Commerce Act regulatory framework.

This additional work on the appropriate point estimate of WACC for airports will have an impact on the capital charge Airways uses and consequently the level of prices required to achieve the required return (over whatever period is determined).

In conclusion, while Air New Zealand supports Airways proceeding with the lighting and building upgrade investment, there remain considerable uncertainties regarding the level of price increase (if any) required to fund that investment. Air New Zealand considers that the issue of pricing should be revisited as part of the price review due to come into effect on 1 July 2016. This will ensure that the uncertainties described above can be properly taken account of in establishing the final price.

4 BARNZ

Queenstown Lights and Buildings

Thank you for the opportunity to make a submission on the proposal for light and equipment upgrades to enable night operations into Queenstown and a building upgrade, and for the opportunity to discuss the proposal at a meeting on 19 November.

We have been engaged with Air NZ, Qantas, Jetstar and Virgin Australia over the proposal for the capital expenditure. They support the installation of the lighting equipment and the part of a new building to house it at a total cost of \$2.2m. BARNZ therefore also supports that capital expenditure.

The airlines also support the construction of a new facility to accommodate equipment, office space, meeting and training space and staff facilities at a cost of \$4.0m. The intermediate option of only refurbishing the existing equipment room would be taking a very short term view of expenditure. BARNZ therefore also supports this capital expenditure.

Your proposal also raises the question of pricing. The airlines have remained silent on the pricing part of the proposal. They believe it should be considered as part of the price setting for the 2016-19 pricing period because the equipment and buildings would come into operation only three months in advance of that pricing period. BARNZ supports that view, given that the intervening period is so short and the pricing consultations will be under way at the time. Furthermore, in this context we note that Airways revenue for 2013/14 was higher than expected at the time that prices were reset, and we believe that there is a good chance that this result will be repeated in 2014/15 and 2015/16.

5 Jetstar

Queenstown Lighting Proposal

Jetstar writes to you to provide feedback on the proposal for night lighting and building upgrades at Queenstown Airport. Please see the response below which sets out Jetstar's position.

5.1 Lighting project

Jetstar has reviewed the proposal and our preference is to implement night lighting and defer building works. Jetstar understands that overall system reliability for tower services would remain unchanged at 99.8%.

Under the lighting only option presented, Jetstar notes that an increase on current >30tonne aircraft costs is planned, however there is no increase in aircraft costs between 5-30 tonnes. Jetstar is strongly opposed to an unbalanced allocation of cost and notes that costs must be recovered from all users. Jetstar would be grateful to receive a revised pricing model prior to a funding decision being made by Airways.

Jetstar suggests that Airways may source funding from unspent capital expenditure budget from other projects, opposed to implementing a significant increase in Queenstown charges.

5.2 Building upgrades

In order to fully evaluate the need for additional building upgrades, Jetstar would require an in depth cost breakdown in order to adequately assess the capital expenditure required.

Jetstar also notes that the asset life stated in the Airways proposal is 20 years. Jetstar believes that a 40 year asset life is more appropriate.

6 Qantas/Jetconnect (received late)

Airways Queenstown Proposals

Firstly, thank you for providing an extension to Jetconnect on behalf of the Qantas Group to enable us to review this proposal in detail and to provide feedback to Airways. As you can appreciate both proposals are important to our operation since we commenced international services to Queenstown on behalf of Qantas from March 2014. Please see Jetconnect and Qantas' response to Airways proposal.

6.1 Night operation lighting proposal

We have reviewed Airways proposals and whilst Qantas has not confirmed its intention to commence night operations into and out of Queenstown at this time, the upgrade of the runway lighting to enable night operations will enable each operator to have the opportunity to consider if they wish to take advantage of night operations.

Having considered the lighting only option, we note Airways has proposed that there is an increase to the existing charges for aircraft greater than thirty (30) tonne; however there is no increase to aircraft charges where the aircraft weight is between five (5) – thirty (30) tonnes. We do not support an unequable allocation of costs associated with the proposed lighting project. Given Queenstown Airport has extensive operations completed by aircraft of between five (5) – thirty (30) tonnes it is imperative that the costs associated with this proposal are recovered from all airport users whether they chose to have night operations or not at this point in time. To disadvantage one group of Airport users through a cost recovery mechanism is in contrast to the philosophy of a fair and equitable user pays model and potentially could facilitate unfair competitive advantage.

If Airways could please provide a revised pricing model which reflects the equitable apportionment of costs across all aircraft movements prior to Airways making a final funding and pricing decision.

Another concern is the intent to increase charges only three months shy of the expiry of the current pricing period. It would more reasonable and practical to include any costs for this project as part of the overall pricing adjustment for the next pricing period.

We would also like to propose that Airways explore the contributions to be made from other key stakeholders of night flights into Queenstown in particular Queenstown Tourism and the associated tourism infrastructure in Queenstown. These are key stakeholders who will directly benefit from the forecasted incremental increase in passengers traveling to/from Queenstown as a consequence of having the opportunity to facilitate night flights and it seems fair and reasonable that there should be a contribution from these stakeholders in addition to the airline operators.

Finally, we would like to understand if Airways have considered self-funding the lights for night operations from its own unallocated or any delayed capital expenditure budget. This would be a more acceptable proposal to airlines and other community stakeholders rather than imposing significant increases to Queenstown Airways charges.

6.2 Building upgrade proposal

To ensure our Airlines can make an informed decision regarding the proposed building upgrade at Queenstown, we request an in depth cost breakdown in relation to the proposed works. This cost breakdown will enable us to assess the capital expenditure proposed and the potential impact on our operations if the works are not progressed.

However, it is understood that the overall system reliability for tower services would remain unchanged at 99.8% without the building work being completed. Therefore if there is a capital expenditure priority it is a preference that night lighting is given the priority and the building works to the Tower are deferred.

Another element that is important is the timing of the pricing increases related to lumpy infrastructure builds that materially increase charges. It is not an efficient or equitable process to calculate the charges only over a short 3 year recovery period, rather pricing should be smoothed over a much longer period of time to avoid a pricing shock to the industry. This is particularly relevant at Queenstown, being a leisure and seasonal destination, whereby substantial cost increases reduces demand, lowering the revenue and increases the charges again, thus creating a negative cost recovery cycle for all parties involved.

The timeline and information provided for the consultation for these substantial projects has been insufficient to provide a well-informed response.