Impact of Auckland Airport's charging regime on New Zealand aviation

Final Report to Air New Zealand Limited

May 2025

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Definitions

ACCC	Australian Competition and Consumer Commission
AER	Australian Energy Regulator
AERA	Airports Economic Regulatory Authority of India
AIAL	Auckland International Airport Limited
ARTC	Australian Rail Track Corporation
AvSec	Aviation Security Service
BAU	Business as Usual
BISOE	BIS Oxford Economics
BLR	Bengaluru International Airport
CAA	New Zealand Civil Aviation Authority
EBITDA	Earnings Before Interest Tax Depreciation and Amortisation
FY	Financial Year
GDP	Gross Domestic Product
ID	Information Disclosure
IM	Input Methodology
PSE	Price Setting Event
PSE4	Price Setting Event 4
PSE5	Price Setting Event 5
RAB	Regulated Asset Base
RCG	Rail Capacity Group
UKCAA	United Kingdom Civil Aviation Authority
WACC	Weighted Average Cost of Capital

Executive summary

Auckland International Airport Limited (AIAL) operates New Zealand's main gateway to the rest of the world and is the largest airport for domestic and regional flights. Air New Zealand is AIAL's largest customer and an important driver of economic activity in New Zealand. It connects New Zealand to the world (alongside other airlines) and links major New Zealand centres and smaller regional towns.

The price of air travel is a key determinant of aviation demand, with flow-on effects for New Zealand's economic performance. Higher ticket prices reduce demand for air travel. Aeronautical charges at airports and several Government regulatory charges (for aviation safety, security, biosecurity and border clearance) are included in the ticket prices passengers pay. These additional costs on air travel affect demand.

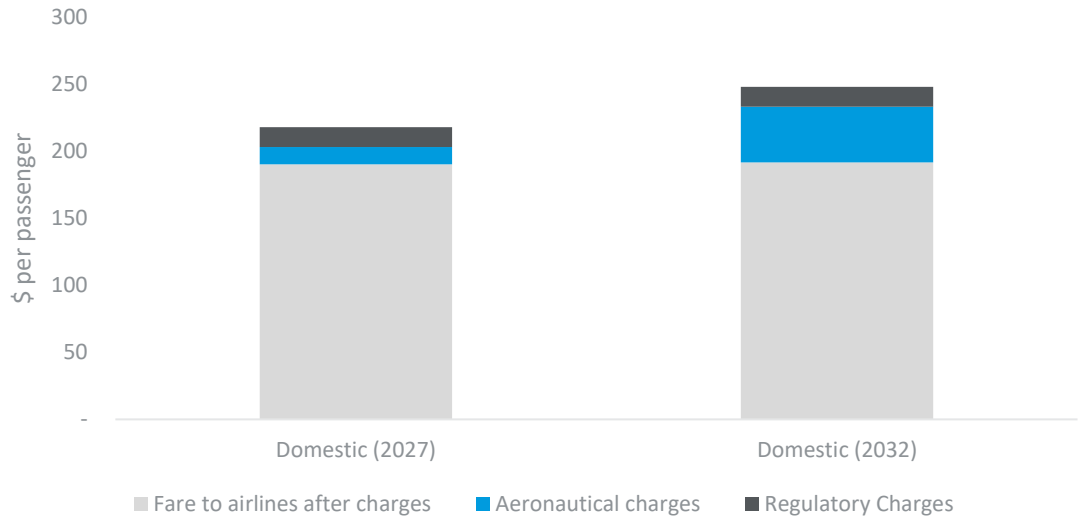
While all airport charges matter, AIAL can be expected to have a disproportionate effect on air travel in New Zealand in the coming years. From PSE4 to PSE5, AIAL is planning a major $6.6 billion aeronautical capital expenditure programme, and will commission $5.7 billion into the regulated asset base (RAB). This capex is for a new integrated domestic-international terminal and associated apron, airfield, and enabling works, plus taxiway expansions, pier extensions, transport-hub upgrades, and resilience projects. Under AIAL's regulatory regime, these capital expenditures are added to the RAB and the capital costs are passed on to airline customers in aeronautical charges (which are, in turn, added to ticket prices) over PSE5 and into the future. The current regime gives airports significant leeway in determining their investment programs, even though they are opposed by the users and pass the costs of the major capex expenditures into immediate increases in the aeronautical charges paid by air travellers.

While the proposed re-development of the Auckland airport is an exciting project, the wisdom of imposing the costs of a major infrastructure upgrade on airlines at the time when the aviation industry is already struggling has to be questioned. AIAL has itself recently noted that New Zealand is sitting well behind Australia and other markets in the recovery of capacity to pre-COVID levels. While at some Australian airports seat capacity now exceeds 2019, New Zealand is at 89 percent of pre-COVID level.[1]

Overall, while the state of infrastructure is not a constraint on aviation growth in New Zealand for the foreseeable future, costs and demand are. Given the material effect of the expected airport and regulatory charges on airline pricing and hence aviation demand, Air New Zealand asked Castalia to model the effects under different scenarios for capital expenditure and regulatory treatment of AIAL. Airport and regulatory charges are a significant portion of the ticket price that passengers pay. The below figure shows the share of aeronautical and regulatory charges as a share of ticket prices for domestic passengers flying in and out of AIAL, both before AIAL's terminal redevelopment (2027) and after (2032):

[1] AIAL news release, "1H25 results", 20 February 2025, available at: https://corporate.aucklandairport.co.nz/news/latest-media/news-articles/1h25-results-increased-demand-from-kiwis-for-international-travel

Figure 0.1: Airfare cost breakdown



Note: 2032 breakdown figures are modelled results

Since the current regulatory regime allows and to some extent incentivises airports to drive capital projects without regard to their effect on demand, it may be necessary to consider changes to the regulatory regime. In essence, two types of changes are possible:

- Rules that impose constraints on airports in deciding to advance major capital projects without user consent
- Rules that require airports to use non-aeronautical revenues to contribute to the costs of major infrastructure development in a way that promotes air travel, as is common in other jurisdictions.

In this report, we outline how AIAL's capex programme will significantly increase future aeronautical charges under the current regulatory regime—"Business as Usual" (BAU). We model the impact on air travel using previously conducted research on demand elasticities in response to changes in airfares.

We then examine the effects on air travel of applying alternative regulatory approaches to capital expenditure decisions and cost sharing. The alternative scenarios we model are all based on regulatory models routinely used in other jurisdictions as well as a realistic alternative capital expenditure program.

Current dual till regime has weak controls over airport capital expenditure—with potentially severe consequences

New Zealand's regulatory regime for prescribed airports such as AIAL is relatively weak given their effect on demand for air travel and the consequential economic and connectivity. The consequences of regulatory weakness can be severe when the scale of airport re-development is huge relative to the market size.

AIAL charges airlines for aeronautical services, such as landing, aircraft parking and terminal use. Under Part 4 of the Commerce Act 1986, its aeronautical services are subject to

Information Disclosure (ID) regulation. AIAL sets its own charges, but must disclose its costs, returns, and quality outcomes.

New Zealand's regulatory treatment of airports is premised on the assumption that large airline users will effectively negotiate with AIAL over the quality of service (which drives capital and operating costs) and the prices it charges. Public scrutiny by the Commerce Commission and the possibility of heavier regulation are intended to create an incentive for AIAL to price and invest efficiently while protecting passengers and airlines.

Every five years, AIAL consults airlines on price-setting events (PSEs) and sets its aeronautical charges. The Commerce Commission then reviews the disclosed pricing decision to test whether the expected returns are consistent with the statutory objective of promoting the long-term interests of consumers. In March 2025, the Commerce Commission reviewed AIAL's aeronautical pricing and found that the airport's charges were yielding an excess profit of approximately $190 million, with a return of 8.73 percent, which exceeded the reasonable range of 7.3 to 7.8 percent. In response, AIAL changed its aeronautical charges for the remainder of Price Setting Event 4 (PSE4) (to the 2027 financial year).

While the current regulatory regime is intended to prevent excessive returns, it provides limited restraint on the airport monopolies from undertaking developments that may not be affordable to the users. AIAL will be able to recover from airlines its significant capital costs for the planned capex programme. These increased charges will take effect when the new assets enter the RAB at the end of PSE4 and through Price Setting Event 5 (PSE5) (2028-2032 financial years) and will feed into airfares.

Castalia analysed three alternative regulatory scenarios for AIAL's capex programme and regulatory model to test the effects of viable changes on aeronautical charges and air travel

We modelled the aeronautical charges under the following scenarios:

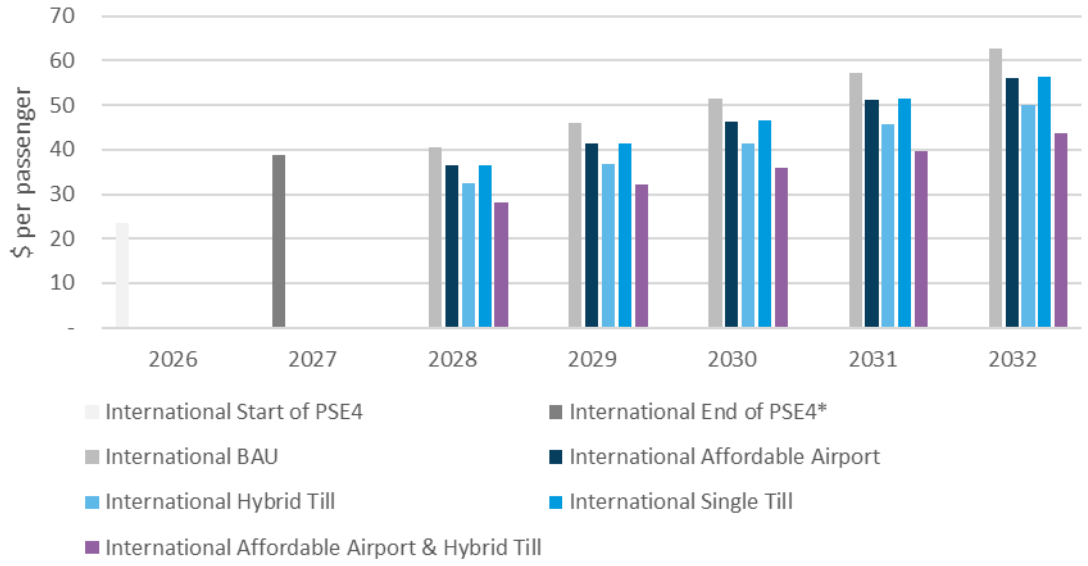
- Business As Usual (BAU): assumes that AIAL's airport investment proceeds as planned, and AIAL applies the same price-setting methodology in PSE5 as it did in PSE4
- Affordable Airport: AIAL invests in a fit-for-purpose terminal at a more affordable level to meet forecast demand
- Hybrid Till: AIAL's airport investment proceeds as planned, and it sets charges using a globally proven Hybrid Till model, which allocates a proportion of non-aeronautical revenues to recover aeronautical charges
- Single Till: AIAL's airport investment proceeds as planned, and it sets charges by recovering costs from regulated aeronautical and non-aeronautical revenues
- Affordable Airport + Hybrid Till: AIAL invests in a fit-for-purpose terminal, and allocates a portion of non-aeronautical revenues to recover aeronautical charges.

Under the BAU Scenario, aeronautical charges are forecast to increase by the following amounts from 2027 to 2032:

- 61 percent for international air travellers
- 203 percent for domestic air travellers
- 99 percent for regional air travellers.

Under Castalia's potential alternative regulatory scenarios, the change in aeronautical charges is less. Each of the alternative scenarios describes an outcome of a realistic alternative approach to regulating capital projects or the funding of those projects. The below figures show the modelled aeronautical charges under the scenarios for international (Figure 0.2), domestic (Figure 0.3) and regional passengers (Figure 0.4):[2]

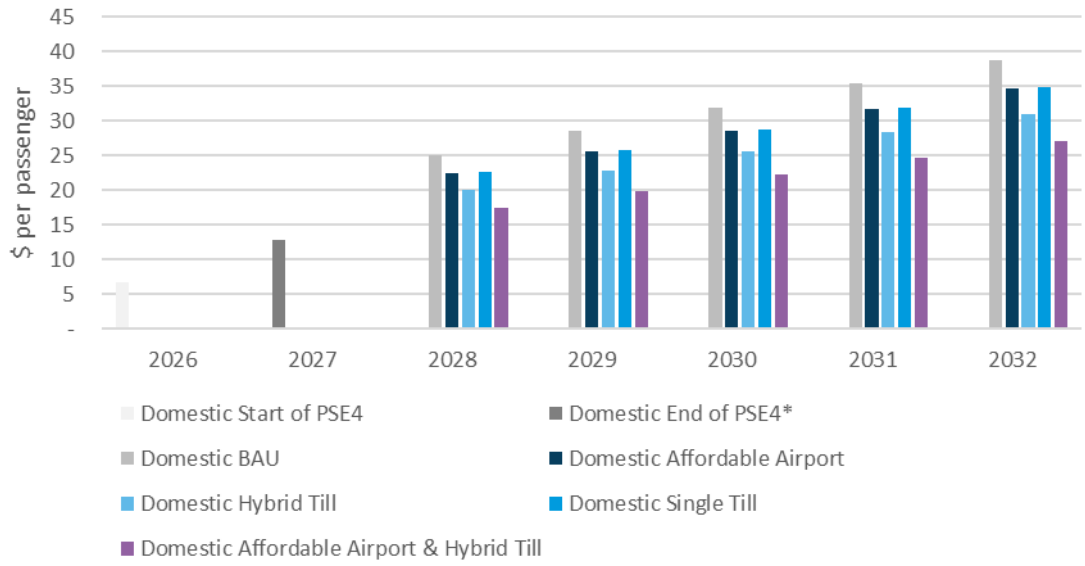
Figure 0.2: International passenger aeronautical charges under all scenarios



**Average of FY26 and FY27 aeronautical charges. "Auckland Airport lowers price increases; Commerce Commission confirms airport investment is reasonable". Available at: https://corporate.aucklandairport.co.nz/news/latest-media/news-articles/auckland-airport-lowers-price-increases*

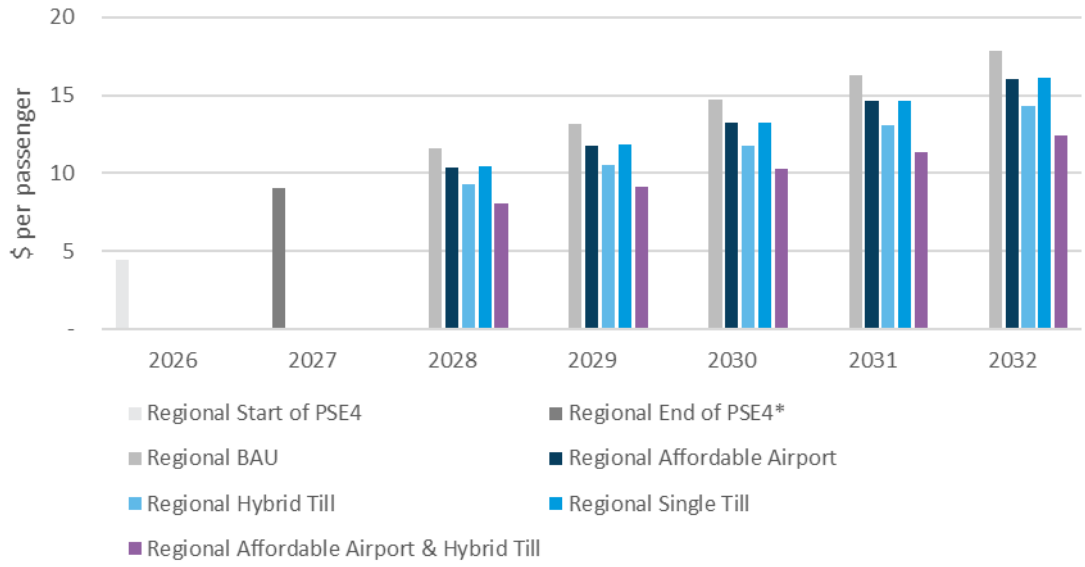
[2] The End of PSE4 aeronautical charge in each chart is taken as an average of AIAL's FY26 and FY27 aeronautical charges and sourced from "Auckland Airport lowers price increases; Commerce Commission confirms airport investment is reasonable". Available at: https://corporate.aucklandairport.co.nz/news/latest-media/news-articles/auckland-airport-lowers-price-increases

Figure 0.3: Domestic passenger aeronautical charges under all scenarios



**Average of FY26 and FY27 aeronautical charges. "Auckland Airport lowers price increases; Commerce Commission confirms airport investment is reasonable". Available at: https://corporate.aucklandairport.co.nz/news/latest-media/news-articles/auckland-airport-lowers-price-increases*

Figure 0.4: Regional passenger aeronautical charges under all scenarios



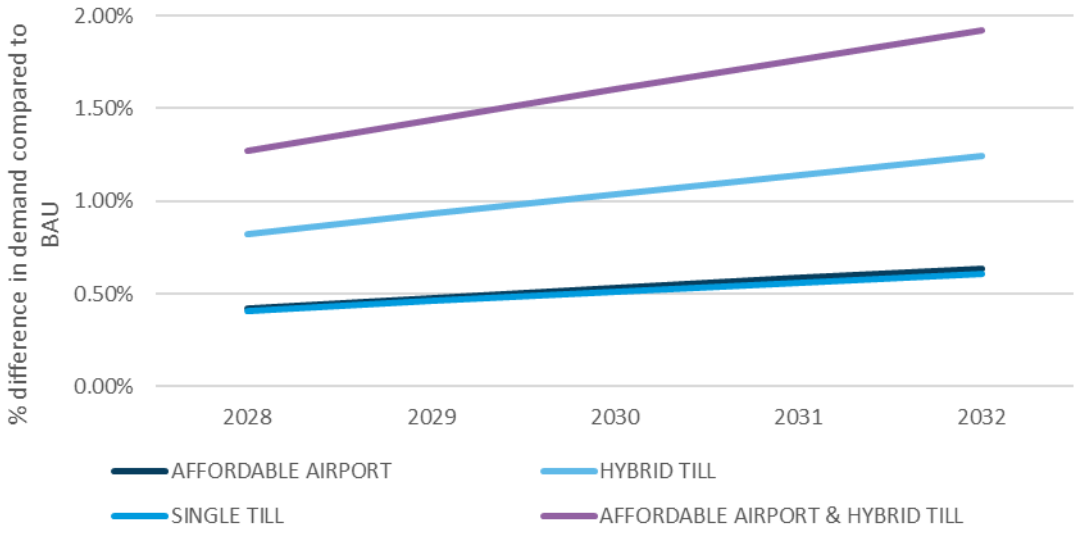
**Average of FY26 and FY27 aeronautical charges. "Auckland Airport lowers price increases; Commerce Commission confirms airport investment is reasonable". Available at: https://corporate.aucklandairport.co.nz/news/latest-media/news-articles/auckland-airport-lowers-price-increases*

Alternative regulatory models would avoid predicted drop in air travel if AIAL's large capex programme proceeds

Alternative approaches to regulating AIAL would lead to lower than currently expected aeronautical charges and would avoid a predicted drop in air travel if AIAL's large capex programme proceeds under the BAU regulatory regime. The effect of the higher aeronautical under BAU will be lower aviation demand—fewer trips—than if AIAL's capex programme was fit-for-purpose, or if policymakers adopted one of the proven international models for regulating airports. In numerical terms, the higher aeronautical charges due to terminal redevelopment in the BAU Scenario will mean there are 353,000 fewer passengers in 2028, rising to 595,000 fewer passengers in 2032 travelling through Auckland airport.

If the alternative regulatory approaches were used, or AIAL built a more affordable airport, the reduction in passenger throughput would be much less marked. Figure 0.5 illustrates the effects of the three scenarios, relative to BAU.

Figure 0.5: Total passenger throughput at AIAL under counterfactual scenarios, compared to BAU



The effect is greatest on "domestic" and "regional" aviation; "domestic" and "regional" travellers are more sensitive to changes in ticket prices. Since "domestic" and "regional" travellers account for around 46 percent of all passenger throughput at AIAL,[3] the effect on aviation demand is significant.

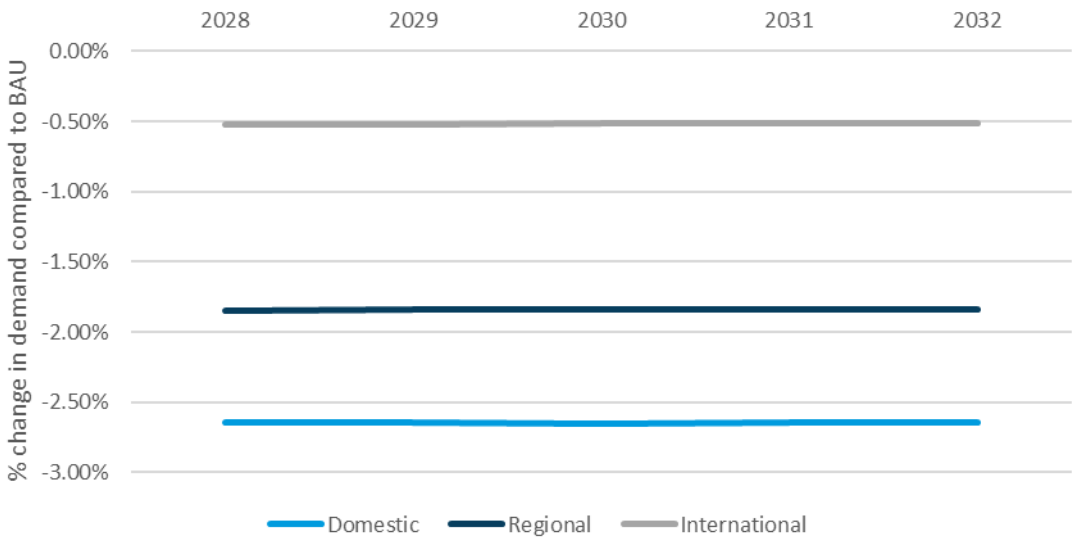
Increases in the Government's regulatory charges will also depress aviation demand

Several Government agencies recover costs for aviation security, aviation safety, border clearance, and there is a visitor levy for conservation and tourism. The agencies have announced increases in regulatory charges. Domestic passengers will face a total $6.66 increase in these charges per trip. International passengers will face a total $32.95 increase in

[3] AIAL Annual Information Disclosure for year ended 30 June 2024, available at: https://corporate.aucklandairport.co.nz/-/media/Files/Corporate/Regulatory-Disclosures/AIAL-2024-Information-Disclosure.ashx

charges per trip. The effect of the increase in Government regulatory charges (leaving aside the change in aeronautical charges) over the modelled period of 2028-2032 is a fall in demand of 0.87 percent and 4.93 percent, depending on the year and route group.

Figure 0.6: Government-imposed regulatory charges will also depress aviation demand



In numerical terms, when new Government regulatory charges are added to the aeronautical charges under the BAU Scenario, the forecast reduction in passengers is 637,000 fewer in 2028 and 908,000 fewer in 2032, compared to AIAL's passenger forecast.

AIAL also plans significant future capital expenditure beyond PSE5 which will affect aviation demand

This report has focussed on the changes in aeronautical and regulatory charges paid by passengers, and the impact on demand during PSE5 (2028-2032). AIAL plans to invest heavily in the years after that. AIAL's 2014 masterplan includes an additional runway and new terminal and other assets. ARUP estimated the additional capex at the end of PSE5 and in later years will be **[CIC]**. ARUP also estimated commissioning timeframes for this capex. We used these cost estimates to model indicative aeronautical revenue that AIAL will be permitted to charge under BAU regulatory settings. Over the same period, AIAL's forecast of passenger throughput also rises, but not as fast as the increase in aeronautical charges. Therefore, we expect in 2033 (PSE6) and beyond, aeronautical charges paid by air travellers to much higher levels than the passenger charges modelled in the BAU Scenario. In other words, aeronautical charges increase at a much faster rate than the growth in passengers who pay the charges. Figure 0.7 illustrates this.

Figure 0.7: AIAL's estimated annual revenue requirement from aeronautical charges in PSE5, PSE6 and PSE7 (2027-2042) and projected passenger throughput

[confidential and commercially sensitive]

Policymakers have choices for alternative regulatory regimes to balance long-term benefits to consumers, returns to airport shareholders and economic growth in New Zealand

The BAU dual till regime allows immediate full recovery of potentially over-specified and unaffordable terminal and other aeronautical investments from airlines. This report shows that the current regulatory regime has relatively weak ex ante oversight and creates incentives for airports to undertake investments ahead of the needs of their customers. This can lead to over-specified and unaffordable infrastructure. Higher than necessary airport charges, in turn, suppress demand with negative economic outcomes to New Zealand. Two broad policy paths can realign the regime with the long-term interests of consumers:

- Tighten capex control inside Part 4 of the Commerce Act; and/or
- Pool commercial revenues to blunt the price shock of aeronautical capital projects.

Tightening capex control would still leave AIAL's fundamental pricing power intact. Even a 'verified' project can trigger steep, lumpy increases in aeronautical charges. This additional review layer could add delays to infrastructure and add verification costs. The information asymmetry between the airport and the verifier is likely to be an issue.

The second, more powerful lever, would require the airport company's commercial revenue—which is only possible because of the existence of the airport—to be applied to offset aeronautical costs. In other words, any significant upgrade in the airport infrastructure that would also create opportunities for commercial returns should be supported by both the aeronautical charges and commercial revenues. A hybrid till model offsets a fixed share (for example, 30 percent) of non-aeronautical revenue against the building-blocks revenue requirement. In a single till model, the airport's non-aeronautical revenue lowers the cost base that is used to calculate aeronautical charges.

A hybrid till model appears to balance competing aims best. Aeronautical charges would be trimmed enough to stimulate traffic growth, but would leave AIAL with genuine commercial upside, preserving investment incentives and debt-raising capacity. A hybrid till model also appears to keep regulatory complexity and forecasting risk manageable. Experience at rapidly expanding Indian hubs demonstrates that airports under hybrid regimes can still finance multi-billion-dollar terminals and runways while delivering lower fares and strong passenger growth.

1 Introduction

Aviation is an important contributor to New Zealand's economic performance. Tourism is a major industry, contributing $44.4 billion to GDP in the year to March 2024.[4] International tourism expenditures were $16.9 billion in the year ended March 2024, and domestic aviation is a key driver of economic growth.

The cost of air travel affects demand for aviation. Airfares include the airlines' costs (fuel, aircraft, pilots, aircrew, ground crew, cost of capital) as well as the airport and regulatory charges, which must be passed to customers. Significant costs included in airfares include:

- Aeronautical charges at airports for runways, air gates, and terminal services
- Regulatory matters such as border clearance costs, biosecurity, and aviation security.

AIAL plans to significantly expand and reconfigure its terminal buildings and spend $6.5 billion over 2022-2032

While all airport charges matter, AIAL can be expected to have a disproportionate effect on air travel in New Zealand in the coming years. AIAL is planning a major $6.5 billion aeronautical capital expenditure programme. This capex is for a new integrated domestic-international terminal and associated apron, airfield, and enabling works, plus taxiway expansions, pier extensions, transport-hub upgrades, and resilience projects. Under AIAL's regulatory regime, these capital expenditures are added to the RAB and the capital costs are passed on to airline customers in aeronautical charges (which are, in turn, added to ticket prices). The current regime gives airports significant leeway in determining their investment programs, even though they are opposed by the users and pass the costs of the major capex expenditures into immediate increases in the aeronautical charges paid by air travellers.

Air New Zealand is concerned about the effect of high and rising aeronautical charges and regulatory charges on aviation demand

Air New Zealand is concerned about the effect of increases in aeronautical charges on air travel to, from, and within New Zealand. Aeronautical charges are passed on to air travellers in ticket prices. Regulatory charges for border clearances (for international travellers), biosecurity and aviation security (for both international and domestic travellers) are also rising, which are also costs borne by air travellers.

Air travellers are sensitive to changes in ticket prices and the total cost of air travel. Reduced air travel has significant impacts on economic activity in Auckland and the other destinations where Air New Zealand flies.

Increases in Air New Zealand's external costs will affect aviation demand and economic activity

The key questions for this report are to:

- Determine the effect of these higher external costs that Air New Zealand must pass on to its customers
- Identify alternative approaches to capital expenditure or the regulatory approach to balance AIAL's commercial interests and long-term benefits to consumers.

[4] Statistics NZ, 14 March 2025, available at https://www.stats.govt.nz/information-releases/tourism-satellite-account-year-ended-march-2024/

This report estimates the effects of changes in Air New Zealand's external costs

This report first documents the aeronautical charges under different scenarios of AIAL's capex programme or different regulatory treatment of revenues (Section 2). We then quantify the effects of the different scenarios on aviation demand using demand elasticity estimates developed by BISOE (Section 3). We then discuss the choices available to policymakers to balance incentivising AIAL to provide high-quality services while promoting the long-term interests of consumers (Section 4).

2 AIAL's aeronautical charges under different scenarios

We modelled the aeronautical charges that AIAL will set for PSE5 under five scenarios: the Business as Usual scenario if AIAL's planned investment proceeds under the current regulatory regime:

- BAU: assumes that AIAL's airport investment proceeds as planned, and AIAL applies the same price-setting methodology in PSE5 as it did in PSE4

With four counterfactual scenarios:

- Affordable Airport: AIAL invests in a fit-for-purpose terminal at a more affordable level to meet forecast demand
- Hybrid Till: AIAL's airport investment proceeds as planned, and it sets charges using a globally proven Hybrid Till model, which allocates a proportion of non-aeronautical revenues to recover aeronautical charges
- Single Till: AIAL's airport investment proceeds as planned, and it sets charges by recovering costs from regulated aeronautical and non-aeronautical revenues
- Affordable Airport + Hybrid Till: AIAL invests in a fit-for-purpose terminal, and allocates a portion of non-aeronautical revenues to recover aeronautical charges.

These scenarios illustrate the impacts of different regulatory regimes on the aeronautical charges. The results are indicative and demonstrate the broad effects of different regulatory choices. They are not precise predictions of future aeronautical charges in PSE5, which would still need to be disclosed and subject to airlines', stakeholders', and regulatory review.

We used AIAL's projections of passenger throughput, published in August 2023, to determine the proportions of passengers who are “international,” “domestic,” and “regional.” Aeronautical charges are based on the aircraft size and type, and other factors, and are set according to whether the aircraft is “international,” “domestic,” or “regional.” [5] Air New Zealand and other airlines operate in a competitive aviation market and generally earn a normal return for shareholders. Therefore, all aeronautical (and Government regulatory) charges are passed through to passengers in their ticket price.

AIAL also intends to invest in new runway and terminal assets after PSE5 according to its masterplan. This new investment will be added to the RAB and the capital costs will be recovered from passengers. We also estimated AIAL’s annual revenue requirement from aeronautical charges using AIAL’s and other experts’ masterplan cost estimates and

[5] In order to estimate the distribution of the total annual aeronautical revenue across the “international”, “domestic” and “regional” passenger classes, we used AIAL’s disclosures and assumed that for PSE5, the capital costs associated with most of the new terminal development would not be passed on to “regional” passengers, since these passengers would use a separate terminal during PSE5. The average allocation of the annual revenue requirement across the modelled period (PSE5) is:
- International: 70 percent
- Domestic: 25 percent
- Regional: 5 percent

assumptions from the BAU Scenario carried forward in those later years after PSE5. This is discussed in Box 2.1.

Box 2.1: AIAL's annual revenue requirement from aeronautical charges in later years

[confidential and commercially sensitive]

2.1 BAU: AIAL's aeronautical charges if planned development proceeds under the current regulatory regime

AIAL's aeronautical charges will increase significantly in PSE5 if the BAU capex programme and regulatory regime continue. We modelled the impact of AIAL's announced approach to setting aeronautical charges following the Commerce Commission's most recent decision.[6] The BAU Scenario models the aeronautical charges that AIAL sets if:

- The current approach to regulating AIAL continues, and
- AIAL proceeds with its capital investment programme proposed in its PSE4 Price Setting Disclosure.[7]

AIAL's most recent published charges

AIAL announced it would reduce aeronautical charges on 31 March 2025 in response to the Commerce Commission's review of PSE4. In March 2025, the Commerce Commission reviewed AIAL's aeronautical pricing and found that the airport's charges were yielding an excess profit of approximately $190 million, with a return of 8.73 percent, which exceeded the reasonable range of 7.3 to 7.8 percent for its Weighted Average Cost of Capital (WACC). In response, AIAL announced it would reduce its charges for the remaining years of PSE4, lowering prices for regional, domestic jet, and international travel to align with the Commission's recommended return of 7.82 percent. Table 2.1 compares the aeronautical charges that AIAL will set for the remaining two years of PSE4 against those that AIAL set after its PSE4 price-setting disclosure in August 2023.

[6] Commerce Commission. (March 2025). "Review of Auckland Airport's 2022-2027 Price Setting Event." Available at: https://comcom.govt.nz/__data/assets/pdf_filenfffhj/0028/365059/Review-of-Auckland-AirportE28099s-2022-2027-Price-Setting-Event-Final-report-31-March-2025.pdf

[7] Auckland Airport. (August 2023). "Price Setting Disclosure – Summary of Capital Investment Programme consistent with pricing decision (Appendix A)." Available at: https://corporate.aucklandairport.co.nz/investors/regulation

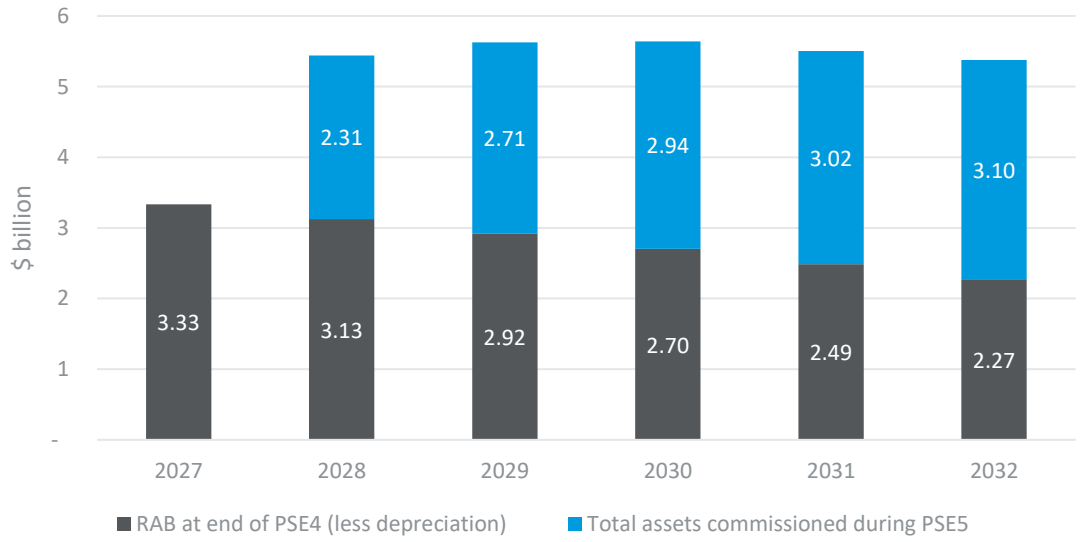
Table 2.1: AIAL aeronautical charges schedule under BAU

Aeronautical charges ($ per passenger for FY26 and FY27)	Regional	Domestic	International
PSE4 charges updated after the Commerce Commission's Review of PSE4 (March 2025)[8]	9.0	12.8	38.9
PSE4 charges set under the AIAL PSE4 Price Setting Disclosure (August 2023)[9]	10.0	14.5	43.6
Variance	**(1.0)**	**(1.7)**	**(4.7)**

AIAL will have to increase charges to recover the costs of new infrastructure investment under BAU Scenario

AIAL's redevelopment plan will significantly raise aeronautical charges in PSE5 as new assets from the redevelopment enter the RAB. In PSE5, AIAL will commission approximately $3.10 billion into its RAB, with $2.31 billion entering the RAB in FY28 alone. This significantly raises the RAB on which AIAL earns its return on capital by approximately 61 percent, as Figure 2.1 demonstrates.

Figure 2.1: Forecast AIAL PSE5 RAB



Source: Auckland Airport. (August 2023). "Price Setting Disclosure – Summary of Capital Investment Programme consistent with pricing decision (Appendix A)." Auckland Airport. (August 2023). "Price Setting Disclosure – Summary of Capital Investment Programme consistent with pricing decision (Appendix A)."

[8] The per passenger charges are the average of the prices for financial years 2026 and 2027. Source: Auckland Airport. (March 2025). "Auckland Airport lowers price increases; Commerce Commission confirms airport investment is reasonable". Available at: https://corporate.aucklandairport.co.nz/news/latest-media/news-articles/auckland-airport-lowers-price-increases

[9] The per passenger charges are the average of the prices for financial years 2026 and 2027. Source: Auckland Airport. (August 2023). "Price Setting Disclosure (Commentary)". Available at: https://corporate.aucklandairport.co.nz/investors/regulation

As a result, our high-level modelling suggests that aeronautical charges will increase by up to 96 percent under the BAU Scenario from the end of PSE4, FY27, to the final year of PSE5, FY28. Table 2.2 presents Castalia's modelled aeronautical charges in PSE5:

Table 2.2: Modelled aeronautical charges in PSE5

Aeronautical charges by charge class ($ per passenger)	2028	2029	2030	2031	2032
Domestic	25.15	28.57	31.98	35.40	38.81
Regional	11.59	13.16	14.73	16.31	17.88
International	40.59	46.10	51.61	57.13	62.64

The BAU Scenario used the following key assumptions:

These assumptions hold for all other scenarios, unless stated otherwise.

Table 2.3: BAU Scenario assumptions

Assumption	Value(s)	Explanation
Target return	7.82 percent	Commerce Commission Review of Auckland Airport's 2022-2027 Price Setting Event (March 2025).[10]
Opening (FY28) RAB	$3.33 billion	AIAL PSE4 Price Setting Disclosure (August 2023).[11]
Assets commissioned into RAB	N/A	According to AIAL PSE4 Price Setting Disclosure (August 2023), Appendix A, Table 2: Forecast capital expenditure, assets commissioned into aeronautical pricing RAB.[12]

[10] Auckland Airport. (March 2025). "Auckland Airport lowers price increases; Commerce Commission confirms airport investment is reasonable". Available at: https://corporate.aucklandairport.co.nz/news/latest-media/news-articles/auckland-airport-lowers-price-increases

[11] Auckland Airport. (August 2023). "Price Setting Disclosure – Schedules." Available at: https://corporate.aucklandairport.co.nz/investors/regulation

[12] Auckland Airport. (August 2023). "Price Setting Disclosure – Summary of Capital Investment Programme consistent with pricing decision (Appendix A)." Available at: https://corporate.aucklandairport.co.nz/investors/regulation

Aeronautical charge progression	13.6 percent per year	Cumulative average growth rate of Castalia forecast RAB estimates
Ratio between aeronautical charges for domestic, regional, and international charge-paying passengers	Set charges to split regulatory revenue according to the following proportions ▪ International: 70 percent ▪ Domestic: 25 percent ▪ Regional: 5 percent.	Proportion of RAB according to passenger throughputs following Commerce Commission Review of Auckland Airport's 2022-2027 Price Setting Event (March 2025).[13]
Non-passenger aircraft revenue	2.5 percent of total regulatory revenue	Average proportion from AIAL Information Disclosures 2023[14] and 2024[15]
Operational expenses	$7.48 per passenger	Follows forecast operational expenses from AIAL PSE4 Price Setting Disclosure.[16] Average operational expenditure forecast per passenger (all inbound and outbound PAX, 50 percent of transit PAX).

BAU Scenario applies the tilted annuities approach to calculating regulatory depreciation

In addition to the assumptions listed above, we applied a tilted annuities approach, with a 2.5 percent tilt and 5.71 percent real discount rate, to calculate depreciation on terminal integration assets commissioned into the RAB during PSE4 and PSE5. Tilted annuities are an approach to calculating depreciation where charges start lower and increase over time, unlike straight-line depreciation, which spreads costs evenly across the asset's life. Christchurch International Airport has implemented a tilted annuity approach to calculating depreciation for price settings since 2017.[17] In its recent review of PSE4, the Commerce Commission stated that straight-line depreciation is unlikely to deliver the best outcomes for consumers and that a tilted annuity approach better reflects those seen in a competitive market. AIAL has indicated it will consult with airlines on adopting tilted annuity depreciation for PSE5 next year (2026).[18]

[13] Auckland Airport. (March 2025). "Auckland Airport lowers price increases; Commerce Commission confirms airport investment is reasonable." Available at: https://corporate.aucklandairport.co.nz/news/latest-media/news-articles/auckland-airport-lowers-price-increases

[14] Auckland Airport. (November 2023), "AIAL 2023 Information Disclosure." Available at: https://corporate.aucklandairport.co.nz/-/media/Files/Corporate/Regulatory-Disclosures/AIAL-2023-Information-Disclosure.ashx

[15] Auckland Airport. (November 2024), "AIAL 2024 Information Disclosure." Available at: https://corporate.aucklandairport.co.nz/-/media/Files/Corporate/Regulatory-Disclosures/AIAL-2024-Information-Disclosure.ashx

[16] Auckland Airport. (August 2023). "Price Setting Disclosure – Schedules." Available at: https://corporate.aucklandairport.co.nz/investors/regulation

[17] Christchurch Airport. (August 2017). "Available at: Disclosure relating to the reset of aeronautical prices for the period 1 July 2017 to 30 June 2022." Available at: https://www.christchurchairport.co.nz/globalassets/about-us/who-we-are/financial-reports/regulatory-disclosures/pricing-disclosure-1-july-2017-to-30-june-2022.pdf

[18] Commerce Commission. (March 2025). "Review of Auckland Airport's 2022-2027 Price Setting Event." Available at: https://comcom.govt.nz/__data/assets/pdf_file/0028/365059/Review-of-Auckland-AirportE28099s-2022-2027-Price-Setting-Event-Final-report-31-March-2025.pdf

Box 2.2: Government-imposed regulatory charges will also increase

Air travellers must also incur the costs of Government-imposed regulatory charges. Several Government regulatory charges are included to varying degrees in ticket prices paid by international, domestic, and regional charge-paying passengers. Government agencies have announced (or are consulting on) increases in these charges.

The Government-imposed charges are:

- AvSec Security Charge (applies to all travellers)
- CAA Safety Levy (applies to all travellers)
- International Visitor Conservation and Tourism Levy (only applies to international visitors).[19]

The agencies have confirmed increases in these charges. "Domestic" passengers will face a total $6.66 increase in these charges per trip. International passengers will face a total $32.95 increase in charges per trip. We determined that the forecast increases in these charges are as follows:

Regulatory charge	Assumption
Domestic charges ($ per passenger)	
AvSec Security Charge[20]	4.34
CAA Safety Levy[20]	2.32
Total increase in domestic regulatory charges	**6.66**
International charges ($ per passenger)	
AvSec Security Charge[20]	9.18
CAA Safety Levy[20]	2.32
International Visitor Conservation and Tourism Levy[21, 22]	21.45
Total average increase in international regulatory charges	**32.95**

[19] Table A.1 provides more details about these Government-imposed regulatory charges, and when they have or will increase.

[20] Civil Aviation Authority. (January 2025). "Civil Aviation Authority confirms increases to levies, fees and charges." Available at: https://www.aviation.govt.nz/about-us/media-releases/show/caa-confirms-increases-to-levies-fees-and-charges

[21] Ministry for Business, Innovation and Employment. (Retrieved April 2025). "International Visitor Conservation and Tourism Levy." Available at: https://www.mbie.govt.nz/immigration-and-tourism/tourism/tourism-funding/international-visitor-conservation-and-tourism-levy

[22] We adjusted the $65 per passenger increase in the International Visitor Conservation and Tourism Levy according to the proportion of visitors expected to pay it. The International Visitor Conservation and Tourism Levy is imposed on visitors who are neither New Zealand citizens nor permanent residents nor Australian citizens. Based on data from 2024 (source below) showing that 67 percent of international arrivals into New Zealand had lived in New Zealand or Australia in the previous 12 months, we assumed that 33 percent of international arrivals at Auckland Airport would pay the International Visitor Conservation and Tourism Levy. Source: Statistics NZ Infoshare: "Total passenger movements by EVERY country of residence (Annual-Mar)."

2.2 Affordable Airport: AIAL's aeronautical charges with a more affordable airport development

The Affordable Airport Scenario models the aeronautical charges under a counterfactual scenario, if AIAL built a fit-for-purpose, but more affordable airport development. The Affordable Airport would still meet forecast growth in passenger demand, but would reduce AIAL's proposed capital investment programme by reducing capital investments that are not strictly required to meet medium-term demand growth.[23]

2.2.1 Affordable Airport Scenario is illustrative of effects of fit-for-purpose lower airport capital expenditure

This lower-cost airport terminal development is based on Arup Group's report on the Affordable Domestic Terminal pathway.[24] The Affordable Airport still meets minimum quality standards and the standards of Air New Zealand and other key airline customers. This lower-cost terminal would lower AIAL's revenue requirement by reducing the RAB on which it earns a return. Consequently, AIAL can lower the aeronautical charges it sets in PSE5, while still meeting its required return and serving medium-term demand, at an acceptable service quality level.

2.2.2 Aeronautical charges are lower in Affordable Airport Scenario

Under the Affordable Airport Scenario, aeronautical charges are lower than the BAU charges. This applies across all route types.

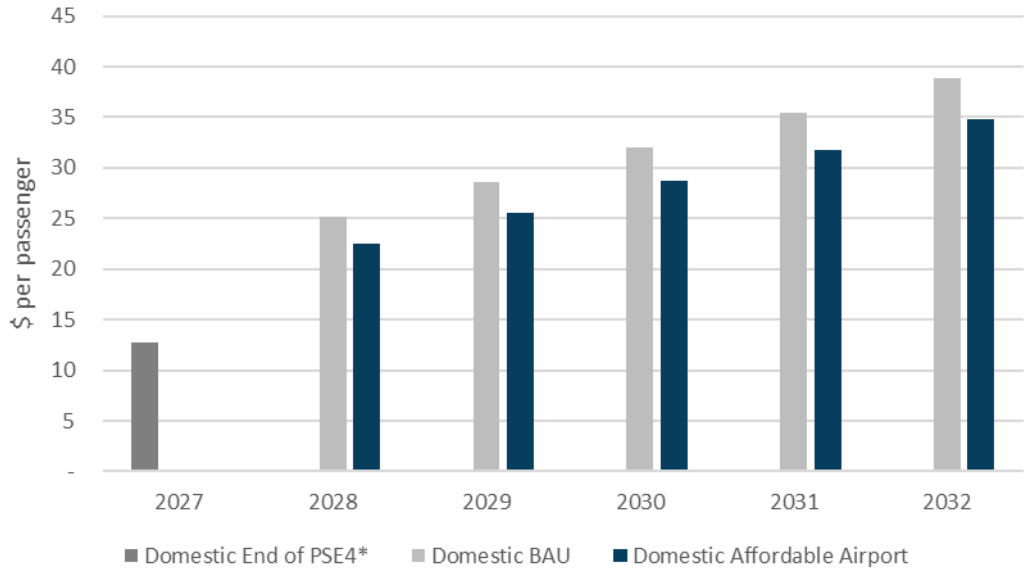
Aeronautical charges will decrease for routes under the domestic flight class under the Affordable Airport Scenario

Under the Affordable Airport Scenario, aeronautical charges for routes under the domestic flight class are about 10.4 percent lower than those under the BAU Scenario. In FY28, airlines pay $22.54 per domestic charge-paying passenger under the Affordable Airport Scenario, compared to $25.15 per passenger under the BAU Scenario. This means that airfares on routes under the domestic flight class will be $2.61 lower per passenger in FY28. By FY32, the final year of PSE5, aeronautical charges under the Affordable Airport Scenario increase to $34.79 per passenger, compared to $38.81 per passenger under the BAU Scenario.

[23] However, these investments provide AIAL with options for expansion in the future.

[24] Arup Group. (April 2024). "Affordable Domestic Terminal Pathway". Available at: https://comcom.govt.nz/__data/assets/pdf_file/0035/358829/Air-NZ-Arup-Affordable-Domestic-Terminal-Pathway-April-2024-17-July-2024.pdf

Figure 2.2: Modelled aeronautical charges under the Affordable Airport Scenario—Domestic

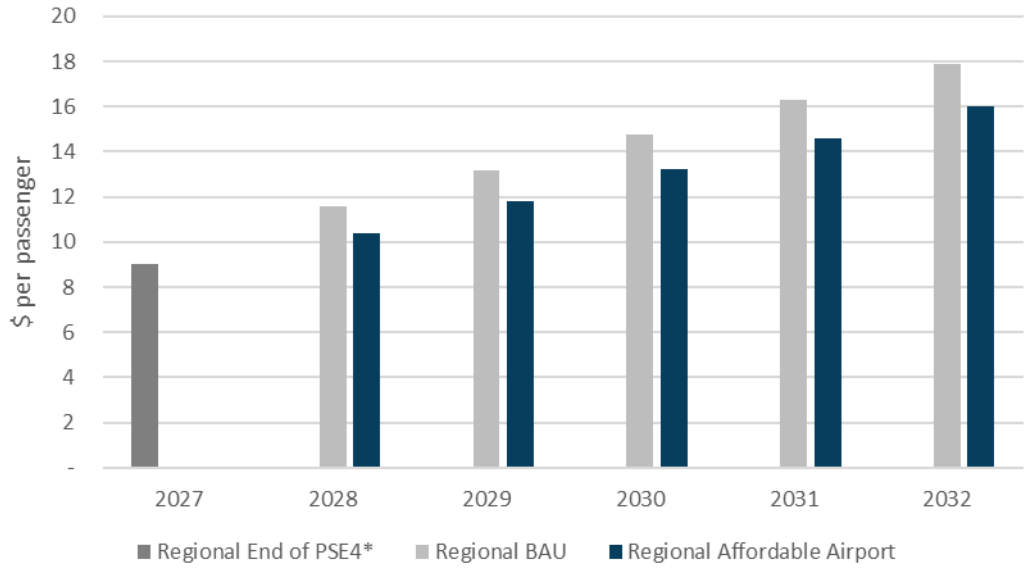


**Average of FY26 and FY27 aeronautical charges. "Auckland Airport lowers price increases; Commerce Commission confirms airport investment is reasonable". Available at: https://corporate.aucklandairport.co.nz/news/latest-media/news-articles/auckland-airport-lowers-price-increases*

Aeronautical charges will decrease for routes under the regional flight class under the Affordable Airport Scenario

Under the Affordable Airport Scenario, aeronautical charges for routes under the regional flight class are about 10.4 percent lower than those under the BAU Scenario. In FY28, airlines pay $10.38 per regional charge-paying passenger under the Affordable Airport Scenario, compared to $11.59 per passenger under the BAU Scenario. This means that airfares on routes under the regional flight class will be $1.20 lower per passenger in FY28. By FY32, the final year of PSE5, aeronautical charges under the Affordable Airport Scenario increase to $16.02 per passenger, compared to $17.88 per passenger under the BAU Scenario.

Figure 2.3: Modelled aeronautical charges under the Affordable Airport Scenario—Regional

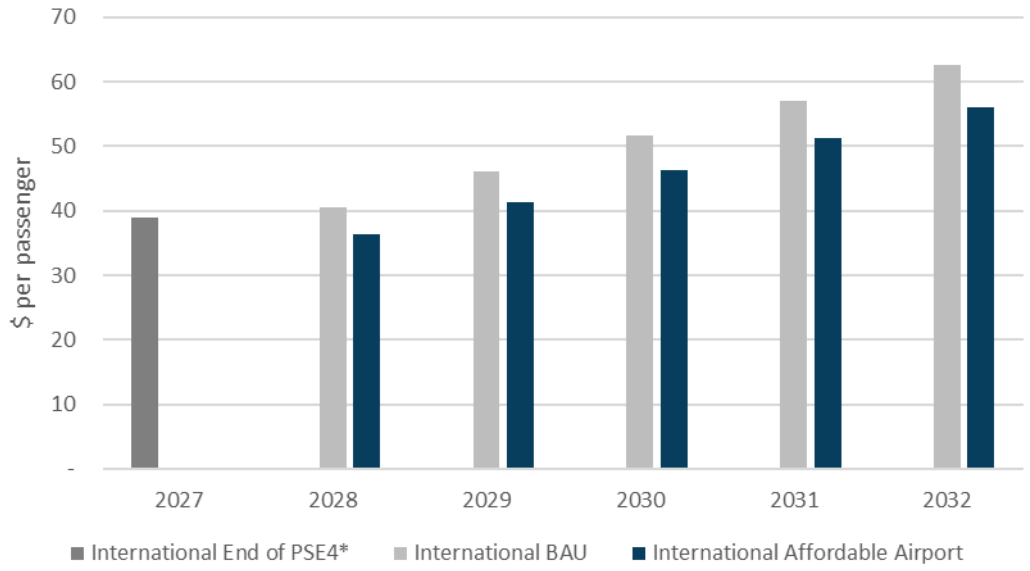


**Average of FY26 and FY27 aeronautical charges. "Auckland Airport lowers price increases; Commerce Commission confirms airport investment is reasonable". Available at: https://corporate.aucklandairport.co.nz/news/latest-media/news-articles/auckland-airport-lowers-price-increases*

Aeronautical charges will decrease for routes under the international flight class under the Affordable Airport Scenario

Under the Affordable Airport Scenario, aeronautical charges for routes under the international flight class are about 10.4 percent lower than those under the BAU Scenario. In FY28, airlines pay $36.37 per international charge-paying passenger under the Affordable Airport Scenario, compared to $40.59 per passenger under the BAU Scenario. This means that airfares on routes under the international flight class will be $4.21 lower per passenger in FY28. By FY32, the final year of PSE5, aeronautical charges under the Affordable Airport Scenario increase to $56.14 per passenger, compared to $62.64 per passenger under the BAU Scenario.

Figure 2.4: Modelled aeronautical charges under the Affordable Airport Scenario—International



**Average of FY26 and FY27 aeronautical charges. "Auckland Airport lowers price increases; Commerce Commission confirms airport investment is reasonable". Available at: https://corporate.aucklandairport.co.nz/news/latest-media/news-articles/auckland-airport-lowers-price-increases*

The Affordable Airport Scenario used the following key assumptions:

Table 2.4: Affordable Airport Scenario scenario-specific assumptions

Assumption	Value(s)	Explanation
Cost reduction in assets commissioned into the RAB	2028: $1 billion reduction	Arup Group's report on the Affordable Domestic Terminal pathway[25] estimates that the domestic terminal could cost around $1 billion less than AIAL's capex plan, while meeting acceptable quality standards.

2.3 Hybrid Till: AIAL's aeronautical charges using a hypothetical Hybrid Till regime

The Hybrid Till Scenario models the effects of adopting a counterfactual regulatory model where non-aeronautical revenue offsets some of the required aeronautical revenue. Under hybrid till models, non-aeronautical costs are not regulated. Rather, a fixed percentage of non-aeronautical revenue is allocated towards aeronautical costs to reflect the fact that the non-

[25] Arup Group. (April 2024). "Affordable Domestic Terminal Pathway". Available at: https://comcom.govt.nz/__data/assets/pdf_file/0035/358829/Air-NZ-Arup-Affordable-Domestic-Terminal-Pathway-April-2024-17-July-2024.pdf

aeronautical commercial activities are enabled and enhanced by monopoly airport operations. For illustrative purposes, we apply a hybrid till model. This is used to set charges at several successful and profitable airports globally. For example, the hybrid till model is used in India, a market that has seen significant growth in aviation demand, airport profitability, and improved transport connectivity.[26] Amsterdam's Schiphol airport is required to make a contribution from non-aeronautical income to aeronautical income, thus reducing aeronautical charges. Copenhagen airport and all Portuguese airports have a hybrid till regime that is used if multilateral negotiations over charges fail.

Under the Hybrid Till Scenario, we assume that the regulator would offset 30 percent of non-aeronautical revenue (the proportion used in India) against the annual regulated revenue required to recover aeronautical costs. This means that 30 percent of AIAL's non-aeronautical revenues from retail, parking, real estate, and other commercial income offset aeronautical charges.

This Hybrid Till Scenario would result in lower aeronautical charges than under the current "dual till" regulatory model used in New Zealand. AIAL would still have a strong incentive to expand profitable non-aeronautical business. Because 30 percent is shared, AIAL would capture most of the upside from growth projects, supporting financeability for large capital expenditures.[27] At the same time, passengers benefit from lower airfares due to cross-subsidised and, therefore, lower aeronautical charges. Lower airfares lead to passenger demand growth (and therefore growth for non-aeronautical business at the airport).

2.3.1 Hybrid Till Scenario assumptions are illustrative only

We used the Hybrid Till Scenario to illustrate the effects of an alternative regulatory approach. The precise details of the level of charge on non-aeronautical revenues and decisions about boundaries between aeronautical and non-aeronautical revenues would need to be determined by the Government and MBIE, in consultation with stakeholders.

In our modelling of this scenario, we simply applied 30 percent of our estimate of AIAL's forecast non-aeronautical revenues to the aeronautical revenue requirement. We estimated AIAL's non-aeronautical revenues by simply inflating the latest annual report results by 2 percent per annum.

2.3.2 Aeronautical charges are lower across all route types in the Hybrid Till Scenario

Under the Hybrid Till Scenario, aeronautical charges are lower than the BAU charges. This applies across all route types.

Aeronautical charges will decrease for routes under the domestic flight class under a Hybrid Till Scenario

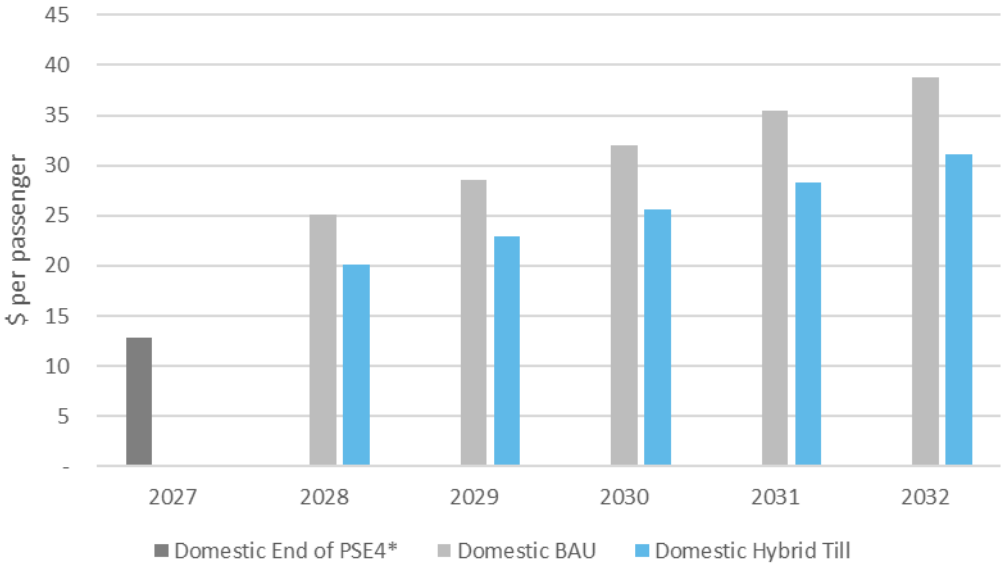
Under a Hypothetical Hybrid Till Scenario, aeronautical charges for routes under the domestic flight class are about 20 percent lower than those under the BAU Scenario. In FY28, airlines pay

[26] India's aviation industry has grown significantly since hybrid till revenue-setting was adopted. Capacity has increased, growing from 98 billion available seat kilometres in 2015 to 169 billion seat kilometres in 2023, an average annual increase of 7.05 percent per year. Demand has followed suit. Revenue passenger kilometres has grown by 7.83 percent per year from 81 billion to 148 billion. Directorate General of Civil Aviation. (2024). "Handbook on Civil Aviation Statistics". Available at: https://www.dgca.gov.in/digigov-portal/?page=4252/4205/sericename

[27] This has underpinned significant runway and terminal expansion in Bengaluru Airport (Bengaluru's second runway and Terminal 2).

$20.13 per domestic charge-paying passenger under the Hypothetical Hybrid Till Scenario, compared to $25.15 per passenger under the BAU Scenario. This means that airfares on routes under the domestic flight class will be $5.02 lower per passenger in FY28. By FY32, the final year of PSE5, aeronautical charges under the Hypothetical Hybrid Till Scenario increase to $31.07 per passenger, compared to $38.81 per passenger under the BAU Scenario.

Figure 2.5: Modelled aeronautical charges under the Hybrid Till Scenario—Domestic

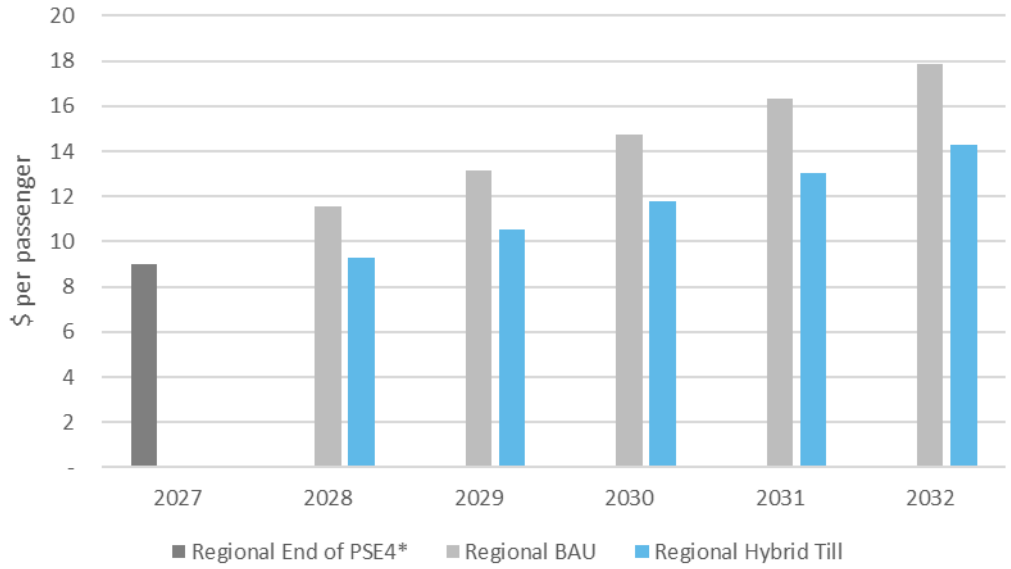


**Average of FY26 and FY27 aeronautical charges. "Auckland Airport lowers price increases; Commerce Commission confirms airport investment is reasonable". Available at: https://corporate.aucklandairport.co.nz/news/latest-media/news-articles/auckland-airport-lowers-price-increases*

Aeronautical charges will decrease for routes under the regional flight class under a Hypothetical Hybrid Till Scenario

Under a Hypothetical Hybrid Till Scenario, aeronautical charges for routes under the regional flight class are about 20 percent lower than those under the BAU Scenario. In FY28, airlines pay $9.27 per regional charge-paying passenger under the Hypothetical Hybrid Till Scenario, compared to $11.59 per passenger under the BAU Scenario. This means that airfares on routes under the regional flight class will be $2.31 lower per passenger in FY28. By FY32, the final year of PSE5, aeronautical charges under the Hypothetical Hybrid Till Scenario increase to $14.31 per passenger, compared to $17.88 per passenger under the BAU Scenario.

Figure 2.6: Modelled aeronautical charges under the Hybrid Till Scenario—Regional



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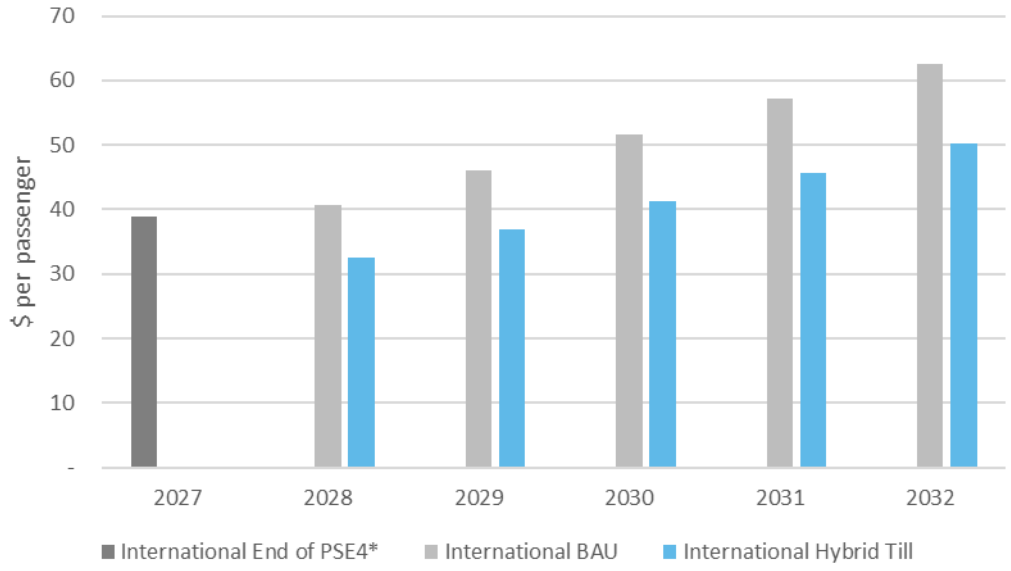
Aeronautical charges will decrease for routes under the international flight class under a Hypothetical Hybrid Till Scenario

Under a Hypothetical Hybrid Till Scenario, aeronautical charges for routes under the international flight class are about 20 percent lower than those under the BAU Scenario. In FY28, airlines pay $32.49 per international charge-paying passenger under the Hypothetical Hybrid Till Scenario, compared to $40.59 per passenger under the BAU Scenario. Airfares on routes under the international flight class will therefore be $8.10 lower per passenger in FY28. By FY32, the final year of PSE5, aeronautical charges under the Hypothetical Hybrid Till Scenario increase to $50.14 per passenger, compared to $62.64 per passenger under the BAU Scenario.

Figure 2.7: Modelled aeronautical charges under the Hybrid Till Scenario—International



**Average of FY26 and FY27 aeronautical charges. "Auckland Airport lowers price increases; Commerce Commission confirms airport investment is reasonable". Available at: https://corporate.aucklandairport.co.nz/news/latest-media/news-articles/auckland-airport-lowers-price-increases*

The Hybrid Till Scenario uses the following key assumptions:

Table 2.5: Hybrid Till Scenario scenario-specific assumptions

Assumption	Value(s)	Explanation
Percentage of non-aeronautical revenue subtracted from revenue requirement	30 percent	Based on the Indian aviation regulation policy
Non-aeronautical revenue	Retail income: $130.9 million Rental income: $170.6 million Rates recoveries: $12.7 million Car park income: $57.7 million Total non-aeronautical revenue: $371.9 million	From AIAL Annual Report 2024.[28] The model inflates this figure from 2024 to 2028, 2029, 2030, 2031, and 2032.
Non-aeronautical revenue inflation	2 percent	

[28] Auckland Airport. (August 2024). "2024 Annual Report" Available at: https://corporate.aucklandairport.co.nz/-/media/Files/Corporate/Annual-Report-2024/AIAL201-Annual-Report-2024-Book_v5c19.ashx

2.4 Single Till: AIAL's aeronautical charges using European-style single till regime

The Single Till Scenario demonstrates the effect of a common regulatory model used in several developed country airport regulatory regimes. Under a single till regulatory model, the regulator includes all airport activities in totality when determining aeronautical charges. The single till model is premised on an underlying assumption that an airport operator earns monopoly returns on all activities in the airport precinct. This includes both aeronautical business (aircraft landing/take-off, terminal/gate services, and aircraft parking) and non-aeronautical commercial activities (retail, hospitality, and logistics). AIAL monopolises (most, if not all) commercial activities at the Airport because it controls commercial developments and leases in the airport development area.

2.4.1 Single Till Scenario assumptions are illustrative only

The Single Till Scenario illustrates the effects of a European-style regulatory approach. The Government and Commerce Commission, in consultation with stakeholders, would need to determine the exact activities that fall within the single till (many overseas airports have some excluded activities) and may need to alter AIAL's expected return (WACC).

In our modelling of this scenario, we allocated 100 percent of our estimate of AIAL's non-aeronautical revenues to the aeronautical revenue requirement to calculate AIAL's regulated revenue. To estimate non-aeronautical revenues, we inflated the figures from AIAL's latest annual report by 2 percent per annum. To estimate regulatory earnings, we deducted AIAL's operating expenditures, also inflated by 2 percent per annum based on the annual report, from the estimated revenues. Based on the plant, property, and equipment section of AIAL's most recent annual report, we adjusted the RAB and depreciation charges to incorporate non-aeronautical assets.

For simplicity, we assumed that AIAL will target a 7.82 percent return, consistent with the most recent target return recommended by the Commerce Commission. The choice of WACC would be a key future regulatory decision. However, for the purposes of our analysis, it has only a minor impact on the differences between aeronautical charges in the scenarios.

Single till regulatory model incorporates all airport revenues when setting the revenue cap for aeronautical charges

Under a single till regime, aeronautical charges are determined based on the entire airport business. Both aeronautical and non-aeronautical revenues are considered when setting airport charges. The regulated return (revenue cap) is set with reference to the airport operator's RAB, depreciation, operational expenditure, and tax provisions. While the specific mechanisms vary, they generally follow a common pattern: the airport operator prepares charge proposals based on cost forecasts and investment plans, consults with airline stakeholders, and submits the proposals to an independent regulator for review and approval. In Europe, Heathrow, Gatwick (UK), Dublin (Ireland) and eight airports in France use single till.

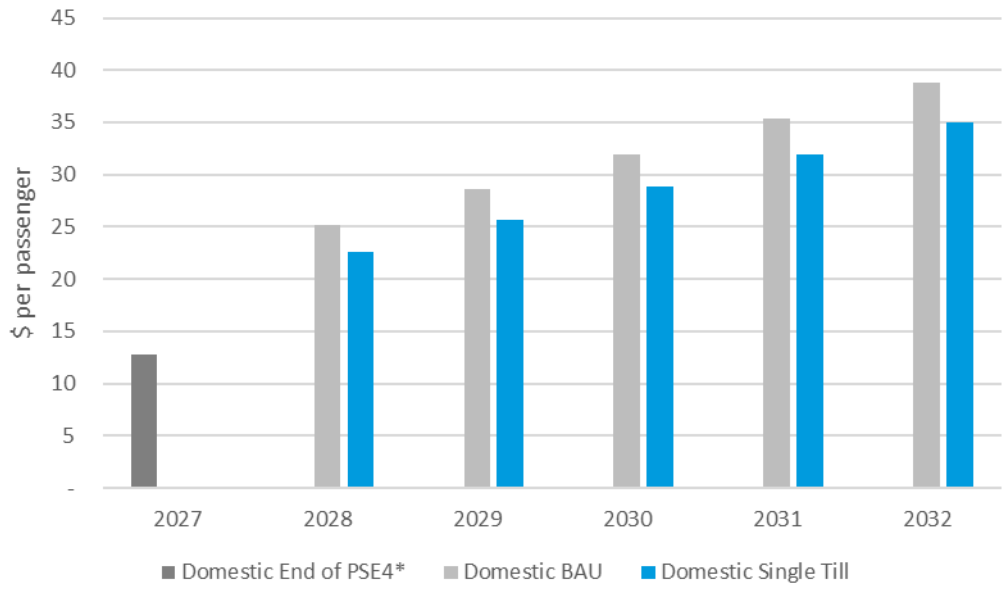
2.4.2 Aeronautical charges are significantly lower across all route types under the Single Till Scenario

Under the Single Till Scenario, aeronautical charges are significantly lower than BAU. This applies across all route types.

Aeronautical charges will decrease for routes under the domestic flight class under a Single Till Scenario

Under the Single Till Scenario, aeronautical charges for routes under the domestic flight class are about 10 percent lower than those under the BAU Scenario. In FY28, airlines pay $22.64 per domestic charge-paying passenger under the Single Till Scenario, compared to $25.15 per passenger under the BAU Scenario. Therefore airfares on routes under the domestic flight class will be $2.51 lower per passenger in FY28. By FY32, the final year of PSE5, aeronautical charges under the Single Till Scenario increase to $34.94 per passenger, compared to $38.81 per passenger under the BAU Scenario.

Figure 2.8 Modelled aeronautical charges under the Single Till Scenario—Domestic



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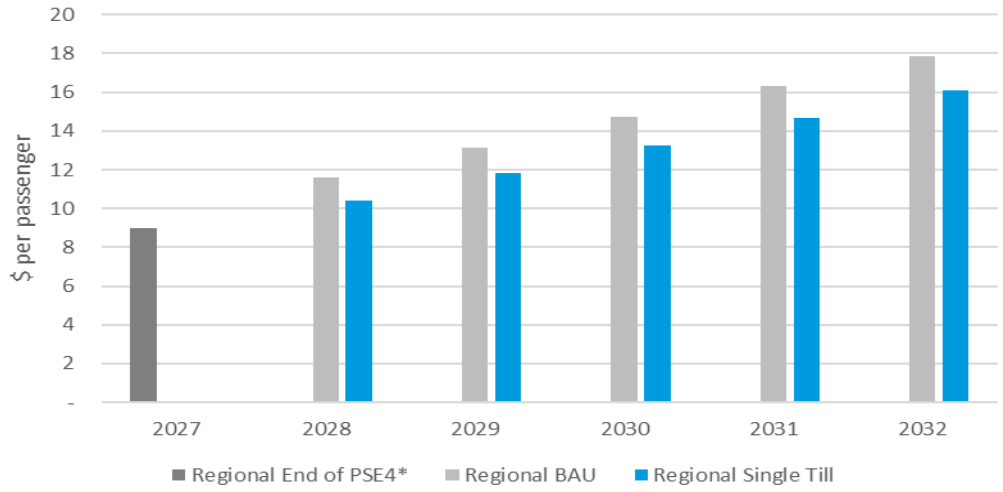
Aeronautical charges will decrease for routes under the regional flight class under a Single Till Scenario

Under a Single Till Scenario, aeronautical charges for routes under the regional flight class are about 10 percent lower than those under the BAU Scenario. In FY28, airlines pay $10.43 per regional charge-paying passenger under the Single Till Scenario, compared to $11.59 per passenger under the BAU Scenario. Airfares on routes under the regional flight class will therefore be $1.16 lower per passenger in FY28. By FY32, the final year of PSE5, aeronautical charges under the Single Till Scenario increase to $16.10 per passenger, compared to $17.88 per passenger under the BAU Scenario.

Figure 2.9: Modelled aeronautical charges under the Single Till Scenario—Regional



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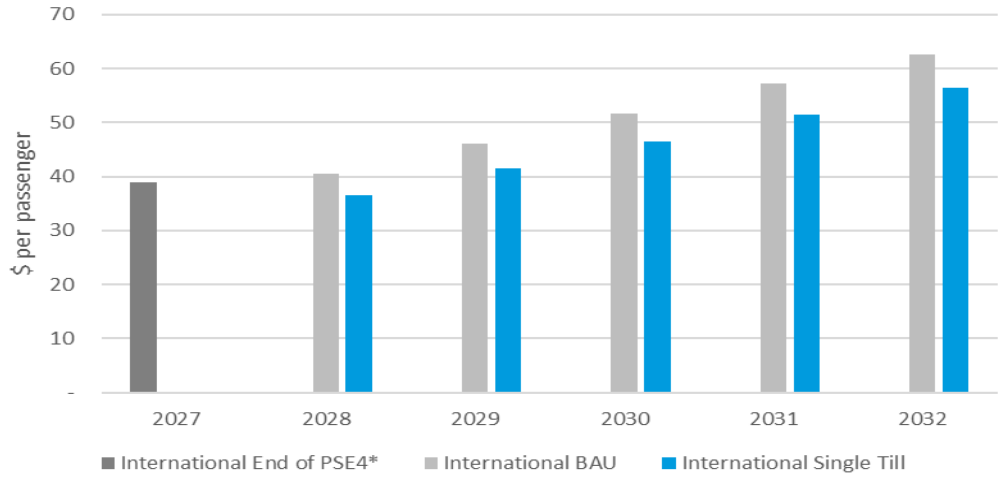
Aeronautical charges will decrease for routes under the international flight class under a Single Till Scenario

Under a Single Till Scenario, aeronautical charges for routes under the international flight class are about 10 percent lower than those under the BAU Scenario. In FY28, airlines pay $36.54 per international charge-paying passenger under the Single Till Scenario, compared to $40.59 per passenger under the BAU Scenario. Airfares on routes under the international flight class will therefore be $4.05 lower per passenger in FY28. By FY32, the final year of PSE5, aeronautical charges under the Single Till Scenario increase to $56.39 per passenger, compared to $62.64 per passenger under the BAU Scenario.

Figure 2.10: Modelled aeronautical charges under the Single Till Scenario—International



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The Single Till Scenario uses the following key assumptions:

Table 2.6: Single Till Scenario scenario-specific assumptions

Assumption	Value(s)	Explanation
Non-aeronautical revenue	2024: ▪ Retail income: $130.9 million ▪ Rental income: $170.6 million ▪ Rates recoveries: $12.7 million ▪ Car park income: $57.7 million ▪ Total non-aeronautical revenue: $371.9 million	From AIAL Annual Report 2024.[29] The model inflates this figure from 2024 to 2028, 2029, 2030, 2031, and 2032.
Operational expenditure	2024: ▪ Staff: $77.7 million ▪ Asset management, maintenance, and airport operations: $118.9 million ▪ Rates and insurance: $35.6 million ▪ Marketing and promotions: $9.7 million ▪ Professional services and levies: $11.7 million ▪ Other expenses: $13.7 million ▪ Total operational expenditure: $267.3 million	From AIAL Annual Report 2024.[30] The model inflates this figure from 2024 to 2028, 2029, 2030, 2031, and 2032.
Non-aeronautical revenue and operational expenditure inflation	2 percent	
Non-aeronautical RAB	2024: $918.7 million	Non-aeronautical RAB in 2024 calculated by subtracting the aeronautical RAB in 2024 (from AIAL PSE4 Pricing Disclosure[31]) from total plant, property,

[29] Auckland Airport. (August 2024). "2024 Annual Report" Available at: https://corporate.aucklandairport.co.nz/-/media/Files/Corporate/Annual-Report-2024/AIAL201-Annual-Report-2024-Book_v5c19.ashx

[30] Auckland Airport. (August 2024). "2024 Annual Report" Available at: https://corporate.aucklandairport.co.nz/-/media/Files/Corporate/Annual-Report-2024/AIAL201-Annual-Report-2024-Book_v5c19.ashx

[31] Auckland Airport. (August 2023). "Price Setting Disclosure – Schedules." Available at: https://corporate.aucklandairport.co.nz/investors/regulation

		and equipment (historical cost) from the AIAL Annual Report 2024.[32] Non-aeronautical RAB in 2028 is calculated by adding four years of "Additions to non-aeronautical RAB" to the non-aeronautical asset base in 2024 (from AIAL PSE4 Pricing Disclosure).[33]
Additions to the non-aeronautical asset base	$133.4 million per year	Average capital expenditure on retail and property development from the AIAL Annual Report 2024[34] over 2020-2024.
Non-aeronautical depreciation	$59.1 million per year	Average total depreciation over 202-2024 from AIAL Annual Report 2024,[35] less aeronautical depreciation in 2024 from AIAL PSE4 Price Setting Disclosure.[36]
Target return	7.82 percent	Commerce Commission Review of Auckland Airport's 2022-2027 Price Setting Event (March 2025).[37]

[32] Auckland Airport. (August 2024). "2024 Annual Report" Available at: https://corporate.aucklandairport.co.nz/-/media/Files/Corporate/Annual-Report-2024/AIAL201-Annual-Report-2024-Book_v5c19.ashx

[33] Auckland Airport. (August 2023). "Price Setting Disclosure – Schedules." Available at: https://corporate.aucklandairport.co.nz/investors/regulation

[34] Auckland Airport. (August 2024). "2024 Annual Report" Available at: https://corporate.aucklandairport.co.nz/-/media/Files/Corporate/Annual-Report-2024/AIAL201-Annual-Report-2024-Book_v5c19.ashx

[35] Auckland Airport. (August 2024). "2024 Annual Report" Available at: https://corporate.aucklandairport.co.nz/-/media/Files/Corporate/Annual-Report-2024/AIAL201-Annual-Report-2024-Book_v5c19.ashx

[36] Auckland Airport. (August 2023). "Price Setting Disclosure – Schedules." Available at: https://corporate.aucklandairport.co.nz/investors/regulation

[37] Auckland Airport. (March 2025). "Auckland Airport lowers price increases; Commerce Commission confirms airport investment is reasonable". Available at: https://corporate.aucklandairport.co.nz/news/latest-media/news-articles/auckland-airport-lowers-price-increases

2.5 Affordable Airport + Hybrid Till: AIAL's aeronautical charges with a more affordable airport development and a hypothetical Hybrid Till regime

The Affordable Airport + Hybrid Till Scenario models the aeronautical charges under a counterfactual scenario, if AIAL built a fit-for-purpose, but more affordable airport development and an alternative regulatory approach (hybrid till) is used where non-aeronautical revenue offsets some of the required aeronautical revenue.

2.5.1 Affordable Airport + Hybrid Till Scenario is illustrative of effects of fit-for-purpose lower airport capital expenditure and the hybrid till regulatory approach

Our modelling combines the effect of AIAL developing a lower-cost airport that still meets minimum quality standards and the standards of Air New Zealand and other key airline customers, while cross-subsidising aeronautical charges with non-aeronautical revenue.

This lower-cost airport terminal development is based on Arup Group's report on the Affordable Domestic Terminal pathway.[38] The Affordable Airport still meets minimum quality standards and the standards of Air New Zealand and other key airline customers. This lower-cost terminal would lower AIAL's revenue requirement by reducing the RAB on which it earns a return. Consequently, AIAL can lower the aeronautical charges it sets in PSE5, while still meeting its required return and serving medium-term demand, at an acceptable service quality level.

In modelling this scenario, we applied 30 percent of our estimate of AIAL's forecast non-aeronautical revenues to the aeronautical revenue requirement. We estimated AIAL's non-aeronautical revenues by inflating the latest annual report results by 2 percent per annum.

2.5.2 Aeronautical charges are lower across all route types in the Affordable Airport + Hybrid Till Scenario

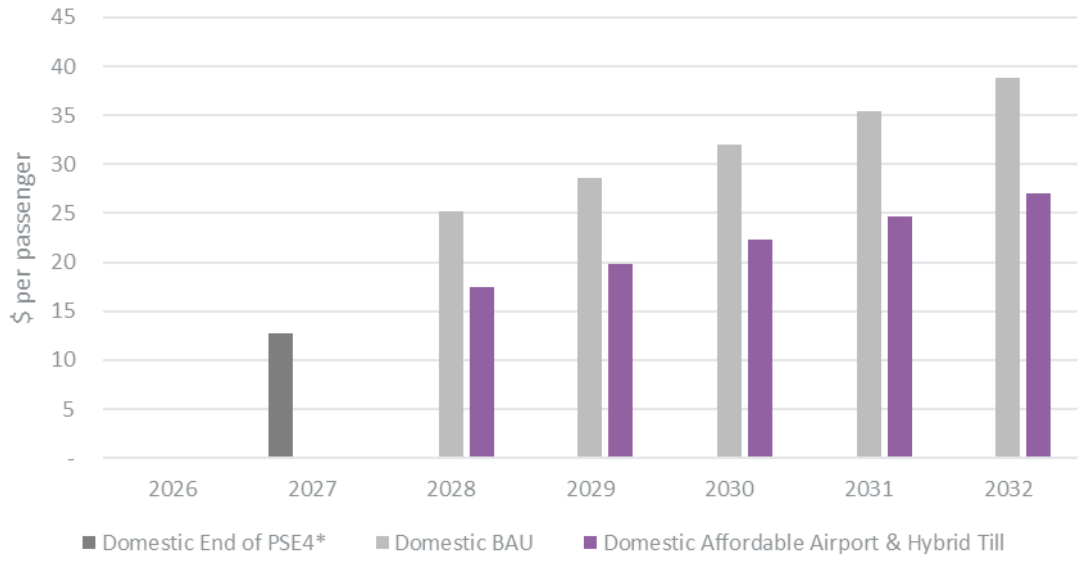
Under the Affordable Airport + Hybrid Till Scenario, aeronautical charges are significantly lower than BAU. This applies across all route types.

Aeronautical charges will decrease for routes under the domestic flight class under an Affordable Airport + Hybrid Till Scenario

Under an Affordable Airport + Hybrid Till Scenario, aeronautical charges for routes under the domestic flight class are about 30 percent lower than those under the BAU Scenario. In FY28, airlines pay $17.51 per domestic charge-paying passenger under the Affordable Airport + Hybrid Till Scenario, compared to $25.15 per passenger under the BAU Scenario. This means that airfares on routes under the domestic flight class will be $7.64 lower per passenger in FY28. By FY32, the final year of PSE5, aeronautical charges under the Affordable Airport + Hybrid Till Scenario increase to $27.02 per passenger, compared to $38.81 per passenger under the BAU Scenario.

[38] Arup Group. (April 2024). "Affordable Domestic Terminal Pathway". Available at: https://comcom.govt.nz/__data/assets/pdf_file/0035/358829/Air-NZ-Arup-Affordable-Domestic-Terminal-Pathway-April-2024-17-July-2024.pdf

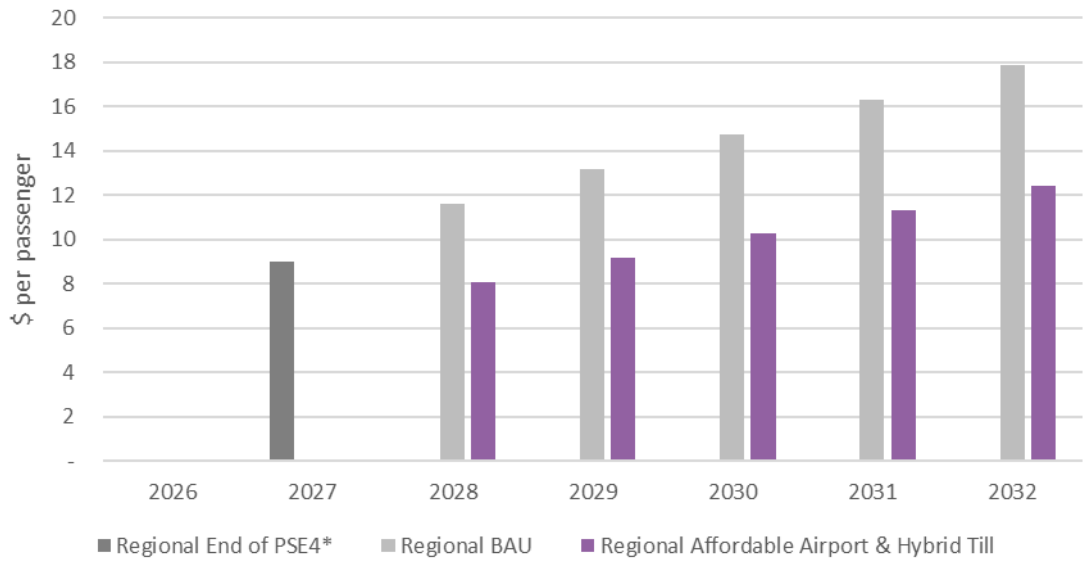
Figure 2.11: Modelled aeronautical charges under the Affordable Airport + Hybrid Till Scenario—Domestic



Aeronautical charges will decrease for routes under the regional flight class under an Affordable Airport + Hybrid Till Scenario

Under an Affordable Airport + Hybrid Till Scenario, aeronautical charges for routes under the regional flight class are about 30 percent lower than those under the BAU Scenario. In FY28, airlines pay $8.06 per regional charge-paying passenger under the Affordable Airport + Hybrid Till Scenario, compared to $11.59 per passenger under the BAU Scenario. This means that airfares on routes under the regional flight class will be $3.52 lower per passenger in FY28. By FY32, the final year of PSE5, aeronautical charges under the Affordable Airport + Hybrid Till Scenario increase to $12.45 per passenger, compared to $3.52 per passenger under the BAU Scenario.

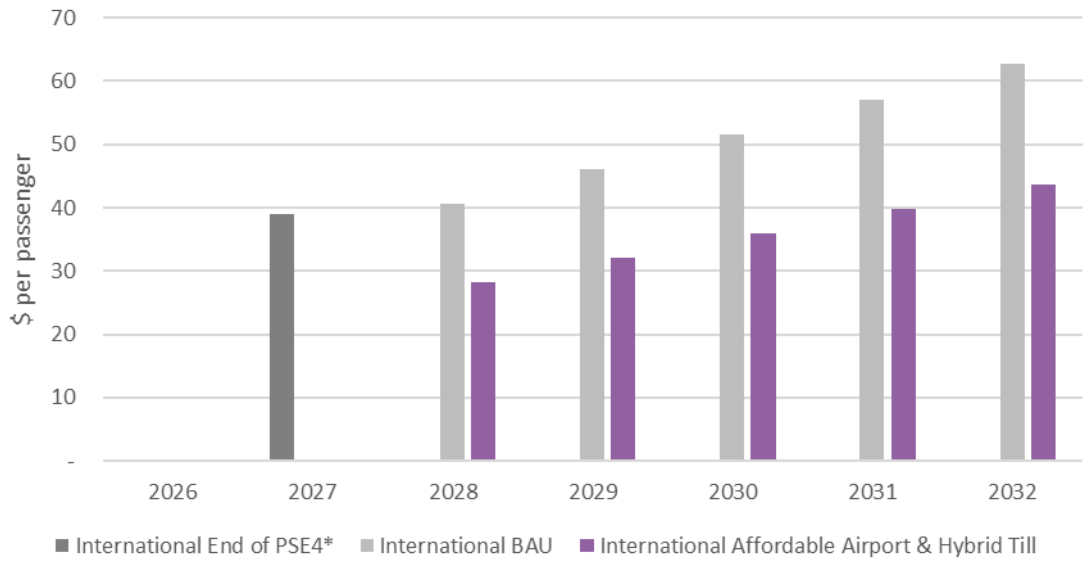
Figure 2.12: Modelled aeronautical charges under the Affordable Airport + Hybrid Till Scenario—Regional



Aeronautical charges will decrease for routes under the international flight class under an Affordable Airport + Hybrid Till Scenario

Under an Affordable Airport + Hybrid Till Scenario, aeronautical charges for routes under the international flight class are about 30 percent lower than those under the BAU Scenario. In FY28, airlines pay $28.25 per international charge-paying passenger under the Affordable Airport + Hybrid Till Scenario, compared to $40.59 per passenger under the BAU Scenario. Airfares on routes under the international flight class will therefore be $12.34 lower per passenger in FY28. By FY32, the final year of PSE5, aeronautical charges under the Affordable Airport + Hybrid Till Scenario increase to $43.60 per passenger, compared to $62.64 per passenger under the BAU Scenario.

Figure 2.13: Modelled aeronautical charges under the Affordable Airport + Hybrid Till Scenario—International



The Affordable Airport + Hybrid Till Scenario uses the following key assumptions:

Table 2.7: Affordable Airport + Hybrid Till Scenario scenario-specific assumptions

Assumption	Value(s)	Explanation
Cost reduction in assets commissioned into the RAB	2028: $1 billion reduction	Arup Group's report on the Affordable Domestic Terminal pathway[39] estimates that the domestic terminal could cost around $1 billion less than AIAL's capex plan, while meeting acceptable quality standards.
Percentage of non-aeronautical revenue subtracted from revenue requirement	30 percent	Based on the Indian aviation regulation policy
Non-aeronautical revenue	Retail income: $130.9 million Rental income: $170.6 million Rates recoveries: $12.7 million Car park income: $57.7 million Total non-aeronautical revenue: $371.9 million	From AIAL Annual Report 2024.[40] The model inflates this figure from 2024 to 2028, 2029, 2030, 2031, and 2032.
Non-aeronautical revenue inflation	2 percent	

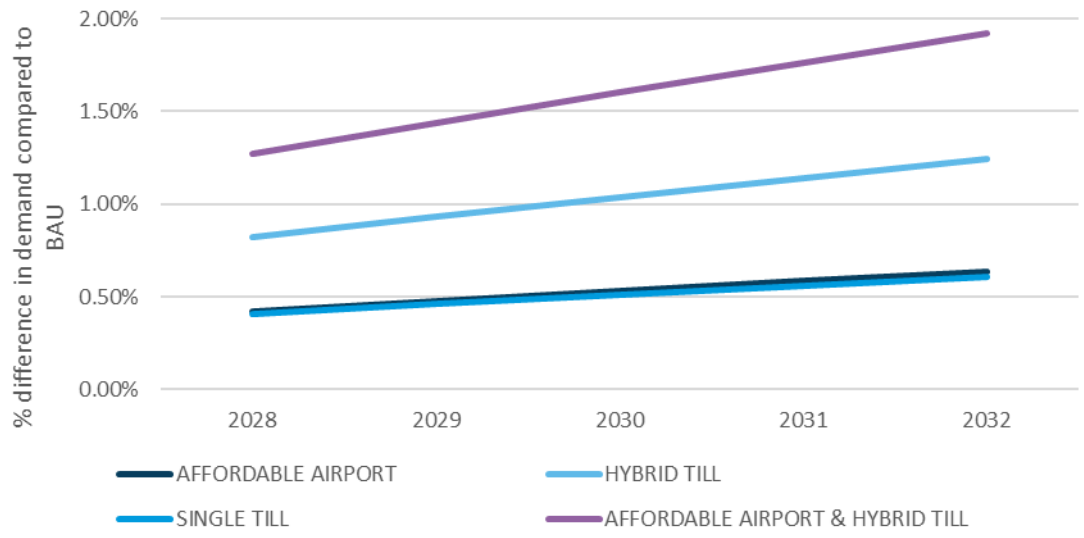
[39] Arup Group. (April 2024). "Affordable Domestic Terminal Pathway". Available at: https://comcom.govt.nz/__data/assets/pdf_file/0035/358829/Air-NZ-Arup-Affordable-Domestic-Terminal-Pathway-April-2024-17-July-2024.pdf

[40] Auckland Airport. (August 2024). "2024 Annual Report" Available at: https://corporate.aucklandairport.co.nz/-/media/Files/Corporate/Annual-Report-2024/AIAL201-Annual-Report-2024-Book_v5c19.ashx

3 AIAL's aeronautical charges affect New Zealand's aviation demand

AIAL's aeronautical charges impact New Zealand's aviation demand. Higher aeronautical charges are added to ticket prices, and passengers respond to price changes depending on how elastic their demand is. We have used flight price elasticities produced by BISOE to calculate how aviation demand changes under the counterfactual (Affordable Airport, Hybrid Till, Single Till) scenarios, relative to the factual (BAU) scenario. Figure 3.1 summarises how passenger throughput at AIAL differs under the three modelled scenarios compared to the BAU Scenario:

Figure 3.1: Total passenger volumes under counterfactual regimes, compared to BAU



3.1 Passengers are sensitive to changes in aeronautical charges

In 2023, Air New Zealand commissioned two reports by BISOE with flight price elasticities for passengers travelling to and from Auckland Airport. These *own-price* demand elasticities reflect how passengers respond to a change in airfares. We calculate the change in airfares resulting from the change in aeronautical charges[41] to estimate demand, using these elasticities, such that AIAL achieves its WACC.

[41] Assuming 100 percent pass-through of aeronautical charges onto passengers.

BISOE estimated elasticities for the following routes:

Table 3.1: Price elasticity of demand by route

[confidential and commercially sensitive]

Skylark Consulting Group ("Skylark") reviewed BISOE's analysis and concluded that BISOE's elasticities are mostly robust. For Domestic and International elasticities, Skylark found that BISOE's approach to its analysis was "in a reasonable way" given the available data. Skylark also found that long-haul (Asia, North America and South America) and Domestic elasticities are "credible and fall within the range of expected values considering the market and the impact of passenger mix."

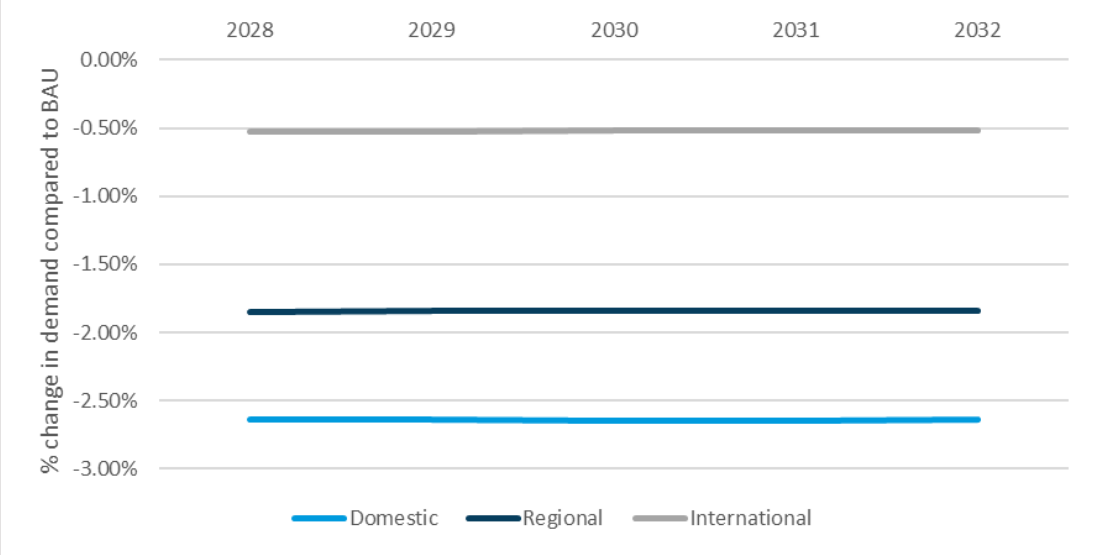
Skylark noted that "short-haul [Australia and the Pacific Islands] results almost certainly underestimate the impact of price increases on future traffic." [confidential and commercially sensitive].

Changes to the aeronautical charge regime affect aviation demand

Aeronautical charges under the counterfactual scenarios (Affordable Airport, Hybrid Till, and Single Till) are lower than under the factual scenario (BAU). Since our model (which reflects airlines' practices) assumes a 100 percent pass-through of aeronautical charges to airfares, aviation demand rises in three counterfactual scenarios compared to factual ones. Our model uses BISOE's elasticities for each route grouping to estimate the magnitude of these relative differences.

Box 3.1: Government-imposed regulatory charges will also depress aviation demand

Higher Government-imposed regulatory charges cause total aviation demand to be between 0.87 percent and 4.93 percent greater than under the BAU Scenario, depending on the year and route group. The decrease in aviation demand (relative to the BAU Scenario) due to increased Government-imposed regulatory charges is lower for international flight class than the domestic or regional flight classes, because routes under the international flight classes have lower elasticities.

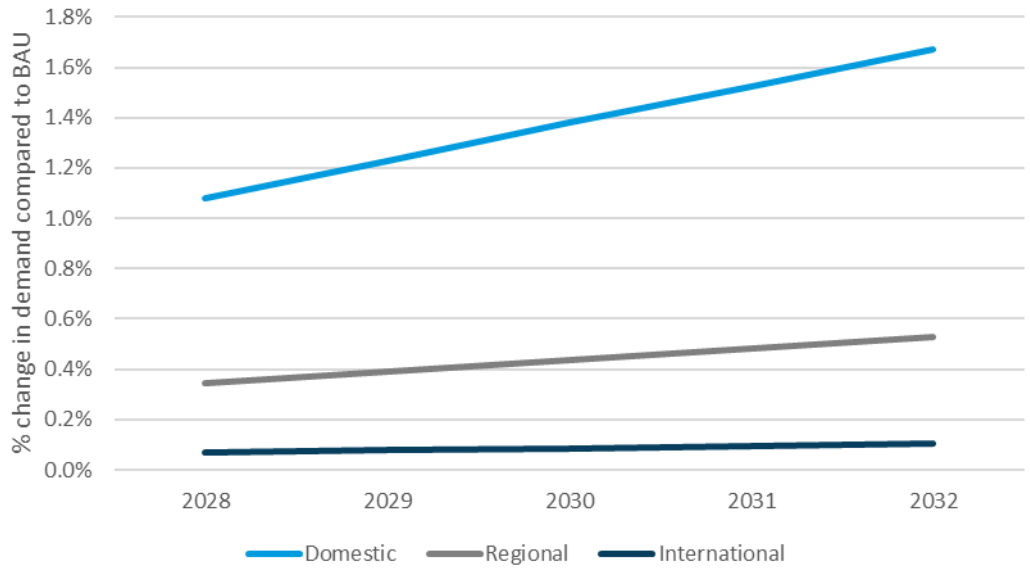


3.2 Affordable Airport Scenario

Under the Affordable Airport Scenario, aviation demand is between 0.11 percent and 3.00 percent greater than under the BAU Scenario, depending on year and flight class. Compared to other counterfactual scenarios, the Affordable Airport Scenario increases aviation demand by the lowest percentage (relative to the BAU Scenario) because aeronautical charges are higher than the Hybrid Till and Single Till Scenario charges.

Figure 3.2 summarises how aviation demand under the Affordable Airport Scenario compares to the BAU scenario for each flight class:

Figure 3.2: Increase in passenger volumes under the Affordable Airport scenario



Affordable Airport Scenario would result in higher passenger volumes compared to BAU for the international flight class

Under the Affordable Airport Scenario, aviation demand for the international flight class is between 0.11 percent and 0.26 percent greater than the BAU Scenario for a given year. Compared to the domestic and regional flight classes, aviation demand for the international flight classes under the Affordable Airport Scenario is only modestly higher than the BAU Scenario, because demand for routes under the international flight class is less elastic than other flight classes.

Appendix **Error! Reference source not found.** presents how passenger volumes under the Affordable Airport Scenario for specific routes within the international flight class compare to the BAU Scenario.

Affordable Airport Scenario will result in higher passenger volumes compared to BAU for the domestic flight class

Under the Affordable Airport Scenario, aviation demand for the domestic flight class is between 0.53 percent and 3.00 percent greater than the BAU Scenario for a given year.

Appendix **Error! Reference source not found.** presents how passenger volumes under the Affordable Airport Scenario for specific routes within the domestic flight class compare to the BAU Scenario.

Affordable Airport Scenario will result in higher passenger volumes compared to BAU for the regional flight class

Under the Affordable Airport Scenario, aviation demand for the regional flight class is between 0.34 percent and 0.53 percent greater than the BAU Scenario for a given year.

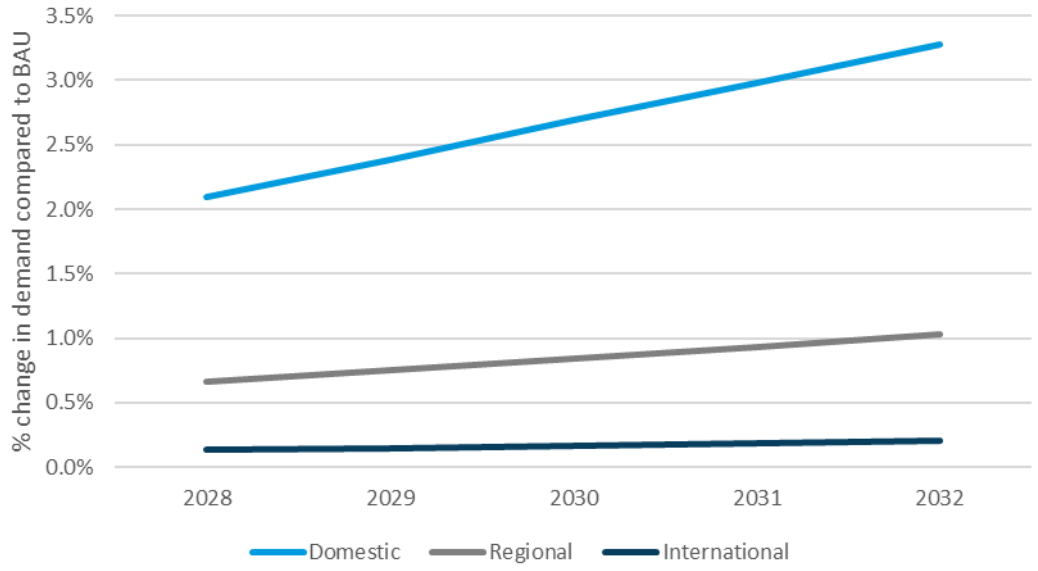
Appendix **Error! Reference source not found.** presents how passenger volumes under the Affordable Airport Scenario for specific routes within the regional flight class compare to the BAU Scenario.

3.3 Hybrid Till Scenario

Under the Hybrid Till Scenario, aviation demand for the domestic flight class is around 3.5 percent greater than BAU in 2032, with the impact on underlying routes varying between 0.22 percent and 5.90 percent greater than the BAU Scenario for a given year. Compared to the other counterfactual scenarios, the Hybrid Till Scenario increases aviation demand by the second highest percentage (relative to the BAU).

Figure 3.3 summarises how aviation demand under the Hybrid Till Scenario compares to the BAU scenario for each flight class:

Figure 3.3: Increase in passenger volumes under the Hybrid Till scenario



Hybrid Till Scenario will result in higher passenger volumes compared to BAU for the international flight class

Under the Hybrid Till Scenario, aviation demand for the international flight class is between 0.22 percent and 0.50 percent greater than the BAU Scenario for a given year. Compared to the domestic and regional flight classes, aviation demand for the international flight classes under the Hybrid Till Scenario is only modestly higher than the BAU Scenario, because demand for routes under the international flight class is less elastic than other flight classes.

Appendix **Error! Reference source not found.** presents how passenger volumes under the Hybrid Till Scenario for specific routes within the international flight class compare to the BAU Scenario.

Hybrid Till Scenario will result in higher passenger volumes compared to BAU for the domestic flight class

Under the Hybrid Till Scenario, aviation demand for the domestic flight class is between 1.03 percent and 5.90 percent greater than the BAU Scenario for a given year.

Appendix **Error! Reference source not found.** presents how passenger volumes under the Hybrid Till Scenario for specific routes within the domestic flight class compare to the BAU Scenario.

Hybrid Till Scenario will result in higher passenger volumes compared to BAU for the regional flight class

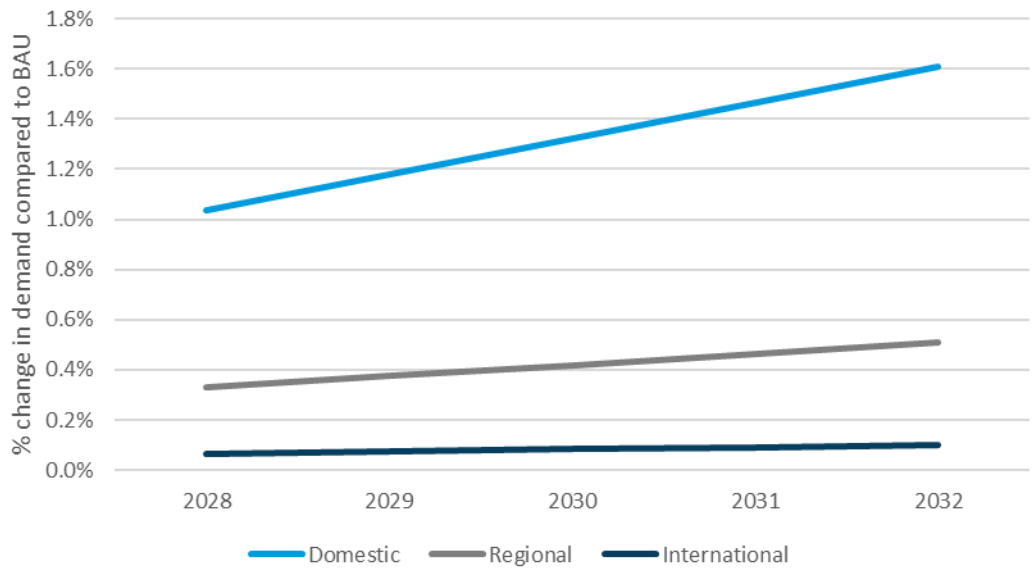
Under the Hybrid Till Scenario, aviation demand for the regional flight class is between 0.66 percent and 1.03 percent greater than the BAU Scenario for a given year.

Appendix **Error! Reference source not found.** presents how passenger volumes under the Hybrid Till Scenario for specific routes within the regional flight class compare to the BAU Scenario.

3.4 Single Till Scenario

Under the Single Till Scenario, aviation demand is between 0.11 percent and 2.88 percent greater than under the BAU Scenario, depending on year and flight class. Figure 3.4 summarises how aviation demand under the Single Till scenario compares to the BAU scenario for each flight class:

Figure 3.4: Increase in passenger volumes under the Single Till scenario



Single Till Scenario will result in higher passenger volumes compared to BAU for the international flight class

Under the Single Till Scenario, aviation demand for the international flight class is between 0.11 percent and 0.25 percent greater than the BAU Scenario for a given year. Compared to the domestic and regional flight classes, aviation demand for the international flight classes under the Single Till Scenario is only modestly higher than the BAU Scenario, because demand for routes under the international flight class is less elastic than other flight classes.

Appendix **Error! Reference source not found.** presents how passenger volumes under the Single Till Scenario for specific routes within the international flight class compare to the BAU Scenario.

Single Till Scenario will result in higher passenger volumes compared to BAU for the domestic flight class

Under the Single Till Scenario, aviation demand for the domestic flight class is between 0.51 percent and 2.88 percent greater than the BAU Scenario for a given year.

Appendix **Error! Reference source not found.** presents how passenger volumes under the Single Till Scenario for specific routes within the domestic flight class compare to the BAU Scenario.

Single Till Scenario will result in higher passenger volumes compared to BAU for the regional flight class

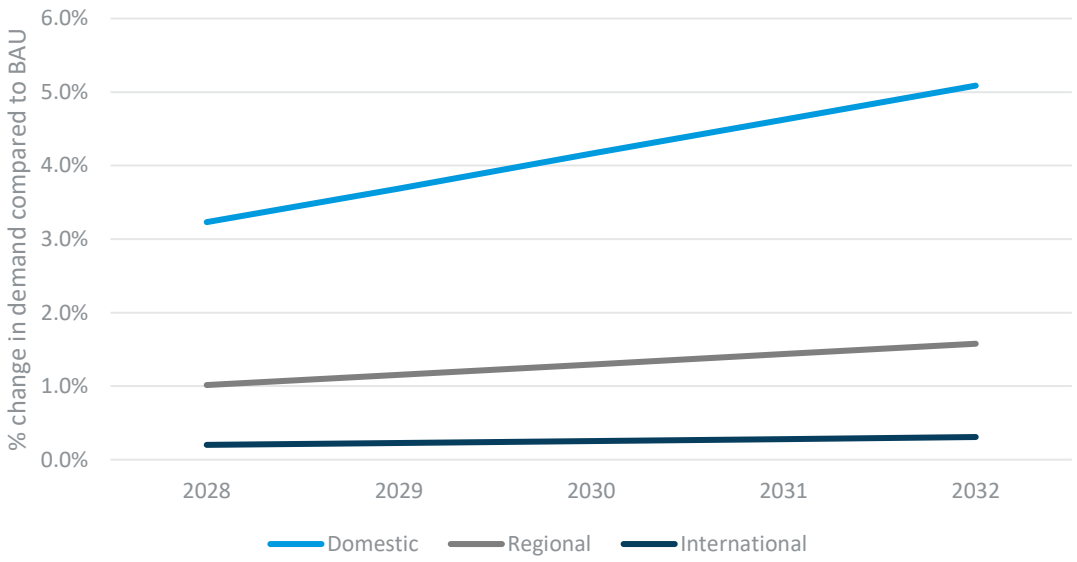
Under the Single Till Scenario, aviation demand for the regional flight class is between 0.33 percent and 0.51 percent greater than the BAU Scenario for a given year.

Appendix **Error! Reference source not found.** presents how passenger volumes under the Single Till Scenario for specific routes within the international flight class compare to the BAU Scenario.

3.5 Affordable Airport + Hybrid Till Scenario

Under the Affordable Airport + Hybrid Till Scenario, aviation demand is between 0.33 percent and 9.20 percent greater than under the BAU Scenario, depending on year and flight class. Figure 3.5 summarises how aviation demand under the Affordable Airport + Hybrid Till scenario compares to the BAU scenario for each flight class:

Figure 3.5: Increase in passenger volumes under the Affordable Airport + Hybrid Till Scenario



Affordable Airport + Hybrid Till Scenario will result in higher passenger volumes compared to BAU for the international flight class

Under the Affordable Airport + Hybrid Till Scenario, aviation demand for the international flight class is between 0.33 percent and 0.76 percent greater than the BAU Scenario for a given year. Compared to the domestic and regional flight classes, aviation demand for the international flight classes under the Affordable Airport + Hybrid Till Scenario is only modestly higher than the BAU Scenario, because demand for routes under the international flight class is less elastic than other flight classes.

Appendix **Error! Reference source not found.** presents how passenger volumes under the Affordable Airport + Hybrid Till Scenario for specific routes within the international flight class compare to the BAU Scenario.

Affordable Airport + Hybrid Till Scenario will result in higher passenger volumes compared to BAU for the domestic flight class

Under the Hybrid Till Scenario, aviation demand for the domestic flight class is between 1.58 percent and 9.20 percent greater than the BAU Scenario for a given year.

Appendix **Error! Reference source not found.** presents how passenger volumes under the Affordable Airport + Hybrid Till Scenario for specific routes within the domestic flight class compare to the BAU Scenario.

Affordable Airport + Hybrid Till Scenario will result in higher passenger volumes compared to BAU for the regional flight class

Under the Affordable Airport + Hybrid Till Scenario, aviation demand for the regional flight class is between 1.01 percent and 1.58 percent greater than the BAU Scenario for a given year.

Appendix **Error! Reference source not found.** presents how passenger volumes under the Affordable Airport + Hybrid Till Scenario for specific routes within the regional flight class compare to the BAU Scenario.

4 Choices for alternative regulatory regimes to promote the long-term interests of consumers

The BAU regime leads to high aeronautical charges, which depresses aviation demand. Other approaches to recovering the costs of airport infrastructure are comparatively better for supporting aviation demand, with the economic benefits it delivers to New Zealand. Under the BAU dual till regime, airports can pass on the full costs of expensive capital expenditure with only limited review and recourse for customers and stakeholders. Airports also do not have to share the benefits of non-aeronautical revenues with aeronautical customers, even though the demand for most of those services exists because of the airport's position and captive customer base.

Policymakers could choose one or both of the following approaches to address this issue:

- Make regulatory changes that strengthen control over AIAL's capital investment programme; and/or
- Adopt overseas best-practice regulatory models for high-performing, dynamic aviation sectors, which pool some or all of the airport's revenues.

4.1 Regulatory changes that strengthen control of AIAL's capital expenditure programme

The key issue for AIAL's customers is the cost of aeronautical infrastructure, and the service quality that airline customers receive. Airports have incentives to increase the costs of aeronautical infrastructure because they can pass on these costs, including the cost of capital, to airlines. The core weakness of the status-quo ID regime is that AIAL's capital expenditure plans are scrutinised ex-post with limited ability for customers to influence over-built, expensive investments. The Commerce Commission can comment, but it cannot amend or block investments that airlines will ultimately fund through charges. By strengthening controls over AIAL's capital expenditure programme, the negative effects of over-built or sub-optimal capital expenditure could be avoided. Focusing on regulatory-only changes, there are two broad options for this:

- Make the regulatory regime covering AIAL within the existing Part 4 Commerce Act paradigm more rigorous

- Provide AIAL's customers with veto rights over the capital expenditure programme.

4.1.1 Apply a more rigorous regime under the existing Part 4 paradigm

AIAL could be progressed from ID to more rigorous processes under the existing Part 4 paradigm. The key choices within the Part 4 framework include:

- Enhancing the current ID regime by introducing independent verification of the capital expenditure plan
- Price-quality regulation.

Policymakers will need to consider the effects of progressing AIAL into a more rigorous process under Part 4 in terms of balancing long-term consumer interests and the corresponding regulatory overhead costs. Independent capex verification directly targets the over-investment risk with lower compliance cost and fewer unintended effects on long-term productive and dynamic efficiency. Price-quality regulation would be a blunt tool to address the key concern of inefficient capital expenditure.

Independent verification of the capital expenditure plan under existing ID regime

AIAL could be required to have ex-ante independent verification of its capital expenditure. This would be a calibrated step-up, similar to the Transpower Capex IM process. It would oblige AIAL to submit each multi-year expenditure programme (and any major project above a materiality threshold) for pre-implementation verification by an independent engineering and cost-assurance panel appointed under a tripartite deed between AIAL, the Commission and the independent panel/advisor.

The goal would be to assure passengers and airlines that proposed projects are the least-cost means of delivering agreed service outcomes. The verifier would test the demand forecast, options appraisal, cost estimates and risk allowances, and publish a report that the Commission must consider before AIAL can capitalise the expenditure.

Independent verification preserves much of AIAL's commercial flexibility. Management retains the choice of timing and procurement method, but faces a credible risk that imprudent spending will be excluded from the RAB. That would improve internal governance without imposing a revenue cap. Because the mechanism focuses on the largest value drivers (for instance, the integrated terminal and pier expansion), the incremental regulatory overhead is modest. A verification cycle every five years, plus project-specific reviews, would cost less than a full price-path reset. This process would introduce an arms-length capital expenditure review by the verifier. It would also give airline customers a meaningful voice through submissions and cross-examination of the verifier's draft report.

Independent verification could add potential delays and result in asymmetric information issues for the verifier

Introducing an independent verification step, however, could add to the regulatory overhead costs faced by AIAL, airlines, and the Commission (all ultimately borne by air travellers). Airlines and AIAL already engage engineering experts to review the airport capital expenditure plans. Policymakers would need to test whether the marginal change in regulatory overheads from introducing an independent verifier would materially add to the total regulatory costs. It may duplicate AIAL's own investment case work. Extensive engineering, quantity surveying, and economic analysis would be required on top of the similar work AIAL would do to determine the optimal airport infrastructure. A verification step would also lengthen the time from investment decision to breaking ground on a new investment, which adds a holding cost

ultimately borne by consumers. The verifier must also rely heavily on AIAL's supplied data, which may still provide opportunities to over-specify the capex. Finally, the verification step could weaken AIAL's discipline to manage construction costs after the verifier's report has been accepted and construction has commenced. Cost increases could be more easily defended as matters outside its control or cost-creep, because the verifier already approved the base cost estimate ex-ante.

Price-quality regulation would add a layer of review for limited benefits

A second option is activating price-quality regulation under Part 4. This would shift AIAL onto the same footing as 16 of the 29 electricity line companies. The Commission would determine a five-year maximum revenue (or price-cap) path, reset WACC, and monitor compliance with quality standards (average queue times, and so on). While this would deliver comprehensive control over both prices and investment, it adds to the existing checks of airline consultation under the Airport Authorities Act, and ID disclosures with Commission oversight and final decision making.

Price-quality regulation would increase regulatory overheads without targeting the risk of over-specified capital expenditure

Several policy arguments speak against full price-quality regulation. The approach would impose higher regulatory overhead costs (which are deadweight costs). Preparing, auditing and litigating a full determination could probably cost tens of millions of dollars, a burden ultimately borne by travellers. It would also expose AIAL to regulatory standing risk, dampening investment incentives just as the airport enters a high-capex phase. International evidence suggests that where customers are few, well-informed, and already party to bilateral negotiations (as is the case with airlines), the marginal welfare gain from a revenue cap over strengthened capex assurance is small.

Imposing stricter control on prices and quality would not solve the real concern—whether AIAL's capital projects are sized and timed efficiently. Unless paired with a separate ex-ante investment test, a price-quality path still allows an airport to shift funds within its capex allowance. Price-quality regulation would offer broad protection, but lacks the nuance of identifying appropriate and efficient capital investments.

4.1.2 Provide AIAL's customers with significant input or veto rights over the capital expenditure programme

Several overseas regulatory regimes ensure that customers of key monopoly infrastructure have input into the capital expenditure programme. Some regulatory policy reasons need to be balanced when considering these types of customer input/veto processes.

Regulatory regimes that provide customer input or veto rights to infrastructure customers (such as airlines)

Several Australian regulatory regimes and the UK airports regime give customers either a veto right or strong influence over the monopoly infrastructure owner's capital expenditure programme. Examples of these regimes include:

- Australian electricity and gas networks are regulated by the Australian Energy Regulator (AER)
- Australian mining rail networks under access undertakings, ultimately regulated by the Australian Competition and Consumer Commission (ACCC)
- UK airports regulation and constructive engagement process.

These regimes ensure that the capital expenditure programme balances optimising for customers' needs while ensuring the monopoly infrastructure owner earns a reasonable return on investment.

Australian Energy Regulator and electricity and gas networks

In the Australian energy sector, networks that develop capital expenditure plans without customer support risk wholesale rejection or significant revision by AER. Customers and consumer representatives, therefore, have real leverage over both the size and timing of monopoly energy infrastructure owners' capital expenditure programmes.

The AER sets five-year revenue allowances under the National Electricity and Gas Rules, using a building-blocks model that aims to protect the long-term interests of consumers. Networks submit a regulatory proposal that must justify forecast capex, opex and service targets. The AER then tests it against prudence and efficiency criteria, financeability and the need to maintain reliability.[42]

Since 2024, the AER's Better Resets Handbook has increased the extent of consumer engagement. Networks that follow the "early-signal pathway" must publish an independent consumer report and show how engagement with consumers has shaped their capex plan. Poor engagement can trigger a more adversarial review.[43] The AER also draws on its Consumer Challenge Panel, made up of consumer representatives. In a regulatory regime trial of AER's "NewReg" with AusNet Services, AER empowered a Customer Forum to negotiate elements of the capex programme before lodgement.[44]

Australian Rail Track Corporation and Hunter Valley Coal Network Access Undertaking

Customers of major Australian rail track operators have an effective veto over the Australian Rail Track Corporation's (ARTC) capital expenditure programmes. ACCC oversees the "negotiate-arbitrate" regime for any infrastructure service that the National Competition Council recommends the Federal Minister should declare as a regulated service. Major infrastructure operators can enter into voluntary agreements that regulate access to the infrastructure service.

The Hunter Valley Access Undertaking, accepted by the ACCC under Part IIIA of the Competition and Consumer Act 2010, governs the ARTC pricing and investment in the coal export rail network. ARTC may only roll new spending into the RAB if the ACCC is satisfied it is prudent and efficient. This prudent and efficient threshold includes tests of long-run demand, cost allocation and competitive neutrality between existing and prospective coal producers.[45] There are important parallels between the Hunter Valley rail infrastructure and the airport in that both are used by a relatively small number of customers who compete with each other.

Prudence is presumed when projects are endorsed by the Rail Capacity Group (RCG), a monthly forum of access holders (mining companies and their rail service providers) whose votes are weighted by contracted tonnes. Both expansion and major sustaining projects must

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42 https://www.aer.gov.au/system/files/2024-11/State%20of%20the%20energy%20market%202024%20-%20Chapter%203%20-%20Electricity%20networks.pdf

43 https://www.aer.gov.au/system/files/2024-07/AER%20-%20Better%20Resets%20Handbook%20-%20July%202024.pdf

44 https://www.aer.gov.au/system/files/CEPA%20New%20Reg%20Final%20Evaluation%20Report.pdf

45 https://www.accc.gov.au/system/files/ACCC%20Final%20Determination%20-%20HVAU%20Annual%20Compliance%202017_1.pdf

clear the RCG before the ACCC will accept them. If endorsement is withheld, ARTC may proceed at its own risk but cannot automatically recover the cost through access charges.[46] RCG opposition has seen proposals deferred, rescaled or withdrawn entirely. The mechanism aligns investment with coal-chain efficiency, protects smaller customers from gold-plating and keeps entry barriers low by preventing incumbent-driven over-capacity.

Civil Aviation Authority (UK) constructive engagement negotiation

The UK airports regulator, the Civil Aviation Authority (UKCAA), mandates a Constructive Engagement negotiation process where the airport and its airline customers discuss capital expenditure options, service levels, and affordability before the UKCAA drafts proposals. Airlines have significant influence (but not a veto) through the combination of Constructive Engagement transparency and ex-ante incentive mechanisms. Airport capital expenditure that fails to demonstrate clear passenger benefits, cost efficiency and competitive neutrality faces a heightened risk of rejection or claw-back.

Under the Civil Aviation Act 2012, the UKCAA imposes price-control licences on airports with substantial market power, balancing its financeability against its primary duty to further users' interests and promote competition. It sets a five-year revenue cap (most recently H7 for Heathrow) after analysing traffic, cost of capital, efficiency benchmarks, and service-quality outcomes.

The Constructive Engagement process requires detailed cost breakdowns, option appraisal, and minutes of areas of agreement or dispute.[47] Airlines can block inefficient spending during Constructive Engagement informally. If consensus is not reached, the UKCAA arbitrates, informed by airline evidence and its own efficiency tests, and may disallow or stagger projects. From H7 onward, a new ex-ante capex-governance framework ties future cost recovery to meeting efficiency and output milestones, further disciplining over-investment.[48]

Balancing policy considerations in regimes with customer input or veto over capital expenditure

There are several policy considerations Air New Zealand should bear in mind if arguing for more input or a veto right by airlines over airports' capital expenditure programmes. Policy officials advising the Minister will be aware of these arguments.

Airline customers have shorter investment and business planning timeframes than airports. Airlines compete in a highly competitive market for air travel, where customers are price sensitive and most are not loyal to particular brands. Airports have much longer planning and investment horizons.

Such customer input or veto rights are unlikely to affect productive efficiency at airports. However, these rights can put dynamic (long-term) efficiency at risk, with knock-on effects for allocative efficiency. Airports (including AIAL) are likely to object to airlines having significant input or a veto right on this basis. Air New Zealand should be aware of this risk.

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[46] https://www.accc.gov.au/system/files/hvau-2022-capital-consultation.pdf; https://www.accc.gov.au/system/files/_Final_%202022%20Hunter%20Valley%20Annual%20Compliance%20-%20Final%20Determination%2817394719.14%29.pdf

[47] UKCAA, Letter to Heathrow Airport, 24 September 2024, available at: https://www.caa.co.uk/publication/download/22894

[48] UKCAA, Guidance on capital expenditure governance, November 2023, available at: https://www.caa.co.uk/publication/download/20795

A customer group dominated by incumbent users has a commercial incentive to block capacity expansion that would let new entrants access runway slots. If the veto delays or cancels projects with positive net social value, the airport gradually becomes capacity-constrained, service quality erodes, and potential future technologies (for example, larger aircraft or aircraft with different take-off/landing needs, such as electric or hydrogen aircraft) cannot be accommodated. This diminishes dynamic efficiency. Once capacity tightens, prices or access fees rise above the marginal cost of serving an additional user. The quantity supplied is held below the welfare-maximising level, and allocative efficiency also falls. In response to such a blocking power by its customers, airports would probably respond by under-investing, imposing a social cost.

4.2 Using all sources of airport revenue to underpin capital expenditure costs

The second broad option for reducing the effect of expensive aeronautical capital expenditure on aviation demand is to diversify the sources of airport revenue used to recover airport infrastructure costs. Commercial revenue pooling regimes apply income from an airport's non-aeronautical business towards the aeronautical charges airlines (and ultimately air passengers) pay. Both the hybrid till and single till approaches are globally proven. We first outline the policy reasons for applying commercial revenue pooling non-aeronautical income to aeronautical charges, and then compare the hybrid or single till regimes specifically.

4.2.1 Applying commercial revenue pooling regimes can balance promoting commercial returns with long-term consumer outcomes

Hybrid and single till regimes apportion commercial income towards aeronautical charges. The key policy justification for both regimes is that airports earn commercial revenues by virtue of their location and monopoly position. To the extent those margins are earned because of the monopoly position, this would meet the Part 4 section 52A(c)–(d) Commerce Act objectives to share efficiency gains and curb excessive profits.

Airport companies likely to claim that revenue pooling adds complexity, reduces their incentive to take risks and increases sovereign risk for New Zealand

AIAL and other airport companies are likely to object to a shift to a revenue pooling regime. The objections will probably cover:

- Added complexity and grounds for disputes may increase regulatory overhead
- Diverting non-aero revenue will blunt the airport company's incentives to take risks on non-aero projects
- Changing the regulatory regime ex-post will create sovereign risks to New Zealand.

We deal with each objection and potential response below:

Added complexity

Airport companies may argue that a new sharing factor can introduce new cost-allocation rules, true-ups and audit trails. Because all non-aeronautical revenue must be included alongside aeronautical revenue in pooling regimes, the forecasting burden can be much higher. Any forecast errors will translate into user charges. This raises the stakes of each price review, which would increase the volume of submissions. It would likely increase the risk of litigation over the inputs into cost forecasts. A key question, however, is whether this marginal

increase in complexity is higher than any other change to address the underlying policy concerns.

Reduced incentive to take risks on non-aero projects

Airport companies will claim that the commercial revenue pooling will blunt the incentive to take risks and will lower overall economic activity at the airport precinct. Knowing that future mall, car park, and other property development revenue will be applied to aeronautical charges may dull the airport's appetite for incremental, higher-risk projects, especially those on marginal land outside the core footprint. In AIAL's case, it would mean shareholders face the cost and risk of large aeronautical projects while capturing only a regulated return, which may make them more cautious and potentially delay projects or downsize projects below the long-run efficient scale.

There are counterarguments to this:

- Significant commercial investment has already proceeded at the airport precinct
- True-ups of actual revenues against forecasts are not necessarily required (true-ups occur in India, but not in many European airport regimes)
- Commercial revenue pooling may well reward AIAL because lower aeronautical charges will lift passenger numbers, according to our modelling. Higher passenger throughput boosts retail, parking, and hotel turnover, multiplying the value of the non-aero revenue share (70 percent in the Indian example), the airport still retains. The higher volume can offset the revenue diversion, leaving the airport with greater total EBITDA than under dual till
- Regulators can allow ring-fenced carve-outs. For example, Heathrow's cargo village is excluded from the single till calculation. Carve-outs would require detailed regulatory submissions in a complex process
- There is asymmetric risk transfer. The 30 percent share is determined from actual revenue. However, aeronautical charges are set based on forecast non-aero revenue. If forecasts are conservative (which is likely), the airport gets the difference on top of the 70 percent share.

Revenue volatility transfers to passengers

The revenues from non-aeronautical activities can be more cyclical than straight aeronautical activities, which means passengers would share the volatility. A mechanism to smooth out this volatility could be included in the regulatory regime. However, several European regimes avoid ex-post true-ups on the basis that airport commercial businesses are not much more volatile than the aeronautical business.

Financing capacity may be diminished, especially for large future capex programmes

Since revenues are pooled to recover aeronautical infrastructure costs, opponents of these regimes tend to argue there is insufficient retained cash to support borrowing for new capex programmes. This might be an issue where major capital expenditure programmes are planned, and significant borrowing is required. However, airports under pooling regimes, for example, at Heathrow in the UK, have been able to finance major capex programmes in the recent past[49] and the rapidly growing Indian aviation sector has not suffered from a lack of access to financing.

Introducing sovereign or regulatory regime risk to New Zealand

Airports will also argue that changing the rules of the game will increase New Zealand's sovereign risk and dissuade investors. They will claim a change to a commercial pooling regime will create a perception that the Government is willing to divert commercial business revenues to subsidise lower prices for the public (with benefits for the national airline), when presented with lobbying efforts.

However, there are several counterarguments to this:

[49] Heathrow media announcement, 18 December 2024, available at: https://mediacentre.heathrow.com/pressrelease/detail/21584

- Part 4 of the Commerce Act already expressly allows the Government to escalate regulation when the light-touch ID regime fails to protect consumers. It is likely to be a lawful application of Part 4 to introduce an IM that pools non-aeronautical income to determine allowable revenue
- It directly advances the purposes of Part 4 (set out in section 52A), specifically:
  - Section 52A(c): "*share with consumers the benefits of efficiency gains in the supply of the regulated goods or services, including through lower prices*". Diverting monopoly retail rents into the regulated revenue passes existing surpluses through to users
  - Section 52A(d): "*limited in their ability to extract excessive profits*". By offsetting commercial income, the airport's return on investment moves closer to the cost of capital, aligning with competitive-market outcomes.
- There is regulatory precedent in New Zealand for switching the regulatory regime 'mid-stream'. It is a legitimate use of regulatory authority to ratchet up regulation in response to investment cycles and consumer impacts:
  - Transpower shifted from ID only to price-quality and ex-ante independent capex verification when large capex programmes began
  - Non-consumer trust electricity distribution businesses graduated from a CPI-X regime to default and customised price-quality regulation when the previous regime proved inadequate.
- Such a shift would correct several decades of unshared economic rents (and a gradual shift from public/council ownership to private). The airport's strategic, bottleneck location and historical zoning protection created a quasi-natural monopoly that generated large commercial surpluses. Location rents are a classic policy rationale for redistributive regulation, akin to resource-rent taxes in mining
- Lower aeronautical charges resulting from commercial revenue pooling will lift aeronautical throughput towards the optimal and efficient scale for the airport. This reduces AIAL's unit costs and reduces AIAL's risk of owning a stranded asset. This is fully consistent with section 52A(a) by promoting AIAL's incentive to "*innovate and to invest, including in replacement, upgraded, and new assets.*"

4.2.2 Hybrid till has been successfully introduced in several growing aviation markets

The hybrid till model is proven in successful Asian aviation markets, such as in India. The regulator sets a building-block revenue requirement for aeronautical services and then offsets only a fixed proportion of forecast non-aeronautical revenue (for example, 30 percent in India) against that requirement. The remaining 70 percent of non-aeronautical revenue (for example, retail, parking, real-estate and other commercial income) is retained by the airport company. The Airports Economic Regulatory Authority of India (AERA) adopted this rule in its 2016 National Civil Aviation Policy and applies it in successive price orders for Kempegowda International Airport, Bengaluru (BLR) and other airports. The Indian aviation market has thrived under this model, completely transforming the air travel market. Several European airports have hybrid-style regimes where airport investment and profitability has been maintained.

By apportioning part, but not all, commercial earnings, the hybrid till delivers lower charges than a pure dual till approach (New Zealand's current approach). The hybrid till approach still gives the operator a strong incentive to expand its non-aeronautical business. It remains incentivised to develop profitable retail space, hotels or business parks that raise the overall attractiveness of the hub. Because only 30 percent is shared, the airport captures most upside from growth projects, supporting financeability for large capex. At BLR, this has underpinned significant runway and terminal expansion (BLR's second runway and Terminal 2). Passengers still benefit from a cross-subsidy that tempers aeronautical fees and therefore ticket prices.

Under the hybrid till approach, the regulator needs to be satisfied (either through ID or IMs) that:

1. Forecast aeronautical costs, demand, and WACC are reasonable
2. RAB is appropriately valued
3. Forecast non-aero income to apply the 30 percent (or other) sharing factor.

The first two steps mirror the current New Zealand process. The third step simply requires commercial forecasts to be made for the sharing factor to be included. It would therefore be a low incremental cost above the current regulatory overheads.

Hybrid till regime preserves the airport company's risk-taking incentives while acknowledging its monopoly location affords it the ability to earn high returns

The hybrid till model reflects the reality that commercial revenues arise partly from entrepreneurial risk-taking (for example, leasing land for or building hotels, retail, parking and logistics businesses on surplus land) and there are arguments not to fully socialise those revenues. However, because the airport earns returns in large part or only because the airport exists, returning part of the margin to passengers is equitable and mitigates the demand-suppressing effect of higher aeronautical charges.

The hybrid till is simpler than the single till with respect to calculating a regulated return on the airport's commercial activities. It simply applies a sharing factor from the commercial activities. Since AIAL's airport zone is large, there may be disputes over including activities at the fringe into the single till or not. A hybrid till can avoid this. The introduction of new rules is unlikely to be a significant step-up in regulatory compliance costs above the current BAU dual till regime, and in the long-run, will avoid disputes over capital expenditure budgets.

4.2.3 Single till regulatory model is proven at European airports

A single till regulatory model would treat the airport as one integrated business. The Commerce Commission would need to:

1. Calculate the building-blocks revenue requirement for aeronautical services
2. Forecast the net contribution from commercial activities (non-aeronautical revenue minus the costs of generating that revenue)
3. Deduct 100 percent of forecast net contribution from commercial activities from the aeronautical revenue requirement to determine the amount to be recovered from aeronautical charges.

The resulting net amount is then divided by forecast passengers (or aircraft movements) to set the price-cap for airport charges. The UKCAA applied this formula when setting Heathrow's H7

control.[50] The International Civil Aviation Organisation identifies the single till as the appropriate regulatory approach "*at airports where non-aeronautical revenues are generated from activities linked to passenger throughput*" in its Airport Economics Manual.[51]

Because every non-aeronautical dollar lowers the aeronautical bill by the same dollar, the airport has a built-in incentive to keep its costs down. Any overspecification of aeronautical infrastructure erodes its retained surplus. Passengers and airlines capture the full benefit of the airport's land-value rents.

Single till regime stimulates aviation demand and is used at several successful airports

There are several key reasons why the single till would promote greater aviation activity while also incentivising AIAL to invest in all airport and non-aviation businesses:

Single till incentivises investment at AIAL

A single till regime would ensure that the airport company bears the whole cost of any over-specified infrastructure, while recovering only prudently incurred capex through charges. The airport company management faces a strong discipline to pursue the least-cost solutions and defer low-value projects.

Single till promotes long-term benefits to consumers and shares efficiency gains

The single till regime fully socialises the retail, parking and property margins earned by the airport company. This aligns prices with marginal social cost, where margins are earned by virtue of the airport's location and monopoly position. To the extent those margins are earned because of the monopoly position, this would meet the Part 4 section 52A(c)–(d) Commerce Act objectives to share efficiency gains and curb excessive profits.

Positive regulatory outcomes in several mature markets

Mature airport hubs in the UK and Ireland (Heathrow and Dublin) have operated successfully under a single till for decades. Those airports have successfully financed multi-billion-dollar terminals and runways without evident under-investment. This reflects long-term dynamic efficiency outcomes.

[50] UK CAA (2022), Economic regulation of Heathrow Airport: H7 Final Proposals – Summary, Available at: https://www.caa.co.uk/publication/download/19735

[51] ICAO (2020), Economics Manual, fourth edition, Available at: https://www.icao.int/publications/Documents/9562_cons_en.pdf

Appendix A: Government-imposed regulatory charges

Table A.1 summarises the existing regulatory charges that Government imposes on air passengers, which air passengers they apply to, and when and if they will increase.

Table A.1: Government-imposed regulatory charges on air passengers

Regulatory charge	Paid by domestic passengers	Paid by international passengers	Effective date of increase
AvSec Security Charge[52]	Yes	Yes	1 July 2025
CAA Safety Levy[20]	Yes	Yes	1 July 2025
Border Clearance Levy (Biosecurity)	No	Yes	No change after consultation
NZ Electronic Travel Authority – Web[53]	No	Yes	Consultation ongoing
NZ Electronic Travel Authority – Web - App[53]	No	Yes	Consultation ongoing
International Visitor Conservation and Tourism Levy[54]	No	Yes	1 October 2024
Visitor Visa Fee[55]	No	Yes	Consultation ongoing

[52] Civil Aviation Authority. (January 2025). "Civil Aviation Authority confirms increases to levies, fees and charges." Available at: https://www.aviation.govt.nz/about-us/media-releases/show/caa-confirms-increases-to-levies-fees-and-charges

[53] Immigration New Zealand. (Retrieved April 2025). "New Zealand Electronic Travel Authority (NZeTA)." Available at: https://www.immigration.govt.nz/new-zealand-visas/visas/visa/nzeta

[54] Ministry for Business, Innovation and Employment. (Retrieved April 2025). "International Visitor Conservation and Tourism Levy." Available at: https://www.mbie.govt.nz/immigration-and-tourism/tourism/tourism-funding/international-visitor-conservation-and-tourism-levy

[55] New Zealand Immigration. (Retrieved April 2025). "Fees, decision times and where to apply." Available at: https://www.immigration.govt.nz/new-zealand-visas/preparing-a-visa-application/the-application-process/office-and-fees-finder

Appendix B: AIAL's aeronautical charges' effect on specific routes

[confidential and commercially sensitive]

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