MINISTRY OF BUSINESS,
INNOVATION & EMPLOYMENT
HIKINA WHAKATUTUKI

Regulatory impact statement

Amendments to strengthen the regulatory regime for major international airports

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Agency disclosure statement

This regulatory impact statement has been prepared by the Ministry of Business, Innovation and Employment.

It provides an analysis of options to ensure that the information disclosure regime for regulated international airports under Part 4 of the Commerce Act 1986 continues to operate effectively.

This analysis is undertaken with the perspective that the information disclosure regime for international airports has been operating well to date. This is based on the Commerce Commission's summary and analysis of airport information disclosures.

It assumes that the Commerce Commission's oversight combined with the threat of further regulatory intervention is what ensures that airports act consistently with the Part 4 purpose. This assumption is based on conversations that we have had with airports and airlines around airport behaviour, and the response of Wellington and Christchurch International Airports to the Commerce Commission's section 56G reports.

The analysis is based on addressing risks, rather than problems that have manifested themselves to date and the changes proposed are not expected to have immediate impacts. It seeks to address issues with how legislation is currently drafted and to provide a safety net in case the Commerce Commission's approach to assessing airport performance or market conditions change.

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Contents

Agency disclosure statement **2**
Contents **3**
Executive summary **4**
1 Status quo **6**
How airports are currently regulated under Part 4 7
Process for changing the type of regulation for an already-regulated airport 8
Context of the review 9
2 Problem definition **10**
Issue 1: The Commerce Commission's ongoing power to consider the effectiveness of information disclosure 10
Issue 2: Cost and difficulty of the process for changing the type of regulation that applies to airports 11
3 Objectives **13**
4 Options and impact analysis **14**
Issue 1: The Commerce Commission's ongoing power to consider the effectiveness of information disclosure 14
Issue 2: Cost and difficulty of the process for changing the type of regulation that applies to airports 16
5 Summary of analysis **20**
6 Consultation **24**
7 Conclusions and recommendations **25**
8 Implementation plan **26**
9 Monitoring, evaluation and review **27**

Executive summary

New Zealand's three major international airports are subject to information disclosure regulation under Part 4 of the Commerce Act 1986 (**the Act**).

The Ministry of Business, Innovation and Employment has conducted a review of this regulatory regime, in consultation with the public and with stakeholders. Given the light-handed nature of the information disclosure regime, a key consideration was whether current settings provide sufficient incentives for airports to behave in a way that is consistent with the purposes of Part 4 regulation.

The review concluded that information disclosure has largely worked well to date, and there is not currently a need to change the type of regulation to which major airports are subject. However, officials did identify two areas where the current regime could be improved, to ensure it can operate effectively both now and in the future:

- **Lack of clarity about the content of summary and analysis reports**: The Commerce Commission has previously included, as part of its one-off section 56G reports, analysis and conclusions as to whether information disclosure is being effective at achieving the Part 4 purpose. However, it is not clear in the Act that the Commission has the power to do this in regular section 53B summary and analysis reports; and in any event, the Act does not require the Commission to do so. This analysis is important for observers, including Ministers and the public, to understand whether information disclosure is working as intended.
- **Unduly onerous process for changing the type of regulation that applies to airports**: The current process for changing the type regulation that applies to an already-regulated airport is complex and expensive, which could reduce the effectiveness of the threat of further regulation on which information disclosure relies. In particular:
    - The full Part 4 inquiry process for investigating the need for regulation is likely to be unduly onerous for the investigation of the costs and benefits of changing the type of regulation for airport services that are already subject to regulation under Part 4, because it would include re-consideration of whether regulation was justified at all. This may lead to higher-than-necessary costs, and may reduce the effectiveness of the threat of further regulation.
    - Legal advice indicates that the Act's prescribed legislative process for imposing regulation under Part 4 (Order in Council) is not suitable for altering the type of regulation that applies to an already regulated good or service specified directly in the Act, for example the imposition or removal of additional types of regulation. As a result, changing the type of regulation that applies to an already regulated airport would require a legislative amendment.

These issues have not yet had any impact on the regulatory regime, but have the potential to undermine the effectiveness of the regime in the longer term.

To address these issues, officials propose the following changes to the Act:

- amending the Act to make it clear that the Commerce Commission can, as part of its summary and analysis reports under section 53B of the Act, undertake analysis and reach conclusions as to whether information disclosure is effective at achieving the Part 4 purpose;
- removing unnecessary steps in the Part 4 inquiry process for investigating the need to change the type of regulation that applies to an already-regulated airport; and

- clarifying in the Act that changes to the type of regulation for an already-regulated airport can be effected through an Order in Council.

This is the preferred approach because the proposed changes:

- enable a comprehensive analysis of how well the regime is working, without the need to completely reconsider whether regulation of the specified airports is required in the first place; and
- provide a proportionate and consistent process for imposing further regulation if airports do not meet the Part 4 purpose.

We have recently identified a subsequent issue around how additional airports could be regulated if it was considered that a certain airport had market power. If we consider further amendments are required to address this issue we will report back with a further Cabinet paper and Regulatory Impact Statement.

1 Status quo

1. The specified airport services[1] provided by Auckland, Wellington and Christchurch international airports (**airports**) are regulated under Part 4 (**Part 4**) of the Commerce Act 1986 (**the Act**). Part 4 regulates suppliers of goods and services in markets where there is little or no competition.[2]

2. The purpose of Part 4 is to promote the long-term benefits of consumers by promoting outcomes in regulated markets that are consistent with the outcomes that would have been produced in competitive markets.

3. There are three types of regulation that can be imposed on a business under Part 4:

   a. ***Information disclosure regulation*** requires sufficient information to be readily available to interested persons to assess whether the purpose of Part 4 is being met. This is the 'lightest' type of regulation provided for under Part 4 and applies to all regulated businesses. The idea behind this regime is that the threat of further regulation, if the purpose of Part 4 is not met, acts as an incentive on suppliers to act consistently. Airports are only subject to information disclosure, but the Act currently does not provide mechanisms for airports to move between these different types of regulation.[3]

   b. ***Negotiate/arbitrate regulation*** requires suppliers and their customers to seek agreement through negotiation on prices and quality standards, and provides for binding arbitration if negotiation is unsuccessful. This is the next step up from information disclosure and this type of regulation is not currently applied to any industry in New Zealand.

   c. ***Price-quality regulation*** requires suppliers to cap prices or revenues, and meet minimum quality standards. These caps and quality standards are determined by the Commission. In addition to information disclosure, this type of regulation applies to a number of electricity lines businesses (in particular, those that are not community-owned), as well as Transpower and gas pipelines. This is the most intensive type of regulation under Part 4.

4. The Commerce Commission (**the Commission**) sets input methodologies – the upfront rules, requirements and processes that apply to regulated services.

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[1] Specified airport services comprise services relating to aircraft and freight activities, airfield activities and specified passenger terminal activities. They do not include car parks, taxis, buses, retail facilities, etc. although the coverage of specified airport services could be expanded by Order in Council.

[2] The markets regulated under Part 4 are: Electricity lines businesses, gas pipeline businesses, and specified airport services. Each of these regimes has particular provisions specifying what type of regulation applies. Telecommunications and dairy markets are regulated under separate Acts.

[3] In contrast, the Act enables price-quality regulation to also be applied to electricity lines businesses that are currently only regulated by information disclosure.

How airports are currently regulated under Part 4

Airports must produce information disclosures annually and following each five-yearly price-setting event

5. The current information disclosure regime for airports was introduced in 2010. The purpose of the information disclosure regime is to promote the efficient operation of the market by ensuring that major airports make publicly available reliable and timely information about the operation of their businesses.

6. A range of information must be disclosed, in accordance with the input methodologies set by the Commission and the Commission's information disclosure determination. This enables a wide range of people to be informed about factors such as profits, costs, asset values, price, quality, security and reliability of the services.

7. Under the regime, airports are required to produce information disclosures annually, and following each price-setting event (which occur approximately every five years). The first price-setting event under the regime was in 2012. When airports engage in a price-setting event, they are required to publish their financial information such as the airport's pricing methodologies, forecast revenue requirements, and forecast demand.

8. Information disclosure combines with other components of airport regulation under Part 4 to create incentives for airports to perform in accordance with the Part 4 purpose, and particularly to constrain monopoly profits. These components are:

    a. the Commission's summary and analysis of airport information disclosures, in which it assesses airport performance and (currently) reports on whether the Part 4 purpose is being achieved;

    b. the Commission's ability to, at the request of the Minister or on its own initiative, perform a detailed inquiry into the costs and benefits of imposing a different type of regulation on particular airports; and

    c. the Government's ability to, on the basis of the Commission's inquiry and recommendation, impose a different type of regulation (such as negotiate/arbitrate or price-quality regulation) on particular airports.

9. These incentives include the threat of further regulation if airports are observed to be acting in a way that is not in line with the Part 4 purpose.

Summary and analysis reports are then published by the Commerce Commission

10. Following each information disclosure, the Commission reviews the information disclosed and, based on this information, publishes **summary and analysis reports** under section 53B of the Act. These reports are made publicly available on the Commission's website. The purpose of summary and analysis reports is to promote greater understanding of the performance of individual airports (including their performance against the Part 4 purpose), their relative performance, and the changes in performance over time.

11. Following the first price-setting event under the new provisions in 2012, the Commission was also required (under section 56G of the Act) to report back to Ministers on whether information disclosure regulation was meeting the Part 4 purpose detailed above, in respect of each airport being regulated. The section 56G reports have previously assisted

officials and Ministers in their respective assessments of the effectiveness of information disclosure, and to consider whether any regulatory changes might be necessary.

12. These **section 56G reports** for each airport were a one-off statutory requirement and will not be carried out following future price-setting information disclosures. Going forth, the Commission is only required to undertake summary and analysis reports on the information disclosed by each airport.

13. To date, the Commission has also published two summary and analysis reports following the initial section 56G reports that found information disclosure was only effective for Auckland Airport, and that Wellington and Christchurch Airports were targeting excessive profits. Wellington and Christchurch Airports subsequently amended their intended pricing and disclosure methodology, respectively, following the Commission highlighting issues with these in the section 56G reports.

Process for changing the type of regulation for an already-regulated airport

A Part 4 inquiry is required for investigating the need for change

14. Part 4 of the Commerce Act contains an inquiry process under which the Commission can investigate the state of competition in an industry and, if warranted, regulation can be imposed through Order in Council. The Commission can instigate an inquiry of its own volition, or may be directed to do so by the Minister of Commerce and Consumer Affairs.

15. If, through this process, the Commission identifies that a good or service would benefit from regulation, then it must determine whether the benefits of regulation would materially exceed the costs. It must also determine how the goods or services should be regulated, and develop input methodologies for the good or service.

16. Following an inquiry the Commission makes a recommendation to the Minister as to whether and how the good or service should be regulated. The Minister can then make a recommendation to the Governor-General to make an Order in Council imposing regulation.

17. This inquiry process was developed primarily to enable unregulated industries to be brought into the Part 4 regime.

18. Under the Act, a full Part 4 inquiry is currently required for changing the type of regulation that applies to airports, but not necessarily for changing the coverage of airport services regulated under the Act[4]. The requirements are the same for investigations into goods and services that are currently unregulated, as for already-regulated airports (that is, for which a previous inquiry has already found there is little competition and a net benefit from regulation).

Legislative amendment would be required to effect any changes

19. Part 4 allows for regulation to be imposed on a good or service by Order in Council, following a Part 4 inquiry by the Commission. The Order in Council specifies the goods or

[4] Additional airport services at already regulated airports can be included by Order in Council under the special process specified in section 56A of the Commerce Act.

services that are to be regulated, and the type of regulation that applies – i.e. information disclosure, negotiate/arbitrate, or price-quality regulation.

20. This process can be used to apply any type of regulation to an unregulated good or service, but as presently drafted in the Act, it cannot be used to apply more or less regulation to businesses already regulated under Part 4, despite there being an Order in Council process for including additional airport services. As such, the current Order in Council process could not be used to apply negotiate/arbitrate or price-quality regulation to airports.

21. However, there are specific legislative mechanisms in place for a different type of regulation to be imposed on certain regulated services under Part 4, such as electricity lines and gas pipeline businesses. There is no such mechanism in the Act to impose different types of regulation for already-regulated airports, which would require legislative amendment to make any changes.

Context of the review

22. MBIE began a review of the regulation of specified airport services under Part 4 in 2014, following a long history of debate about whether airports should be subject to a light-handed regulatory regime (information disclosure) or a more heavy-handed regime (i.e. negotiate/arbitrate). The overall purpose of the review was to ensure that airport regulation operates effectively both now and in the future.

23. In 2015, the Minister of Commerce and Consumer Affairs decided that airports would remain subject to information disclosure only. This was determined on the basis that the overall purpose of Part 4 appeared to be largely met. It was agreed that the Commerce Commission and officials would continue to actively monitor the performance of Part 4.

24. The later stages of the review focused on potential improvements to the information disclosure regime to ensure that it could continue to work effectively in the future. This included making sure the Commission has adequate powers to review information disclosed by airports and assess how well they meet the Part 4 purpose, and ensuring there is a process for changing the type of regulation applied to airports if required. In early 2016, targeted consultation took place and options were developed taking account of this feedback.

25. Recently, we have also identified a potential issue around how other airports in New Zealand could be regulated under the regime if it was considered that another airport had market power. It is not specified in the Act what the process is for extending regulation to include a presently unregulated airport.

26. Initial legal advice indicates that legislative amendment would be required to impose regulation on an airport that is not specified in the Act, which would be out of line with the existing processes in the Act and the proposals in the paper. A tidy-up would be beneficial as this potential issue relates to the process by which additional regulation can be imposed. We are seeking further legal advice on the possible options to address this issue. If we consider further amendments are required to address this issue, we will report back with a further Cabinet paper and Regulatory Impact Statement.

2 Problem definition

27. As outlined above, the overall information disclosure regime has worked well to date for specified airport services. However, we have identified two issues with the current legislative settings which may inhibit the effectiveness of information disclosure for specified airport services in the future.

    - ***Issue 1***: It is not explicit in the Act that the Commission has the power, as part of its regular summary and analysis reports, to undertake analysis and reach conclusions as to whether information disclosure is effectively promoting the Part 4 purpose. In any case, the Commission is not required to do so.
    - ***Issue 2***: If information disclosure is found to be ineffective for an airport (for example, an airport is not effectively limited in its ability to extract excessive profits), the process for changing the type regulation is expensive and onerous, creating a barrier that may reduce the threat of further regulation. The two main impediments are:
        - The requirement that a full Part 4 inquiry be undertaken, an expensive process that may be unduly onerous for investigating the merits of changing the type of regulation.
        - The Act's process for imposing regulation (Order in Council) would not be appropriate for changing the type of regulation that applies to already-regulated services, meaning that the imposition of further regulation would require legislative amendment.

28. These issues are set out in more depth below.

29. The combined effect of these issues is to weaken the regulatory threat which supports information disclosure to be effective. There is therefore a risk that airports could, in future, act contrary to the Part 4 purpose with minimal fear of regulatory intervention.

30. The impact of these issues on wider stakeholders (such as air travellers and the wider public) is relatively minor. Airport charges form a small part of airlines' charges to customers, and are generally not significant compared to other factors (such as competition within the airline industry). Moreover, evidence indicates that the current regulatory regime is working well under current conditions.

31. However, it is important to ensure that effectiveness of the regime is maintained so that the threat of further regulation is credible.

Issue 1: The Commerce Commission's ongoing power to consider the effectiveness of information disclosure

32. For information disclosure to work effectively, the Commission needs sufficient resources and powers to analyse and report on the information disclosed by airports following price-setting. The Commission currently performs this role through its summary and analysis reports.

33. Information disclosures are long and complex documents, and can be difficult for non-experts to analyse and interpret without the benefit of expert commentary. Even regulators may need to "look behind" the disclosed information before they can form a

view on whether airports are meeting broader objectives such as those contained in the Part 4 purpose.

34. The Commission is of the view that it can analyse and report on whether information disclosure is promoting the Part 4 purpose as part of its summary and analysis reports. However, it is not explicit in section 53B (the provision for summary and analysis reports) that the Commission can analyse and report on whether information disclosure is meeting the Part 4 purpose. Section 53B simply states that the Commission must "publish a summary and analysis of [the] information [disclosed by suppliers] for the purpose of promoting greater understanding of the performance of individual regulated suppliers, their relative performance, and the changes in performance over time."

35. The risk of legal challenge to the Commission's approach if it was to analyse whether information disclosure was meeting the Part 4 purpose as part of its summary and analysis reporting is low over the medium term, but possible given that Part 4 regulation has high stakes and a litigious history. It is also possible that the Commission, which is an independent Crown entity, might at some future date unilaterally cease to provide advice on the effectiveness of information disclosure even if it was considered appropriate – either due to a change of priorities, personnel, or constrained resources.

36. If the Commission was prevented from looking at the effectiveness of information disclosure in its summary and analysis reports, this might limit the analysis of information about airports' performance and make it difficult for Ministers and other interested parties to form a view on whether information disclosure was effectively promoting the Part 4 purpose. The resulting reduction in effective regulatory oversight would likely have an adverse impact on the effectiveness of the information disclosure regime as a whole.

Issue 2: Cost and difficulty of the process for changing the type of regulation that applies to airports

37. The current process for changing the type of regulation, in particular imposing further regulation on airports, is expensive and complex, and may constitute a barrier that reduces the effectiveness of the threat of further regulation. There are two key elements contributing to this: an inability to target a Part 4 inquiry at the question of more or less regulation, rather than repeating a full inquiry into whether regulation is justified at all; and the need for a different type of regulation to be imposed via legislative amendment, rather than an Order in Council process.

Process for a Commission inquiry investigating the need to change the type of regulation applying to airports

38. The Act currently does not differentiate between Part 4 inquiries into goods or services that are not yet regulated, and those which are already regulated. This means that the Commerce Commission, when investigating the need for a different type of regulation to be applied to already-regulated airports, must begin by:

    a. repeating the inquiry into whether there is competition in the market in which the specified airport service is supplied; and

    b. repeating the assessment of whether the benefits of imposing Part 4 regulation on the good or service materially outweigh the costs of regulation.

39. These preliminary aspects of a Part 4 inquiry are relevant to inquiries into unregulated goods and services, and in situations where a regulated service ceases to hold a monopoly

position, or where concerns about monopoly behaviour and profits have reduced. However, these aspects will tend to be unwarranted where it is already accepted that there is limited competition and that Part 4 regulation (of some form) is appropriate.

40. The most likely situation in which an inquiry would be undertaken in respect of an airport is where information disclosures reveal strong evidence that an airport is extracting excessive profits. It is unlikely that such an inquiry would find that there is now significant competition in the market. It is also unlikely that government would choose to remove Part 4 regulation altogether in this situation. Rather, the main question that (from a practical perspective) needs to be answered by such an inquiry would usually be whether any of the additional regulatory tools under Part 4 would have net benefit (or if the government would need to investigate alternative regulatory tools.)

41. Unnecessary aspects of the inquiry process are of concern because a full Part 4 inquiry is expensive. While it is difficult to estimate the cost of a specific Part 4 inquiry, as it will vary from inquiry to inquiry depending on the complexity of the issues, the Commission has previously estimated the cost of a Part 4 inquiry into Eastland Port at $2.2 million (including $150,000 to establish the degree of competition in the market), and the cost of an inquiry into gas metering at around $1 million.

42. As well as generating unnecessary cost, the perceived barrier of a full Part 4 inquiry's expense and length has the potential to make further regulation seem like a remote possibility rather than a credible threat. This undermines the regulatory threat on which the information disclosure regime depends.

Legislative process for changing the type of regulation

43. The current Commerce Act process provides that Part 4 regulation, where deemed necessary, will be imposed by Order in Council. Legal advice suggests that this process would, in practice, be unsuitable for changing the type of regulation that applies to already regulated goods or services, as secondary legislation (such as an Order in Council) cannot be used to amend or override primary legislation unless it was clearly Parliament's intent to enable it to do so.

44. The Commerce Act currently states that specified airport services are subject to information disclosure only. As presently drafted, it is not clear from Part 4 that Parliament intended for this to be able to be overridden by the Order in Council process.

45. This means that if the Commission did make a recommendation that additional regulation would have material net benefits, implementing the change in the type of regulation would likely require legislative amendment to the Act. Officials understand that this situation is the result of an oversight, and not in line with the original policy intent of Part 4.

46. For other Part 4 regimes, such as certain electricity lines businesses regulated by information disclosure only, the Act specifies how 'exempt status' can be lost for these businesses and price-quality regulation can be applied (through an Order in Council). There is no such provision for the airports regime in the Act.

47. The time and political process required to make legislative changes, if it was recommended that changes to the type of regulation were necessary, further undermine the threat of further regulation if an airport acts inconsistently with the Part 4 purpose.

3 Objectives

49. The purpose of Part 4 of the Act is to:

    promote the long-term benefit of consumers in markets referred to in section 52 by promoting outcomes that are consistent with outcomes produced in competitive markets such that suppliers of regulated goods or services—

    (a) have incentives to innovate and to invest, including in replacement, upgraded, and new assets; and

    (b) have incentives to improve efficiency and provide services at a quality that reflects consumer demands; and

    (c) share with consumers the benefits of efficiency gains in the supply of the regulated goods or services, including through lower prices; and

    (d) are limited in their ability to extract excessive profits.

50. The overall aim of economic regulation is to promote the long-term benefits of consumers.

51. Information disclosure contributes to this by ensuring that sufficient information is readily available to interested persons to assess whether the purpose of Part 4 is being met.

52. The options below are judged against the following criteria:

    a. Interested parties, including Ministers, have sufficient information to assess whether the purpose of Part 4 is being met.

    b. There is a credible threat of further regulation if the Part 4 purpose is not being met.

    c. Regulatory uncertainty is minimised, notwithstanding the above need for a credible threat of further regulation.

    d. The operation of the regime is cost effective and timely.

4 Options and impact analysis

53. The options are:

    Issue 1

    - Option 1: Retain the status quo – the Commerce Commission continues its approach to summary and analysis reports without specific legislative guidance.
    - Option 2: Amend the Commerce Act to enable the Commission to consider whether information disclosure is effective in achieving the Part 4 purpose as part of its summary and analysis reports following each price-setting event.
    - Option 3: Amend the Commerce Act to require the Commission to carry out further rounds of section 56G reports after each price-setting event.

    Issue 2

    - Option 4: Retain the status quo – the Commission undertakes a full Part 4 inquiry into whether airports should be subject to a different type of regulation; and the imposition of additional or less regulation, if deemed appropriate, is done through an amendment to the Act.
    - Option 5: Remove unnecessary steps in the Part 4 inquiry process for investigating whether an already regulated airport should be subject to a different type of regulation.

      and/or

    - Option 6: Amend the Act to clarify that changes to the type of regulation applying to a regulated airport can be made through an Order in Council. Options 5 and 6 are complementary and not mutually exclusive.

54. These options are described in more detail below, along with an assessment of their impacts and the extent to which they meet the objectives. The table on page summarises the options and impact analysis.

Issue 1: The Commerce Commission's ongoing power to consider the effectiveness of information disclosure

Option 1 – retain the status quo

55. Under the status quo the Commission is required to undertake summary and analysis reporting of the information disclosed by regulated airports following each information disclosure.

56. The Commission has previously analysed whether the Part 4 purpose is being met as part of one-off section 56G reports, but it is not explicit in the Act that the Commission can or should do so in their regular section 53B summary and analysis reports. There is therefore a concern that the Commission could be challenged by stakeholders if it chose to examine whether information disclosure was meeting the Part 4 purpose in its summary and analysis reports.

57. If the Commission was prevented from including analysis of whether the Part 4 purpose was being met even if it considered this analysis appropriate, this could limit Ministers and other interested parties from having meaningful analysis about an airport's performance following a price-setting event.

58. Without the Commission explicitly having the ability to consider how well airports' information disclosure aligns with the purpose of Part 4, airports may be less inclined to act consistently with this purpose. This is because interested parties will not have ready access to the information required to make an informed assessment, and to subsequently hold airports to account. A reduced scope of commentary from the Commission is also likely to lead to less media focus on airports' conduct, which in turn reduces the practical incentives on airports to act consistently with the Act.

Option 2 – enable the Commerce Commission to consider whether information disclosure is achieving the Part 4 purpose in its regular reporting (preferred option)

59. Under this option the Commission, following each price-setting event, is empowered to produce a summary and analysis report that includes consideration of whether or not the airport was acting consistently with the Part 4 purpose.

60. The value of this analysis being undertaken following a price-setting event is that this is when an airport sets its intention for the following five years and discloses the basis on which it has set its prices. This information is technical and may be difficult for interested parties to unpick.

61. Empowering the Commission to carry out this analysis following a price-setting event could provide confidence for the Commission to develop a body of conclusions on the outcomes other than price, including efficient investment and the sharing of benefits of efficiency gains with consumers.

62. The reports would draw on the information disclosed as well as other relevant information and would provide comment on how an airport is performing so that interested persons can understand how prices are set. As part of this it would identify any concerns that an airport's behaviour was inconsistent with the Part 4 purpose. This would enable Ministers to make an assessment about whether information disclosure is producing the desired outcomes or whether further regulation needs to be explored.

63. Ensuring that the Commission is active in its detection of any issues with airports' behaviour and that it has an avenue to communicate these concerns increases the threat of further regulation. This is because it means that airports will not be able to fly under the radar and any inconsistent conduct will be detected.

64. The reports may also act as a constraint on airport behaviour. The previous experience with the section 56G reports is that a negative report by the Commerce Commission can influence an airport to rectify its behaviour by either resetting prices or providing further disclosures.

Option 3 – require the Commerce Commission to repeat section 56G reports after each price-setting event

65. Section 56G explicitly required the Commission to report back to Ministers on whether information disclosure regulation of airports was meeting the Part 4 purpose detailed above, in respect of each airport being regulated. As discussed above, these reports were a

one-off statutory requirement and will not be carried out following future information disclosure events.

66. Under this option the Commission would be required to complete further section 56G reports after each price-setting event, providing comment on the effectiveness of the information disclosure regime in respect of each airport being regulated. These would be in addition to the summary and analysis reports, which provide a wider set of information about airport performance.

67. As outlined above, previous experience with the section 56G reports indicated that a negative report by the Commerce Commission can influence an airport to rectify its behaviour by either resetting prices or providing further disclosures. These reports also provide a clear signal to the public and to decision-makers about the ongoing effectiveness of information disclosure.

68. However, carrying out these reports on top of regular summary and analysis would consume both time and resources, and create a less cost-effective and timely regime overall. Such a mandatory review may not always be necessary in every case, for example when an airport is meeting the Commission's expectations with regard to pricing. This option would also reduce regulatory certainty, as it formally places the current regime under review after each price-setting event, which could provide thorough scrutiny of the regime but would impose unnecessary expense and resource.

Issue 2: Cost and difficulty of the process for changing the type of regulation that applies to airports

Option 4 – retain the status quo

69. Under the status quo:

    a. the Commission would be required to conduct a full Part 4 inquiry to investigate the need to change the type of regulation that applies to a specified airport; and

    b. if a change to the type of regulation for an airport is recommended, this would need to be effected through an amendment to the Commerce Act.

70. The Commission has estimated that a full Part 4 inquiry into airports would likely take around 12 months and would likely cost around $1 million. While the existing Part 4 inquiry process does provide a means for inquiring into whether a different type of regulation is required, the process includes repeating analysis that has already been done, imposing both monetary and time costs.

71. As well as generating unnecessary cost, the perceived barrier of a full Part 4 inquiry's expense and length, plus the time and uncertainty involved in making legislative change, has the potential to make further regulation seem like a remote possibility. This undermines the regulatory threat on which information disclosure depends.

72. In terms of the current process required for introducing a different type of regulation, amending legislation (from the policy development stage until when the Act comes into force) typically takes at least a year – after the inquiry and recommendations process had been completed. This slow process may further undermine the threat of further regulation.

73. Further, imposing a different type of regulation on an already-regulated airport may not warrant its own separate legislation, and therefore any changes would be reliant on

another relevant legislative vehicle which is likely to substantially add to the time it takes to impose any additional regulation.

Option 5 – remove unnecessary steps in the inquiry process for investigating the need to change the type of regulation applying to airports (preferred option)

74. Under this option, there would be a truncated inquiry process focused on determining whether the benefits of imposing a different type of regulation on already-regulated airports outweigh the costs.

75. The truncated inquiry process would differ from the existing inquiry process in that the Commerce Commission would not be required to

    a. reconsider whether the already regulated good or service (in this case, airports) should be subject to any regulation at all; and

    b. reconsider whether there is little or no competition in the market.

76. It is unnecessary to conduct the above steps in the analysis when Parliament has already decided that airports should be subject to regulation, and given that the catalyst for an inquiry is likely to be that an airport is not acting consistently with the Part 4 purpose, following the Commission's summary and analysis reporting.

77. Officials propose that under this option, like under the status quo, the Commission would be able to hold an inquiry either if required to by the Minister or on its own initiative. Once an inquiry is triggered the Commission would still be required to:

    a. consider whether the benefits of changing the type of regulation (i.e. imposing an additional type of regulation beyond information disclosure) materially exceed the costs of regulation; if so, what type of regulation should apply and how;

    b. develop input methodologies for the regulation; and

    c. undertake a qualitative analysis of all material long-term efficiency and distributional considerations, in determining whether the benefits of changing the type of regulation exceed the costs.

78. Upon reaching its findings, the Commission would report back to the Minister, who could then decide whether or not to make a recommendation to the Governor-General to create an Order in Council imposing a different type of regulation.

79. Officials are of the view that this process would be proportionate, timelier and less expensive than the process contained in the status quo. It creates a streamlined and more appropriate approach for investigating the need to change the type of regulation if an airport (or other supplier regulated through Part 4 information disclosure) is not acting consistently with the Part 4 purpose, while ensuring that adequate analysis to determine both the costs and benefits of an approach is undertaken. Decision makers would still receive all the information required to make an informed decision on whether changing the type of regulation for an airport is justified.

80. There is a small risk that, by omitting consideration of whether regulation is required at all, the truncated inquiry process for already-regulated services will provide a less comprehensive and robust outcome compared to a full Part 4 inquiry. However, given that the truncated inquiry process will only be applied to the specified airport services of airports that are a) already regulated and b) which may not, in the Commission's view, be sufficiently controlled by existing regulation, officials consider that this risk is minor.

Option 6 – amend the Act to clarify that changes to the type of regulation applying to a regulated airport can be made through an Order in Council process (preferred option)

81. Under this option, the Act would be amended to make it clear that changes to the type of regulation for an already regulated airport can be made by an Order in Council. This is the same mechanism by which Part 4 regulation is imposed on goods or services which are not currently regulated.

82. Option 6 is not mutually exclusive to option 5 above. Instead, it would complement option 5 as a further improvement to the process for changing the type of regulation that applies to regulated airports if considered necessary. This option would bring the airports regime in line with the standard mechanisms under Part 4 for regulating goods or services that are not currently regulated, as well as the mechanism for including additional airport services at regulated airports under the regime.

83. This option would create an efficient method for imposing regulation through the Order in Council process. An Order in Council could be developed and come into force within a few months of the Commerce Commission making a recommendation to the Minister. This would uphold the credibility of the threat of further regulation, as it creates an efficient process for implementing the Commission's recommendation as to the appropriate type of regulation.

84. Officials understand that the current situation is the result of a drafting oversight, rather than an intentional move to introduce a higher bar for the imposition of further regulation on already-regulated airport. Despite this, there is still a risk that the proposed change would be seen by airports as a lessening in the level of scrutiny applied to decisions to impose further regulation. This would be mitigated by the legislative processes in place, which require recommendations from the Commission and the Minister before any proposed changes, which would provide proportionate scrutiny.

85. However, as this option would be aligning the level of scrutiny to that applied to normal processes for imposing Part 4 regulation, it is not clear that the risks to airports are any greater. We therefore consider this a low-risk change.

5 Summary of analysis

86. The tables below assess the options for Issues 1 and 2 against the objectives set out above in Chapter 2. The symbols below represent relative impacts towards achieving the objectives, rather than absolute measures. For example, an option with two ticks is better than an option with one tick, but not necessarily twice as good. The best option cannot be assessed simply by counting the ticks and crosses.

Key	✓ Positive effect	✓✓ Significant positive effect	✗ Negative effect	– No effect

Issue 1: The Commerce Commission's ongoing power to consider the effectiveness of information disclosure

Objective	Option 1: Retain the status quo	Option 2: Enable the Commission to analyse whether information disclosure is effective at achieving the Part 4 purpose (preferred option)	Option 3: Require the Commission to repeat section 56G reports after each price-setting event
Interested parties have sufficient information to assess whether the purpose of Part 4 is being met	✓ If the Commission continues with its approach to summary and analysis reports, interested parties will have sufficient information. However it is not certain that the Commission will consider the effectiveness of the information disclosure regime in its future reporting.	✓✓This option ensures that the Commission has the clear ability to undertake in-depth analysis following each price-setting event, including an assessment as to whether the purpose of Part 4 is being met by the existing regulatory framework, if it considers this analysis appropriate.	✓✓ This option ensures that the Commission will continue to undertake in-depth analysis following each price-setting event, including an assessment as to whether the purpose of Part 4 is being met by the existing regulatory framework.
There is a credible threat of further regulation	✓ The Commission's current view is that they have the ability to analyse the effectiveness of the regime. However, if the Commission considered that it was unable to do so in the future, it could lessen the threat of further regulation and reduce the ability for decision-makers to confidently assess when further regulation is required.	✓✓ This option ensures that the Commission can provide its expert analysis on whether information disclosure is working as intended to the both the public and decision-makers, ensuring a credible threat of further regulation.	✓✓ This option means that the Commission's expert analysis on whether information disclosure is working as intended will be provided after each price-setting event. This creates a strong threat of further regulation, if the Part 4 purpose is not being well met.

Regulatory uncertainty is minimised	✗ Under the status quo the regulatory environment is somewhat uncertain, particularly if the Commission determined it would be too risky (i.e. potential legal challenge) to analyse whether the Part 4 purpose is being met in its summary and analysis reports. Now that the section 56G reports have lapsed, there is no longer a clear, specific trigger for a change in the type of regulation. In the absence of public reports making the Commission's view on the performance of the existing regime clear, airports would lack visibility of views about the effectiveness of information disclosure.	✓✓ This option provides certainty about the Commission's powers and the scope of existing regulation. This minimises the risk of legal challenge to the Commission's analysis. It also provides a clear trigger (the Part 4 purpose not being met) for the investigative process that might lead to a change to existing regulation.	✓ This option provides clarity about the scope of existing regulation and guarantees the Commission will always analyse the effectiveness of the regime in its reports. It also provides a clear trigger (the Part 4 purpose not being met) for the process that might lead to a change to existing regulation. However, it does create a degree of uncertainty for airports, as the Commission would be formally reviewing the current regime after each price-setting event. This provides greater scrutiny of the overall regime but imposes unnecessary expenses and resources.
The regime is cost-effective and timely	✓✓ The status quo is relatively cost-efficient and timely. The Commission's summary and analysis reports are a less time- and resource-intensive process than the section 56G process, but (in their current interpretation) still provide the necessary information.	✓✓ The Commission's summary and analysis reports are a less time- and resource-intensive process than the section 56G process, but (in their current interpretation) still provide the necessary information.	✗ Section 56G reports are a time- and resource-intensive process, and carrying out these reports on top of the summary and analysis would create a less cost-effective and timely regime overall.

87. Option 2 is the preferred option to address Issue 1. While Option 3 would offer the most comprehensive process for analysing how well the regime is working, it would also require considerably more resource and cost without providing the greatest certainty. Option 2 is therefore the favoured approach as it creates a more cost-effective and timely regime by making it explicit what the Commission is able to examine in its regular reporting.

Issue 2: Cost and difficulty of the process for changing the type of regulation that applies to airports

	Option 4: Retain the status quo	Option 5: Remove unnecessary steps in the inquiry process for investigating the need to change the type of regulation for already regulated airports (preferred option)	Option 6: Amend the Act to clarify that changes to the type of regulation for a regulated airport can be made through an Order in Council process (preferred option alongside Option 5)
Interested parties have sufficient information to assess whether the purpose of Part 4 is being met	– These current processes do not affect the information available to assess whether the purpose is being met.	– The truncated process will still provide decision-makers with all the relevant information required to make an informed decision on whether further measures are required.	– This option has no effect on the level of information that is required to make this assessment.
There is a credible threat of further regulation	✗ While additional regulation could be imposed through the full Part 4 inquiry and then legislative amendment, the time and expense involved makes the process onerous. This has the effect of diminishing the threat of further regulation.	✓✓ This option offers a clear legislative process for determining whether an airport should be subject to a different type of regulation.	✓✓This option complements option 5 and strengthens the threat of further regulation if an airport is not complying with the Part 4 purpose. It offers a clear and straightforward process for imposing this regulation, if undertaken alongside the truncated inquiry process.
Regulatory uncertainty is minimised	✓ The current Part 4 inquiry process is a known quantity; however the Act is not clear about how changes to the type of regulation for airports should be made. Legislative amendment would probably be required in the absence of a specified Order in Council process for such a change.	✓✓The process for investigating the need for a different type of regulation would be very clear under this option.	✓✓The process for implementing a change in the type of regulation if recommended by the Commission's inquiry would be very clear under this option.
The process is cost effective and timely	✗ The existing process requires that the Commission undertake analysis into whether or not airports should be subject to any type of regulation, adding time and expense to the inquiry process without any additional	✓✓ As this inquiry is truncated the costs and time associated with undertaking an inquiry would be reduced.	✓✓An Order in Council can be prepared within a few months, and is not dependent on finding an appropriate legislative vehicle.

	benefit. If a different type of regulation is to be imposed, primary legislation can take over a year to work its way through the policy and legislative process. Amendments of this nature are unlikely to warrant their own bill, and therefore timing would be dependent on other amendments being made to the Commerce Act.	

88. Options 5 and 6 are preferred to the status quo, because in combination, they provide a more proportionate and consistent process for imposing further regulation if airports do not meet the Commission's expectations. This creates a more credible threat of further regulation and there is a stronger incentive for airports to behave in a way that is consistent with the purpose of Part 4 regulation.

6 Consultation

89. The Ministry consulted with key stakeholders who are affected by the regulation of specified airport services. A discussion document was released in November 2014, and eight submissions were received.

90. A targeted consultation on the issues outlined in this RIS was also conducted between late-2015 and early 2016, including written submissions and interviews.

91. Broadly, airports were of the view that:

    a. The information disclosure regime is working well.

    b. The Commission's powers to undertake analysis could be clarified, but it should not be a full section 56G report and should not be resource intensive.

    c. The current Part 4 inquiry process should remain the process for determining whether the type of regulation is appropriate.

    d. Regulation should be able to be imposed and removed.

    e. An Order in Council should be able to be used to impose additional regulation.

92. Broadly, airlines were of the view that:

    a. Airports should be moved to negotiate/arbitrate regulation.

    b. A full section 56G report should be undertaken following each price-setting event.

    c. There should be a truncated process for inquiring into whether additional regulation is required. This process should put the consumer at the forefront.

    d. An Order in Council should be able to be used to impose additional regulation.

93. The Treasury and the Ministry of Transport have been consulted throughout the review. The Commerce Commission has also been consulted on the proposals, and the Commission's view is that the proposed changes are reasonable.

7 Conclusions and recommendations

94. On the basis of the analysis set out above, we recommend that the Commerce Act be amended to:

    a. make it explicit that following a price-setting event, the Commerce Commission (as part of its section 53B summary and analysis reports) can look into whether the part 4 purpose is being met (**Option 2**);

    b. create a truncated inquiry process to investigate the need to change the type of regulation for regulated airports (**Option 5**); and

    c. allow for the type of regulation to be changed via Order in Council, if this is recommended following the above inquiry (**Option 6**).

95. We are of the view that the combined effect of these changes will ensure that the information disclosure regime for airports continues to be effective under current conditions.

96. The changes ensure that the Commerce Commission has the clear ability to undertake analysis of the effectiveness of information disclosure following each price-setting event, if it deems this analysis appropriate for an airport.

97. Removing unnecessary steps in the inquiry process for investigating whether a currently-regulated airport should be subject to a change in the type of regulation will reduce the cost and time associated with this particular inquiry, as the Commerce Commission will only have to undertake the analysis that is necessary to determine whether additional or less regulation is required.

98. Clarifying that changes to the type of regulation can be made through an Order in Council process ensures that any recommendations following such an inquiry can in fact be effected in a timely and efficient manner.

99. These proposals do not go as far as airlines indicated they would wish (in that we are not proposing a move to a stronger type of regulation for airports at this time). However, they do help ensure a credible threat of further regulation, if stronger regulation is required in the future.

100. The impact of these proposals on wider stakeholders (such as air travellers and the wider public) is minimal. Airport charges form a small part of airlines' charges to customers, and are not significant compared to other forces (such as competition within the airline industry). Moreover, evidence indicates that the current regulatory regime is working well. The proposed changes are intended to ensure this current effectiveness is maintained.

8 Implementation plan

101. The implementation of the preferred options above would require amendment to the Commerce Act 1986. The Minister of Commerce and Consumer Affairs would introduce a Bill to make these legislative changes. Given that the preferred options only require minor legislative amendments, these changes may be suitable for inclusion in an omnibus Bill.

102. There is the possibility that the proposed changes could be included in the Commerce Amendment Bill (Targeted Review of the Commerce Act), which is currently holding a Category 6 on the legislative programme for 2017. This will depend on whether Cabinet progresses the other proposals under that Bill. Alternatively, the Regulatory Systems Bill No. 3 is another possible legislative vehicle. Officials will work with the Parliamentary Counsel Office to determine an appropriate legislative vehicle for these amendments.

103. The Commerce Commission will be responsible for implementing the proposed amendments. As the amendments seek to clarify the Commerce Commission's ability to undertake meaningful analysis following a price-setting event, there is unlikely to be a major change to the Commission's approach to summary and analysis reports. If amendments are made, we will work with the Commission to ensure that it understands its responsibilities.

9 Monitoring, evaluation and review

104. We will undertake a full review of the Part 4 regime for airports by 2027. This is following two further five-yearly price-setting events for each major airport, which should allow for a body of reports to be developed by the Commerce Commission so that officials can make informed recommendations on the success of the changes and consider any other necessary changes to the regime.
105. A formal review will enable officials to evaluate whether the changes have been successful and review whether the provisions are still fit for purpose over time. The review could consider whether the existing regulatory framework for airports under the Act is the most effective means to promote the Part 4 purpose, and assess whether alternative regulatory frameworks (e.g. price controls or access regimes) may be a preferable and more effective means of achieving these outcomes.
106. MBIE will be responsible for undertaking the review, and report back to the Minister of Commerce and Consumer Affairs on the findings of the review upon conclusion. Possible outcomes could include a fuller review of the Part 4 regime, or recommendations for the Commission to inquire into the need to change the type of regulation that applies to airports, whether the scope of currently regulated airport services is appropriate, or whether other airports may need to be brought into the regime.
107. If there any significant concerns that arise prior to the formal review date, this review does not preclude the necessary changes to be made to the regime.
108. Officials from the Competition and Consumer Policy team at MBIE will also monitor the implementation and outcomes of the regime as part of regular monitoring of the effectiveness of the information disclosure regime for airports. We have regular engagement with airport stakeholders before and after price-setting events. We will seek feedback from key stakeholders after implementation to evaluate how the changes are bedding in.