

Discussion Paper Inviting Submissions

Options for Further Work on Airport Regulation Proposed for 2008/09

The three options for further work are as follows:

- 1) Do further work on both streams as directed by Cabinet;
- 2) Limit the scope of further work to an assessment only, of whether additional airports should be subject to regulation under the Commerce Act; or
- 3) Do not proceed with further work at this time.

Background

On 14 November 2007 the Cabinet Policy Committee agreed that the Ministry of Economic Development (MED) will lead further work in 2008/09 to consider:

- whether additional airports to Auckland, Wellington and Christchurch (AIAL, WIAL, CIAL) should be subject to regulation under the Commerce Act;
- whether other forms of regulation should apply to regulated airport companies under the Commerce Act; and
- invited the Minister of Transport and the Minister of Commerce to report to the Cabinet Economic Development Committee on the outcome of this work by 30 June 2009.

This discussion paper seeks your feedback on three specific options for carrying out the further work on airport regulation as set out above, including your assessment of the benefits and costs of each option to your organisation, and to the wider New Zealand economy.

Option 1: Do further work on both streams as directed by Cabinet

This option would involve engaging a consultant to assess:

- i. whether airports in addition to AIAL, WIAL and CIAL should be subject to regulation under the amended Commerce Act; and

- ii. whether other forms of regulation should apply to regulated airport companies under the Commerce Act.

As outlined above, this option was agreed by Cabinet in November 2007. The report back date would be 30 June 2009.

A review under this option would not be aimed at identifying any evidence of abuse of market power by monopoly airport companies, but would take a conceptual approach in identifying the appropriate form of regulation for all international and potentially major domestic airports in New Zealand. If any recommendations for further regulation were to come out of this review, these would be considered by Ministers directly.

The main advantage of this option is that it takes a holistic approach to airport regulation, which will encompass all international and major domestic airports. Relative to a Part 4 Commerce Act inquiry, this type of review would be completed over a shorter timeframe.

However this option creates the potential for ongoing business and investor uncertainty over the period of the review. Notably one of the overarching objectives of the Commerce Act reforms is to promote business certainty and incentives to invest.

The proposed new regime under the Commerce Act for AIAL, WIAL and CIAL is a significant change to the regulatory framework for the regulator and for these airports, and so will take some time to be implemented. Given this, an overlap in the timing of the development of the new regime and the proposed further work would create additional costs for airport companies going forward.

Given the recent decisions on the regulatory regime for AIAL, WIAL and CIAL, there will also be costs associated with the uncertainty about the final form of any regulatory regime for airports. A conceptual analysis without any experience of the effectiveness of the new information disclosure regime would have its limitations.

In addition, once the proposed information disclosure with binding input methodologies and price monitoring regime for the three major international airports is established, sufficient information should be available to make an informed decision on whether and how additional forms of regulation are warranted. This may be preferable to relying on a conceptual analysis to assess the need for further regulation. Thus there may be little value in reviewing airport regulation for the AIAL, WIAL and CIAL in particular, in the interim.

Option 2: Limit the scope of further work to an assessment only, of whether other airports should be subject to regulation under the Commerce Act

This option would involve seeking Cabinet approval for the proposed scope of the review to be limited to an assessment of whether additional airports should be subject to regulation under the amended Commerce Act. The second limb of the review, whether other forms of regulation should apply to regulated airports under the

Commerce Act, would not be carried out. The report back date for this option would still be 30 June 2009.

The main advantage of this option is that it still allows for the gathering of information and assessment of any need for regulation, of second tier airports in New Zealand. Hamilton, Palmerston North, Dunedin and Queenstown Airports are significant regional airports that contribute to tourism and economic growth yet very little is known about whether regulation of any of second tier airports is warranted.

Another advantage of this option, relative to option 1, is that it allows for the new regulatory regime for AIAL, WIAL and CIAL to become established, and thus will allow for a more informed assessment of the effectiveness of the new regime in meeting the Government's regulatory objectives.¹ Option 2, relative to option 1 is likely to be better for business and investor certainty as the airport companies are operating within the parameters of a known regulatory environment.

In addition, as part of the new regulatory regime for AIAL, WIAL and CIAL the Commission will be required to review the pricing behaviour of those airports after the next price reset in 2012. This review will assess the efficacy of the price monitoring regime, and whether further regulation is warranted and will be informed by the information collected under the new regime in the period to 2012.

A disadvantage of option 2 is that it will ignore any assessment of whether further regulation is required for the three major international airports, in the context of a comprehensive study of all other regional airports. Thus, there is potential with this option for there to evolve, a piecemeal approach to airport regulation. This may not be a significant issue however, as the second tier airport companies are much smaller than AIAL, WIAL and CIAL.

Another disadvantage of this option is that should the 2012 Commission inquiry into airport pricing behaviour show that the new regime has not proved effective in reducing the potential for the exercise of market power by AIAL, WIAL, CIAL, further regulation, such as negotiate/arbitrate, would unlikely be applied until the 2017 price reset by airports.

Option 3: Do no further work at this time

Option 3 involves seeking Cabinet approval to discard the programme for further work on these two work streams as described.

¹ The objectives of the review have been to:

- Provide an efficient and credible regime to address the potential to exercise market power in markets where competition is not possible;
- Improve clarity, certainty, timeliness and predictability for businesses;
- Tailor the regime to New Zealand's small size (with small firms and limited resources);
- Provide specifically for incentives to invest in infrastructure. Certainty is considered a pre-requisite for this.

The advantages of this option are as described in the two options above, namely it:

- reduces potential for ongoing business and investor uncertainty over the period of review;
- allows time for the new regulatory environment for AIAL, WIAL and CIAL, of information disclosure with binding input methodologies and price monitoring, to become established. There may be little value and some redundancy in reviewing airport regulation for these airports in particular, when changes are being proposed to the legislative framework governing these airports; and
- avoids duplication of work as a further review will be carried out by the Commission, as directed by Cabinet, of airport behaviour after the next price reset in 2012, to assess the efficacy of the new regulatory environment, and whether further regulation is warranted.

The main disadvantages are that:

- it does not allow for the gathering of information and assessment of any need for regulation of second tier airports in New Zealand;
- should the 2012 Commission inquiry into airport behaviour show that the new regime has not proved effective in reducing the potential for the exercise of market power by AIAL, WIAL, CIAL, further regulation, such as negotiate/arbitrate, would likely not be applied by users until the 2017 price reset by airports.²

² In stating this however, the outcome of any review cannot be predetermined.