

RELEASED WITH THE AUTHORITY OF THE MINISTER OF COMMERCE

SUMMARY OF SUBMISSIONS ON THE COMMISSION'S FINAL REPORT

	Matters in submissions
Wellington International Airport Limited	WIAL submits that the Minister is obliged by administrative law principles, and by the importance of the matters raised in the report to the interested parties, to consider the full submissions on the report and not just new matters. In any event, WIAL's submission relates to new matters in a sense in so far as WIAL has not previously had an opportunity to make submissions to the Commission on them. This is because those matters were not in the Commission's draft report, or the treatment of them has changed quite fundamentally since the Commission's conference.
Christchurch International Airport Limited (CIAL)	CIAL was concerned about the significant inputs to the Commission's decision that post-dated the conference. It was sympathetic to WIAL's unsuccessful application for judicial review on natural justice grounds.
	Current regulatory environment
Air New Zealand	The principle problem with the current price setting process is that the power to determine the outcome of consultation is fundamentally unbalanced, with one party having the ultimate ability to set charges as it from time to time thinks fit. The consultation process is an ineffective constraint on airport pricing. Challenge is generally only possible in respect of the process rather than issues of principle or substance, which are generally at the heart of the differences. Judicial review options are of limited utility.
BARNZ (also supported by Qantas and Air NZ)	Consultation under the Airport Authorities Act is very frustrating because the airport companies were neither reasonable nor moderate in their quest for shareholder profit. All 3 airports have sought to include assets in the asset base that were not necessary for the service being provided. 2 airports used a cost of capital substantially in excess of what the Commission considered reasonable. 2 valued land substantially above what the Commission considered reasonable. All 3 airports did not rigorously apply efficiency measures.
BARNZ (also supported by Qantas and Air NZ)	For the most part the airlines have provided sufficient information to enable the airlines to understand and meaningfully comment on the proposals. However, obtaining the information from AIAL and CIAL was a long, painful, drawn out process. In contrast, WIAL has been forthcoming and co-operative. Despite this, the holding of information has not given airlines sufficient countervailing market power to prevent the airlines from setting charges that contain monopoly rents.
Qantas Airways Ltd (submitted by Minter Ellison Rudd Watts)	The consultation requirement has not proved to be sufficiently robust to constrain monopolistic conduct (to varying degrees) by the major airport companies. For example, an airport company can manipulate its required revenue by overstating its future operating costs, tax obligations, depreciation expenses, WACC, and value of its assets; including in its asset base assets that are not necessary to provide the output; and understating prospective revaluation gains (or overstating losses).

Qantas Airways Ltd (submitted by Minter Ellison Rudd Watts)	Current consultation with WIAL has provided the airlines with considerable evidence that the company is manipulating its required revenue.
Air New Zealand	Commercial solutions are preferred. The Commerce Commission's report has provided a unique situation where airports may have a real incentive to reach a negotiated income. As such, Air New Zealand approached AIAL in an attempt to reach agreement on a framework for consultation on charging and on reducing the current level of landing charges. Discussions have not reached a point where it is clear whether AIAL will be prepared to settle on a framework based on the principles outlined in the Commission's final report. Similarly consultations with WIAL are continuing, and we ask that the Minister refrain from reaching a decision on control in respect of WIAL until the current process is complete. Air NZ also hopes CIAL will revisit its approach to pricing in respect of terminal charges.
Qantas Airways Ltd (submitted by Minter Ellison Rudd Watts)	In the case of all 3 airports, the availability of certain information has not particularly assisted the airlines in the consultation process and has not particularly assisted them with any effective countervailing power.
Wellington International Airport Limited	WIAL disagrees with the Commission's description of the purpose and effect of the Airport Authorities Act as being incomplete. The Commission fails to acknowledge the effect of the legislation and the crucial judicial interpretations of the application of that legislation. Judicial interpretation has upheld WIAL in all actions taken by the airlines, rejected the use of opportunity cost, rejected marginal cost approaches, and rejected economic efficiency purity generally. The Airport Authorities Act imposes unique obligations on airports.
Wellington International Airport Limited	WIAL notes an oversight by the Commission. The Airport Authorities Act provisions relating to the power of airport companies to fix charges includes an express exemption in relation to section 43 of Commerce Act. The effect of this provision is that the fixing of charges is not specifically authorised and is subject to the restrictive trade practice provisions of the Commerce Act.
	Status of competition in the market
BARNZ (follow up submission)	The Commission did not accept that airlines have significant countervailing power.
Graham Halstead & Associates	The three airports are effectively monopoly businesses in the regions they operate. Airline operators are a captive market. The only effective limitation on charges is the threat of price control.
Qantas Airways Ltd (submitted by Minter Ellison Rudd Watts)	Qantas agrees that competition in the market for the relevant airfield activities is limited. The airport companies are monopoly providers and the airlines' ability to exercise any countervailing power is extremely limited.
CIAL	CIAL is pleased the Commission has accepted that airlines have significant countervailing power that is manifested through the consultation process (10.50). CIAL's experience is that consultation is a significant constraint upon it. However, CIAL believes the Commission has still underestimated the extent of airlines' countervailing power.

New Zealand Business Roundtable	The potential for monopoly problems at AIAL does not justify a heavy-handed response on the analysis presented. Airports are constrained in their ability to abuse market power. This was confirmed by the Australian Productivity Commission in its inquiry into price regulation of airport services which found that commercial pressures and opportunities, particularly the non-aeronautical income to be had from promoting airline passenger traffic, was a constraint. NZBR adds that competition legislation, political pressures and the countervailing power of major airlines constrain the airports further.
Wellington International Airport Limited	The threshold of whether or not competition is limited is very low, as acknowledged by the Commission. WIAL considers the Commission has given insufficient weight to the countervailing power of airlines, as evidenced in examples given by WIAL to the Commission. WIAL disagrees that it accepted a finding that competition was limited for WIAL was inevitable. More importantly, WIAL notes that the Commission's finding that WIAL has "relatively high market power" is tentative and a lower standard than in other parts of the Commerce Act (ie. the new test of "substantial market power" in section 36).
Wellington International Airport Limited	WIAL considers that there are changes in competitive circumstances that were not apparent at the time of the Commission's conference. In particular, if the Air New Zealand and Qantas alliance proceeds it could significantly increase the countervailing power of airlines. In addition, the aviation market is volatile. Freedom Air has withdrawn all its domestic schedules with effect from October 2002. Its trans-Tasman services in WIAL's region will principally operate out of Palmerston North and, where they operate in Wellington, they will only displace an Air NZ schedule.
	Landing charges
Graham Halstead & Associates	It is difficult to reconcile the wide disparity in charges between the three airports. The only common factor is that charges have substantially increased between vesting in 1988 and 2001. Revenue from landing charges has increased at a rate nearly 3 times the CPI over this period and the submitter queries how much is due to growth and how much to excess pricing.
New Zealand Business Roundtable	The focus of competition policy should be on efficient prices. This policy would allow (non-predatory) pricing structures that investors were relying on to recoup long run marginal costs at the time those costs were incurred. This may be the only way investors can hope to recover sunk costs.
Auckland International Airport Ltd (AIAL)	The Commission's report has created a misleading perception that AIAL's airfield charges are too expensive. Of the 27 international carriers that use AIAL, only Air New Zealand has ever complained about the landing charges. The total landing costs at AIAL are the cheapest of the 3 airports for a 737-300 aircraft run domestically (i.e. \$745, as opposed to \$953 at WIAL and \$684 at CIAL). Landing charges are less than [] of an airline's total operating costs.
BARNZ (follow up submission)	AIAL's table of landing costs for a domestic 737-300 as proof that charges are at the lower end is misleading. When looking at landing and passenger charges, AIAL is comparatively expensive compared to other Australasian airports. AIAL is exceeded only by Sydney and Wellington.

BARNZ (follow up submission)	All airlines have issues regarding the level of AIAL charges. It is not just Air NZ complaining about landing charges. BARNZ has written authority to represent 22 airlines. Prior to the 2001 decision by AIAL not to increase charges, Singapore Airlines had declined to pay the second 5% increase.
	Opportunity cost principle for valuing asset base
Alliant Energy	The Commission's approach to opportunity cost has reduced the value of WIAL's asset base by some \$40 million. The practical effect of this is to nearly halve the valuation base upon which a fair return can be earned, which will naturally reduce the future income stream accordingly. We believe that opportunity cost, and its manifestation as scrap value for land and historic cost for improvements is not as robust as the current replacement cost methodology. Alternative, or scrap value, does not reflect the cost of a discounted airport service to the people of Wellington.
Auckland International Airport Ltd	Valuing land on scrap value is an extraordinary and ultra-hypothetical approach, which no business can afford to base sustainable prices on and which is not endorsed by the Commission's own expert valuers. AIAL's approach of valuing assets at the market value of the land in its existing use has not been questioned by the airlines.
Auckland International Airport Ltd	We agree in principle with the use of opportunity cost, however the Commission's overly simplistic interpretation is highly questionable and the approach is inconsistent with Australian regulators addressing similar issues. For example, the Commission uses an assumed value for the operational airfield of \$200,000/ha. which not only represents a figure lower than the mid-point of the identified range, but also seems to be based on a single referenced sale, rather than a more appropriate broader sample of benchmarked residential blocks zoned for urban development. AIAL's registered expert valuers (Seagar & Partners) advise that the Commission's advisors (Telfer Young) may have been unduly influenced by one particular sale for which Seagar & Young dispute the sales price provided. In addition, a correct sales analysis using a broader sample of sales would indicate a value between a range of \$250,000 - \$300,000/ha.
Auckland International Airport Ltd	AIAL's registered expert valuers (Seagar & Partners) advise that the final report does not properly separate the airfield land from AIAL's total land holding, such that the Commission has valued the 351 hectares of airfield land as part of an 825 hectare parcel. Seagar & Partners argue that the 351 hectares has obvious urban potential and should have been valued separately.
BARNZ (follow up submission)	AIAL has incorrectly stated the airlines do not question the use of market value existing use (MVEU) for land valuation. Airlines have consistently supported opportunity cost. MVEU is not appropriate to value land for pricing purposes where limited competition exists, as it reflects current use and returns. Current or future sustainable monopoly returns affect MVEU valuations.
Christchurch International Airport Limited	The Commission's focus on opportunity cost as an appropriate starting point for valuation complicates what is otherwise an entirely orthodox valuation issue. The application of this approach to value non-specialised assets in markets where competition is workable and effective demonstrates that the Commission is departing from real world standards.

Graham Halstead & Associates	Graham Halstead cannot accept the opportunity cost valuation methodology. Economic theory has dominated the report at the expense of business reality.
Graham Halstead & Associates	There are enormous hurdles in creating a new airport. Experience shows any new entrant would have to pay well above the opportunity cost market value to secure land. In addition, development costs (e.g. legal and RMA issues) and holding costs (interest and profit) would need to be taken into account. Agrees that there is greater subjectivity involved in replacement cost.
Infratil	The Commission's approach to valuation is wrong. The principle of opportunity cost implies a perfectly competitive market and is not appropriate for airports. The Commission focuses on the airport's value if it exited the market, where conventional models consider the value payable by a new entrant to the market. The view that income above opportunity cost is economic rent which equates to monopoly profit is wrong. It is wrong to measure opportunity cost only for the landowner and not the airport users. This approach is more consistent with regulatory, commercial and economic thinking. No one would build an airport for \$100 million if it could be valued at \$50 million the next day. WIAL paid approximately \$2 million per hectare for its terminal development and the Commission's scrap value approach values this land at \$450,000 per hectare.
The Special Utilities Investment Trust plc (SUIT)	SUIT has investments valued at £160 million worldwide in infrastructure and utilities, 20% of which is in the transport sector and mainly comprising of airports. It therefore has extensive exposure to different regulatory regimes. There have been numerous reviews by regulators of appropriate asset valuation methodologies for utilities such as airports and we are not aware of another regulatory agency anywhere choosing opportunity cost principles. At a simple intuitive level it is apparent such a model is highly unattractive to investors, as it would reduce approximately 25% of land values. SUIT has experience with both DHC and ODRC, and is comfortable that they can be made to work, but is not comfortable with the Commission's justification for switching from ODRC to DHC on the basis that it gets the closest to opportunity cost.
Wellington International Airport Limited	WIAL considers the concept of opportunity cost for land asset valuation to be seriously flawed. WIAL is operating its airport as a commercial undertaking. The land's use as an airport is its existing use, which is also considered to be its highest and best use. There is no foreseeable other use of the airfield land, which was acknowledged by the Commission in its report (para 5.99).

Wellington International Airport Limited	The Commission's adoption of opportunity cost ignores judicial rulings on the relevance of existing use of WIAL's land to the choice of valuation methodology. The High Court and Court of Appeal (in the 1992/1993 Air NZ WIAL cases) stated: "I do not think the alternative use valuation of \$17 million was one requiring emphasis. While one school of thought at least at times favours an alternative use approach as the minimum component of an overall valuation approach, for the present exercise it is highly theoretical. There will not be another use of Wellington airport, at least under existing aircraft technology" (page 79 of 1992 High Court judgement). "Value must mean its value as it is, enjoying its position as sole provider of airport services in the capital, but subject nevertheless to various actual and potential restraints against any abuse of its monopoly position" (page 9 Court of Appeal judgement). "The statutory direction is to behave commercially. The statute does not use the actual word efficient, let alone the phrase economic efficiency. I am not persuaded through the use of the word commercially it envisaged the economic efficiency purity of marginal cost pricing; short term, long term, or even with provision or recognition of alternative use opportunity cost valuation of land and coverage of future capital expenditure. Apart from the mere semantics, there are indeed a number of indicators rather to the contrary." (page 20, McGechan J).
BARNZ (follow up submission)	The Airport Authorities Act (as interpreted by the High Court) does not require airports to use MVEU to value land. The court cases have been in the nature of judicial reviews, and have held that WIAL's valuation methodology is within the bounds of reasonableness given the power to set charges under the Airport Authorities Act. These cases do not hold that it was the only available methodology or that it was economically efficient pricing.
Wellington International Airport Limited	The Commission provides assertion rather than argument to support opportunity cost as an efficient basis for pricing. It (inexpertly) dismisses the inconvenient views of experts rather than providing substantive analysis to support its views. WIAL considers that opportunity cost has significant detrimental economic efficiency implications. Opportunity cost will discourage efficient investment in land, and would not allow the airport to recover the cost of efficient improvements to land (e.g. the seawall). As this approach would result in writing off existing efficient investments, it would deter future investments that may also be adversely affected. This may impact on productive efficiency if the airport faces an incentive to substitute less efficient operating resources for capital expenditure, where that is feasible. In addition, if pricing is based on opportunity cost when the land is used as an airport, then prices would both be too high or too low and encourage an allocatively inefficient use of the airport.
Wellington International Airport Limited	Opportunity cost has no precedent in economic regulation in New Zealand or globally. It has been rejected as a methodology for valuing airport land in the United States. In <i>City of Los Angeles v United States Department of Transportation</i> No98 1071, USCA, District of Columbia Court, June 18 1999, the court rejected opportunity cost to value airport land because it was highly unlikely that the Los Angeles airport would be used in an alternative use. Opportunity cost was also rejected by the ACCC as a method for valuing Sydney Airport. In this case the opportunity cost was found to be higher than the value of the land as an airport and the ACCC rejected the methodology because of the practical problems of unnatural inflation of the value and prices of the airport.

BARNZ (follow up submission)	The City of Los Angeles case is not a relevant authority rejecting opportunity cost. The Los Angeles case involved rejection of opportunity cost in favour of historic cost as the means to value the land. The airport authority was seeking to use opportunity cost, but the airlines wanted historical cost to continue to be used.
Wellington City Council	Wellington City Council owns 34% of the shares in WIAL. The Commission's approach to opportunity cost is unconnected to reality. Accounting standard FRS 3 requires land to be valued at its highest and best use.
Wellington International Airport Limited	The Commission ignores the advice of its own expert valuers, Telfer Young, who accepted that fair value or Market Value Existing Use approach to valuing airport land. In its peer review of the Commission's draft report, Telfer Young recognised the MVEU zonal methodology as being the primary methodology for valuation, hypothetical subdivision DCF (as less preferred), and suggested the use of replacement cost as a check. Telfer Young were restricted from commenting on valuation methodologies in the final report.
Wellington International Airport Limited	The Commission obscures the extent of expropriation of WIAL's asset base by its adoption of opportunity cost. The Commission has excluded the recognised costs of transiting from bare land to an airport including any holding or levelling costs. Also excluded are costs that are regarded as subsumed in the opportunity cost of land, such as the seawall. The opportunity cost approach was not promoted by any interested party at the conference.
Wellington International Airport Limited	WIAL disputes the use of opportunity cost and the Commission's concept that "incentives to invest should be preserved subject to minimising the divergence of values from opportunity cost." The Commission does not explain what it means by this concept, and it contradicts its own finding that opportunity cost is quite inappropriate for sunk investments.
Wellington International Airport Limited	There is no evidence of overcharging by WIAL. The Commission has made an error and deducted the value of the seabed twice from WIAL's asset base. This is a \$16.5 million mistake and once corrected shows there are no excessive prices for airfield activities. If WIAL increased prices by [] in the current consultation round, it would still not generate excess returns in the 2001-03 period if this correction were made.
Wellington City Council	Wellington Airport is an asset vital to Wellington's current and future economic development. These attributes of the airport's location are ignored by the Commission's highly theoretical approach to valuation methodology, which values the airport land at its next best alternative use. Investment in alternative infrastructure such as roading for people to travel to an alternative airport would be excessive, as would lost time of people driving to an alternative airport.
BARNZ (also supported by Qantas and Air NZ)	The Commission's calculations of future returns at the three airports are understated as the Commission has not included future revaluations of the land (as measured by opportunity cost) as part of the return of each airport company even though it recognises that such revaluations form part of the airport's return. Assuming a conservative 3% increase in the value of land and using the Commission's land value, this means the excess returns at AIAL are understated by approximately \$2 million per annum.

Auckland International Airport Ltd	The Commission has valued airfield land at \$200,000 per hectare. In 1999 AIAL completed a reclamation the cost of which was \$580,000 per hectare, and which land has already been used for extensions to the taxiway. The reduction in average land value represents a revaluation loss of \$380,000 per hectare, which if correctly modelled should be reflected in the performance statement (calculation of airfield returns) in 1998 and 1999.
Auckland International Airport Ltd	The final report has switched to using the opening year asset values for calculating returns, rather than a mid-year average as was used in the draft report. This has a substantial impact on the calculation of excess returns, understating the value of the asset base by approximately 10%. It is presumably based on a misunderstanding of the Lally advice received by the Commission. Such an approach is highly dependent on the period chosen for the analysis. An annual approach implies a firm may need to wait up to 12 months before earning a return on its investment. This matter is new and has not been consulted on previously.
Auckland International Airport Ltd	The Commission has made a spreadsheet error by referencing the wrong cell in calculations the historical asset base. In line 27 of the "airfield" spreadsheet a reference is made to line 84, whereas it should refer to line 80.
Auckland International Airport Ltd	Deloitte Touche Tohmatsu advise that the appropriate asset base should include working capital and not just non-current assets, as returns are earned on all assets. It also advises of an error in the June 2000 balance, where the Commission has used a balance of \$309.2 million but AIAL's financial statements disclosed refer to \$312.7 million.
	Optimisation of asset base - "used and useful", treatment of future capital expenditure
Graham Halstead & Associates	Optimisation does not seem necessary for DHC, or at best should be examined as a secondary exercise only. The report appears to have an obsession with "over-optimisation".
Christchurch International Airport Limited	CIAL supports the Commission's conclusions that future investment may be included in today's prices and that pricing may involve a more long run perspective (4.25 and 4.26).
BARNZ (follow up submission)	The Commission did not authorise the automatic inclusion of future investment in today's prices. The Commission used the term "may" as a "possibility" rather than a permissive as CIAL has represented. The Commission stated that to include in prices the costs of such investments, it must be clearly demonstrated that such investments are efficient. BARNZ members still believe CIAL has inappropriately included the future terminal assets in its pricing model.
Auckland International Airport Ltd	The Commission would not have AIAL earn a return on its investment in the second runway land until construction begins. This is despite AIAL and the airlines being in agreement as to the necessity of a second runway in the short term, and all parties agreeing that AIAL acted prudently and rationally in acquiring the land and obtaining the necessary consents. The consequence is that AIAL has irrational incentives – either to immediately sell the land and wait to purchase at a higher price once congestion is high, or to begin construction immediately ahead of commercial timeframe.

BARNZ (follow up submission)	The airlines have not agreed with the need for a second runway in the short term. AIAL made a unilateral commercial decision to purchase the land for the second runway and for commercial development to the north of the existing runway. The airlines have no quarrel with this decision. Our consensus view is that it was a prudent purchase. It is misleading however to refer to the runway as being needed in the short term. We expect 2008 is the earliest date that the runway will be required. BARNZ members note the suggestion that AIAL now has the incentives to sell the second runway land, and notes that this would allow a potential new entrant to compete with AIAL and constrain prices to economically efficient levels.
Auckland International Airport Ltd	In excluding AIAL's second runway land the Commission has acted in direct conflict with the Airport Authorities Act 1966 (as amendment in 1997).
BARNZ (follow up submission)	The Airport Authorities Act does not authorise charging for land held for future use. The definitions of "airfield activities" and "identified airport activities" are merely a regulatory management tool to enable the management of the disclosure and consultation obligations contained within the Act and associated regulations.
Auckland International Airport Ltd	AIAL also disagrees with the Commission's decision to optimise out Wiroa Island from AIAL's airfield asset based on the grounds that it was no longer necessary. AIAL recently contacted Airways Corporation to confirm that date on which the radar station on the island became redundant. The Airways Corporation replied that, in their view, the assets are presently based on Wiroa Island are equally vital to navigation and Wiroa Island is therefore needed; and the present radar system was replaced on Wiroa Island in 1991 and therefore should not have been optimised out during 1988-1991 as the Commission has done in its analysis.
BARNZ (follow up submission)	Wiroa Island is not needed by AIAL. The majority of navigational aids around the country are situated on land not owned by airports. There is no requirement for AIAL to own the island and airlines should not have to provide AIAL a rate of return on the whole island's value.
Auckland International Airport Ltd	Deloitte Touche Tohmatsu advises that the revenue relating to the optimised assets – farm income on the second runway and the Airways Corporation rental of Wiroa Island – should be removed from AIAL's earnings to be consistent with those assets being optimised out, otherwise it will overstate earnings.
Auckland International Airport Ltd	The valuation methodology used by the Commission for removing the Wiroa Island and the Eastern approaches land from the asset base is different from the valuation methodology used by the Commission to value these assets in the opening vesting valuation. This produces obvious anomalies and errors in the resulting asset base calculations as well as the revaluation calculations.
Auckland International Airport Ltd	The Commission has failed to adjust the costs of depreciation in future years to reflect future capital expenditure and has only incorporated forecast levels of capital expenditure in its projections for the period 2001-04, but excluded any allowance for capital expenditure in 2005-07.
BARNZ (follow up submission)	AIAL alleges an error that the Commission failed to include CAPEX of \$12 million – despite the fact that no evidence has been provided as to whether this capital expenditure will be required and what it will be used for.

	Valuation of specialised assets – replacement cost, historical cost, FRS 3, midlife switching, revaluation gains, special treatment of airports
Graham Halstead & Associates	Valuation approaches used for determining market values and balance sheet values are not necessarily appropriate for examining whether price control should be imposed. Unadjusted HC valuations and ODRC could lead to false conclusions. Need to consider treatment of depreciation and extent of over-design or over-scale.
Auckland International Airport Ltd	The Commission has adopted a highly questionable and unprincipled “mix and match” approach to valuation and economic methodology. The majority view’s novel approach mixes historic and current costs. The use of DHC rather than ODRC is contrary to current valuation practices and inconsistent with what is used by the ACCC and NCC in Australia.
Wellington International Airport Limited	The Commission dismisses pertinent valuation and accounting standards seeking to obtain fair value of airfield land on the grounds that those standards enable monopoly profits to be earned. This is incorrect. These standards adopt detailed methods to find a market proxy. DRC is used on the basis that the non-contestable airport assets could not be created at the date of valuation at a lower price. This is what a new entrant would be willing to pay for the assets required for the airport operating in its existing use. The ODRC methodology has undergone considerable refinement over the years and is sophisticated and robust. The fundamental elements and concepts of valuation should remain the same regardless of whether the valuation is to be used for reporting or for pricing purposes. The Commission’s view that a different methodology should be used for pricing is unique, promotes the notion of the company having multiple books of accounts, and ignores that any assessment of company performance is likely to be on the basis of accounting information.
Major of Christchurch	The Commission’s approach to valuation represents a radical and unwarranted departure from widely accepted valuation principles.
New Zealand Business Roundtable	We have not closely studied the choice of asset valuation methodology that split the Commissioners and do not have a firm position on the issue.

<p>Wellington International Airport Limited (follow up submission) CONFIDENTIAL</p>	<p>[</p> <p style="text-align: right;">].</p>
<p>Air New Zealand (follow up submission) CONFIDENTIAL</p>	<p>[</p> <p style="text-align: right;">].</p>
<p>Christchurch International Airport Limited</p>	<p>The purpose of a valuation is to approximate a hypothetical market transaction. Market value and fair value are synonymous concepts. The Commission wrongly rejects the concept. CIAL considers that economics does not mandate some alternative valuation methodology, whether assets are specialised or not. In the absence of a market for specialised assets, ODRC is a proxy for market value as it estimates the value of those assets to a new market entrant. The Commission has been forced to acknowledge that ODRC and DHC methodologies are equally supportable and this is a significant change from the draft report. CIAL considers that ODRC is preferable.</p>
<p>Graham Halstead & Associates</p>	<p>Treatment of depreciation should be uniform across the airports. The submitter assumes that depreciation of assets relates to buildings and the like and not land or runways.</p>

Christchurch International Airport Limited	At the conference, so far as CIAL is aware, no party advocated DHC other than Simon Terry Associates. STA appear to have had an influence will beyond what may have been expected. Even the airlines did not strongly advocate DHC. The consequences of adopting DHC would be significant. CIAL's sealed surfaces would be devalued by \$20.03 million (10.62) and airfield land values increased by \$16.5 million (10.80). Such arbitrary and substantial adjustments indicate there is something wrong with the Commission's approach.
Powerco	ODRC should be adopted. DHC methodology is not warranted.
New Zealand Property Institute – Valuation & Property Standards Board	The Commission's final report challenges established valuation principles currently adopted by NZ Property Institute members. Valuers currently use ODRC. Members moved away from historic cost in the 1980's and to return to that basis of valuation would be inconsistent with international trends. The NZ valuation standards are closely aligned with the International valuation standards, which require the valuation of specialised assets at DRC. DRC is an assessment based on the replacement of the existing asset in its modern equivalent form to the actual level of capacity or service potential. Land values are also to be determined by valuers competent in that particular market. It would be a backward step to require airports to revert back to historic cost. The use of historic cost could result in meaningless balance sheets with significant discrepancies within the industry.
Wellington International Airport Limited	The Commission had an opportunity to independently verify the outcomes of the airports' applications of ODRC methodology to non-land (specialised assets) but chose not to. The Commission engaged the services of Telfer Young in a peer review of airport valuations in mid 2001, but did not use this information. It is inappropriate for the Commission to dictate a drastic change in valuation methodology mid-stream when it has not verified the outcomes of the airport valuations.
Wellington International Airport Limited	There is no basis for the Commission's concerns with the transaction costs associated with the use and monitoring of ODRC valuations. WIAL knows the actual costs of reconstruction on its runway, so the cost of assessing these specialised assets is limited. In comparison, WIAL valuers have not been able to find suitable information on historic costs of creating Wellington Airport. Historic cost would also require tracking and recording all the additions and changes throughout the life of the asset. A large proportion of WIAL's specialised assets have been renewed, replaced, and improved since their initial construction. Suitable records of these transactions are not available except for the most recent additions.
Wellington International Airport Limited	The ACCC has adopted ODRC in respect of specialised (non-land) assets.
Wellington International Airport Limited	The Commission majority find that, theoretically, there may not be a lot to choose between DHC and ODRC providing they are both implemented correctly and consistently over their lives. However, they conclude that the Commission has to exercise regulatory judgement and force the use of DHC on airports. WIAL disagrees with the majority's arguments. WIAL supports the minority views. That is, New Zealand is quite different from overseas regimes where DHC is used in combination with a regulatory compact of a guaranteed rate of return. In addition, ODRC has more efficient properties than DHC, it is no more complex, and using a mix of historical cost and opportunity cost creates an uncomfortable hybrid of historical and current costs.

Auckland International Airport Ltd	The Commission's statement in its final report that it has yet to come across any independent academic support for the use of replacement cost-type approaches in the literature is difficult to accept. An independent report by NERA, commissioned by AIAL, included a number of specific references. The Commission makes no reference to this literature or to the reasoning used by both the ACCC and the National Competition Council in Australia for applying ODRC valuation principles as the right competitive market benchmark.
Auckland International Airport Ltd	The Commission has not commented on the fact that AIAL's major gateway airport competitor – Sydney Airport – is valued and sets its charges based on ODRC. The adoption of DHC will run counter to the government's policy of establishing a single aviation market between NZ and Australia, and will distort capital market investment signals in relation to the competing airports in both countries.
Auckland International Airport Ltd	The Commission's valuation approach represents a clear departure from the Government's previous shareholder directive to AIAL's Board in 1998 to "revalue assets in the books of the company using ODV concepts." It also runs counter to FRS-3 and the Valuation & Property Standards of the NZ Property Institute.
Auckland International Airport Ltd	The use of the original vesting valuations applied to AIAL on initial privatisation in 1988/89 has been widely criticised (e.g. Forsyth Barr). Virtually every New Zealand utility company that has been privatised or corporatised since the mid-80's has switched from DHC to ODRC to value its assets.
Auckland International Airport Ltd	The Commission states that its preference for DHC for valuing specialised assets of airports does not set a precedent for other industries. However, it does not justify the use of DHC in the case of airports and why airport assets should be different from other industries.
Auckland International Airport Ltd	Listed companies like AIAL are required to value assets on the basis of FRS 3 (which endorses ODRC and not DHC as a fair value basis). The final report raises the spectre that international and local investors will no longer be able to place reliance on stipulated accounting standards.
BARNZ (also supported by Qantas and Air NZ)	FRS 3 provides that where extensive works have been carried out on land, then the fair value of land should be determined by having regard to the replacement cost of the land. In the Commission's view these reclamation costs were captured in the opportunity cost of the land. BARNZ agrees with the Commission that financial reporting standards are not relevant when determining the efficiency of asset allocation or setting economically efficient prices. A letter from Professor RG Bowman, Professor of Finance at the University of Auckland confirms that FRSs are not authoritative for the purposes of pricing.
BARNZ (follow up submission)	It is incorrect to claim that the Commerce Commission's decision to use HC to value specialised assets is inconsistent with the Financial Reporting Standards, and it is incorrect to claim that the FRSs require the airports to use ODRC. The FRSs set out the valuation methodology to be used if it chooses to revalue its assets. They do not require a company to revalue. FRSs relate to financial reporting not values for other purposes such as determining economically efficient prices. The majority of NZ companies use HC.

Christchurch International Airport Limited	The Commission acknowledges that ODRC is the methodology supported by valuation standards for disclosure purposes (5.68). However, it asserts that disclosure is a different process than the control inquiry and that the Commission is seeking “economically efficient” prices as if this is something different. By contrast, disclosure is designed to facilitate the setting of economically efficient prices and we do not understand the point the Commission is trying to make.
Wellington International Airport Limited	Infratil shareholders purchased the government’s 66% shareholding in Wellington Airport. They made that investment relying upon the value that the government had placed on WIAL’s assets and the regulatory regime that applied, and still applies, to the airport industry. It is unacceptable for the government to sell assets on the basis of a particular value and then later approve a valuation methodology to apply to those assets, which will wipe millions of dollars off the value of the assets it sold to investors. If the government does not firmly reject the Commission’s asset valuation principles the level of regulation in the airports industry will be increased without a government decision to do so.
Graham Halstead & Associates	Agrees that DHC is a less subjective measure of asset values, as values are based on vesting date valuations – assuming that these values are what the airport companies paid for the airfields and these figures represent HC at vesting date. Considers that optimising is not necessary for DHC. Notes that HC does not take into account changes in growth and profitability. As a minimum, HC must be adjusted for inflation (and suggests CPI is a simple tool).
Wellington International Airport Limited	The Commission does not provide net economic efficiency grounds supporting DHC over ODRC. At best the discussion in paras 5.45 to 5.52 represent issues to be traded-off, but the majority does not express a firm view either way. In contrast, the minority Commissioners do support their view on efficiency grounds. Similarly, the Commission’s discussion of distributional effects in paras 5.73 to 5.74 appears to be agnostic on both methodologies, even the finding in para 5.83 gives weight to those paragraphs.
Wellington International Airport Limited	The Commission majority emphasised that their preference for historic cost valuation of specialised airfield assets reflects the special circumstances of the airfields inquiry and should not be taken to indicate the Commission’s position with respect to the valuation of other utilities. WIAL submits that it would be ridiculous to adopt different approaches in different sectors and any such distinction for airports is unjustifiable.
Christchurch International Airport Limited	There is no rational reason why airports should be treated differently from other utilities in New Zealand. The Commission appears to be influenced in its decision by how the three airports had treated valuations of their own assets. This point of distinction is completely new and has not been consulted on. It is a bizarre argument that relies on the historical treatment of costs by the three airports as justification for the choice of methodology. The Commission has apparently jumped to the conclusion that airports were revalued so as to manipulate landing charges. This ignores the airports’ operating environment. 40 to 50 years ago, airports as standalone entities and current accounting standards for reporting revaluations did not exist. Airports could not do anything other than revalue the assets in mid-life. In addition, CIAL has always used forward-looking methodologies for the purposes of setting landing charges. In 1988, CIAL set landing charges by reference to vesting values based on ODV, being DCF. In 2000, CIAL set its charges using ODRC. While its balance sheet has changed from historical cost to ODRC, CIAL has not switched its approach to pricing.

Wellington International Airport Limited	The Commission majority is wrong in saying that WIAL first used DRC as late as 1995. WIAL has not benefited from inconsistencies in valuation approaches and has treated revaluations as income. In 1990 (vesting date) Ernst & Young prepared two valuations, based on DCF and DRC. The vesting value was based on the lower value, being DCF. WIAL first revalued its assets in 1993 and again used two valuations. ODV methodology was again followed and the revaluation adopted the lower DCF figure with the asset value allocated over the adjusted (reduced) DRC value. WIAL has revalued its assets since this in 1995, 1996, 2000 and 2002. The prices negotiated in the 1997 Deed reflected an asset base valued at ODRC. The valuations have been consistently applied. Depreciation, asset lives, and maintenance are all based upon the DRC figures. The subsequent valuations have included increasing degrees of optimisation and continuous refinement of the underlying analysis.
Wellington International Airport Limited	In para 5.84, the Commission implies that ODRC valuations of specialised airfield assets may indeed be acceptable, but notes that where firms have switched mid-life, adjustments to pricing to incorporate revaluation gains as income are not sufficient to address issues of potential excess returns. WIAL considers it is entirely ambiguous as to what this means. WIAL concurs that revaluation gains from ODRC should be treated as revenue for pricing purposes.
Alliant Energy	The Commission has acknowledged that the valuation change could result in Infratil not recovering its investment, but says that Infratil should have built this possibility into its expectations for the WIAL investment. However, in purchasing shares Infratil assumed that assets would continue to be valued conventionally as Market Value Existing Use. This valuation standard had been upheld by the court in a number of cases prior to acquisition. A highly reputable independent valuer had performed the valuation. The valuation standard had been followed for the previous period when the Crown was the majority shareholder of WIAL. We consider that there was no basis for Infratil to expect a significant change in the valuation methodology. The Commission's recommendations would significantly penalise existing investors.
Wellington International Airport Limited	The Commission majority's view that ODRC involves considerable subjectivity ignores the sophisticated and robust techniques that have been developed for ODRC measurement. Documented guidelines, sophisticated software valuation models and comprehensive databases of comparative replacement cost parameters have effectively eliminated the subjectivity associated with replacement cost analysis in the 1980s.
Wellington International Airport Limited	Requiring the use of DHC overlooks that this would involve midstream switching of WIAL's approach from ODRC to DHC. The airlines would receive windfall gains at the expense of WIAL and its shareholders. Switching mid-stream would impact on market confidence in the stability of future valuation regimes, increase perceived regulatory risk, discourage investment in infrastructure, and lead to investors demanding increased WACC. BARNZ has recognised that switching methods would pose significant problems and it has expressed support for ODRC.
BARNZ (follow up submission)	The Commission was not wrong in saying WIAL first used ODRC to value its specialised assets in 1995. Charges were based on WIAL's vesting value from 1990 until 1997. Thereafter charges have been a result of commercial negotiation.

BARNZ (follow up submission)	CIAL did not previously use ODRC valuations. The book value (vesting value less depreciation and divestment plus subsequent acquisitions) was the basis for valuing specialised assets until June 2002, when it would appear that CIAL has revalued these assets to ODRC. Prices were set off the vesting value until January 2001, when they were reset based on an ODRC value.
BARNZ (also supported by Qantas and Air NZ)	The 2 dissenting Commissioners agreed with the Commission's views on valuing of land by opportunity cost, optimisation, WACC and pricing principles. The only disagreement relates to valuation of specialised assets, which impacts on the recommendations.
Auckland International Airport Ltd	AIAL supports the minority view regarding valuation of specialised assets at ODRC. Current costs are more relevant than historical costs for considering efficiency. While DHC is widely used in overseas regulatory regimes, there is no equivalent regulatory compact in NZ. ODRC is no more complex than DHC to administer under regulation. ODRC is supported by the wider market, is economically sound, and avoids the uncomfortable hybrid developed by the Commission.
BARNZ (also supported by Qantas and Air NZ)	The minority view did not take into account revaluations. Assuming an annual 2% revaluation of AIAL's specialised assets, then the minority view has understated AIAL's excess returns by an average of approximately \$4 million per annum. If the minority view had included these gains then the level of excess returns resulting from their approach would have been similar to that of the majority.
BARNZ (follow up submission)	If the Minister is considering following the minority view of ODRC as a methodology to value specialised assets, it will be necessary to ensure future revaluations of those specialised assets are taken into account as income. The two members of the minority did not do these calculations. Conservative estimates of land and civil work revaluations amount to \$6 million per annum. The minority would likely recommend control at AIAL if this was done.
BARNZ (follow up submission)	It is incorrect to say that the airlines support ODRC. BARNZ does recognise that over the life of the asset resulting prices will equate expected revenues and expected costs regardless of whether HC or ODRC is used, but this is different from "support". BARNZ experience has been that airports are likely to manipulate revaluation gains under ODRC.
Infratil	The arguments in favour of ODRC and DHC are complex and subtle. The Commission has not justified its preference for DHC other than to note it is closer to opportunity cost. WIAL has always set aeronautical charges based on ODRC values for specialised assets and it has not derived excess returns. The Commission has indicated it would look to oblige industries to switch from ODRC to DHC if the companies under review had achieved over WACC returns, which should not apply to WIAL.

Christchurch International Airport Limited	CIAL considers that economic agents value specialised assets at market value existing use (MVEU). The adoption of DHC, by a majority, is controversial and out of step with accepted valuation methods used in all other utilities in New Zealand. The Commission gives no rational reason why airports should be treated differently from other utilities. The Commission quotes a number of academic articles opposed to ODRC but fails to mention the huge range of commentators and considerable weight of practitioner literature supporting ODRC. ODRC is the recognised standard in the valuation and accounting professions in New Zealand.
Auckland International Airport Ltd	A definitive response is required on the final report because, if it is not dealt with decisively, it will leave a legacy of confusion and misleading assumptions. The fact that it has been greeted with incredulity by the commercial and valuation community is indicative of the problems the final report could cause. We submit that you should note that the economic and valuation principles set out in the final report are not definitive for the valuation of airfield or other assets.
Powerco	Powerco is concerned that the acceptance of the report will create inappropriate and improper precedent and influence the decisions yet to be made in the electricity lines sector. Depreciated HC is not warranted. ODRC should be adopted.
Auckland International Airport Ltd	The Commission's decision to recommend control on AIAL was split 3 – 2. This is extremely unusual. Only 7 out of a total of 318 decisions by the Commission have ever been split since 1986. The fact that the decision is closely balanced indicates real doubt as to whether the recommendation (and the methodologies upon which it is based) should be followed. Even the recommendation of the 3 majority Commissioners is only marginal.
Wellington City Council	The use of historic cost for airport improvements represents a completely unjustified switch from replacement cost to historical cost. The Council notes that all local government infrastructure is valued at ODRC. It is evident the Commission is completely out of step with the widespread use of ODRC and the sophisticated and robust techniques for its measurement.
Auckland International Airport Ltd	The Commission has again mixed valuation methodologies in determining revaluation gains, and in addition, has mixed the way it has treated the resulting revaluation gains via the balance sheet and profit and loss accounts. The 1988 vesting valuation was based on DCF and the 1999 revaluation used ODRC. It is inappropriate to simply look at the difference between these two valuations to calculate a net movement in the asset base. A recommended approach would be to adjust the 1999 values using the property index movements to estimate the value of land in 1988. The Commission's use of the 1988 valuation in this manner was not consulted on.

	Calculation of WACC
Christchurch International Airport Limited	The Commission has relied heavily upon Dr Lally's work and this approach is a significant shift between the draft and final reports. CIAL contends that the WACC range outlined in the final report is too low for CIAL. Even Dr Lally acknowledges that CIAL's asset beta many not adequately reflect its risk (page 498) but he has not attempted to quantify this. However, CIAL's calculation of WACC falls within the range outlined, albeit at the upper end (10.101) and therefore it is inappropriate to say it is earning excess returns. It is not appropriate to focus on a point estimate and assume other points within the range are inappropriate. The Commission acknowledges that calculating WACC is an imprecise science and point estimates give the illusion of greater accuracy than is actually justified.
Graham Halstead & Associates	The appropriate rate of return for a new entrant would be at least 15% given the high risk, but risk is low for the existing airports given the growth of airline travel and freight carrying, and limited competition. Suggests that airports should produce EBITs of no more than 6% of CPI adjusted HC asset values.
Auckland International Airport Ltd	The Commission has mistakenly used 6.33% as the relevant risk free rate. However, this was the rate applying at the time when AIAL's new prices became effective (September 2001) and not the average yield on government stock over the period it consulted with its customers. Deloitte Touche Tohmatsu advises that no review of prices occurred in 2001, rather a price increase previously announced was waived in light of exceptional circumstances relating to a major customer. AIAL argues that the 2000 rate of 7.04% should be used instead, as this is the period when the price consultation occurred. In addition, the WACC should not have been revised in June 2002, as the change in prices was not a consequence of a new pricing review. The correction of this error has a significant effect on the estimate of excess returns.
BARNZ (follow up submission)	AIAL alleges the Commission's use of a WACC based on the risk free rate in 2001 was incorrect. The airlines are very clear that commercial negotiations were held in 2001 and the resulting charges were quite distinct from those set by AIAL in August 2000. The approach taken by the Commission accords with the airlines experience and is correct.
Wellington International Airport Limited	Despite differences in approach, WIAL's estimate of WACC in respect of future charges that are still subject to consultation is well within the Commission's range. Adjustments are also made for compounding and the higher assumed debt margin and leverage. WIAL estimates a WACC of 10%, which is within the range of 8.1% to 10.7% (or as adjusted 11.1%). However, WIAL notes the uncertainty created by the Commission's report may prompt investors to require an increased rate in respect of systemic risk.
BARNZ (follow up submission)	WIAL's WACC comparisons are not valid as they do not use comparable costs of debt. WIAL's claim that its current WACC of 10% is in line with the Commission's WACC is therefore incorrect. Applying the current risk free rate to the Commission's inputs produces a 2002 WACC for WIAL of 8.4%.

Wellington International Airport Limited	<p>WIAL has further differences with the Commission regarding WACC parameters. These are:</p> <ul style="list-style-type: none"> • In estimating the risk free rate, WIAL considers that a longer maturity is more appropriate (10 years as opposed to 5), • the reference period should be from the date of reaching agreement on prices rather than over the whole consultation period, but for practical purposes it should be an average over a short rather than long period, • the Commission notes that there are three approaches to estimating the market risk premium and WIAL prefers the approach of basing the estimate on sets of long time series of market and bond returns for developed open economies. WIAL's estimate differs from the Commission's point estimate but is within the Commission's range. • WIAL considers that debt premium and the debt to equity ratio is simply an empirical issue based on WIAL's actual values. The Commission seems to have used those applying to AIAL. • The Commission has largely adopted WIAL's estimate of its range of asset beta, but WIAL notes its expert (LECG) considers that the upper end of this range may be more appropriate. LECG give more weight to comparative values for international airports, rather than regulated electricity utilities, and consider airports are more sensitive to demand shocks. The Commission justifies its use of regulated utilities on guidelines from Treasury's capital guide for SOEs, but is has only focused on one aspect of those guidelines. It has ignored a considerable body of evidence of airport betas from decisions of the ACCC.
Infratil	<p>The Commission's derivation of a cost of capital for WIAL is incorrect. It has used information about AIAL's capital structure and cost of debt to set the WACC for WIAL. WIAL supplied this information to the Commission but for unexplained reasons did not use it. The Commission has used asset betas from regulated industries with very low risk as a basis to estimate systemic risk of New Zealand airports. It is unreasonable to measure WIAL's past returns as if it had been a heavily regulated very low risk utility as poor past returns belie this case. In addition, it is unreasonable to use the regulated WACC to determine future returns as it presupposes that WIAL is now to be regulated and somehow derisked. This WACC is irrelevant if WIAL is not regulated. The Commission's approach to factors such as WACC has a consistent bias to low value outcomes will little or no margin of error.</p>
Wellington International Airport Limited	<p>WIAL supports WACC as an appropriate measure of return. WACC and its parameters are a matter of uncertainty and dispute between experts, and therefore, WIAL supports the use of ranges of estimates both for WACC parameters and the overall WACC rates, which should be specific to each individual airport. However, WIAL disagrees with the Commission's approach in using US and UK regulated electricity companies to derive a range of beta, and in using AIAL's capital structure and cost of debt for WIAL. WIAL presented clear and unequivocal evidence on its own capital structure and cost of debt but this was not used.</p>

BARNZ (also supported by Qantas and Air NZ)	The Commission's calculations of future excess returns at WIAL from 2003 onwards are understated due to the Commission having used WIAL's 1997 cost of capital for these calculations. Given that the Deed expired in 2002, a new cost of capital (based on 2002 debt rates) should have been applied. This would result in a WACC for WIAL of 8.4% at the midpoint and excess returns in 2003 of \$1.8 million (as opposed to the \$1.3 million calculated by the Commission).
	Calculation of excess returns – errors, bias, uncertainty, inflation
Auckland International Airport Ltd	The Commission's calculations include a large number of numerical and data errors. In addition, the methodology used by the Commission is far from robust. When corrected, we can conclusively prove that there are no excess returns for AIAL. AIAL's supposed excess profits of \$4 million per annum are reversed and fall short of the deemed excess returns level by more than \$1 million per annum. The calculated benefit of \$2 million per annum disappears completely and significant compliance costs would be incurred if control were imposed. These errors and our corrections have been independently audited by Deloitte.
Auckland International Airport Ltd	The draft report contained numerous errors, which once independently verified by Deloitte and pointed out to the Commission, were all corrected by the Commission. When corrected, the Commission's calculations in the draft report showed no excess returns for AIAL. We were astounded that the final report has created a picture of excess returns, and once again the analysis is riddled with errors. We would have expected the Commission to have the prudence and courtesy to consult with AIAL and check its revised calculations before releasing the report to the Minister.
New Zealand Business Roundtable	Ex-post returns should not be used as an indicator of monopoly power. Investors will be deterred if they perceive that the regulatory environment will remove their upside returns while leaving them fully exposed to downside risks. There are many reasons why ex-post accounting returns provide at best a weak indication of ex ante monopoly profits – such as superior performance or even good luck. The Commission does not consider the good luck aspect. Governments should protect investors from unprincipled or ill-founded changes to the legal rules that have retrospective effect.
Graham Halstead & Associates	Non-current asset values show an enormous increase between vesting in 1988 and 2001, particularly for AIAL and WIAL. EBIT for AIAL and WIAL increased significantly and only a small proportion of listed public companies could claim similar results. EBIT for CIAL appears to have dropped due to unusually high expenses. Rates of return in the year after vesting and in 2001 are not unreasonable.
Graham Halstead & Associates	There appears to be excess charging by the airport companies and excess profits being made, particularly at WIAL and AIAL. However, Graham Halstead is not satisfied that the Commission's final conclusions and recommendations are backed up with a realistic analysis.
BARNZ (follow up submission)	AIAL's reports from Seagars, Deloitte and PricewaterhouseCoopers should be treated with a degree of caution. The terms of reference for the reports raise issues of impartiality. The alleged errors identified all flowed in one direction – AIAL's favour.

Auckland International Airport Ltd	The Commission has wiped off \$121 million (39%) from AIAL's total airfield asset base through optimisation and revaluation. This has a material impact on the assessment of excess returns. Many of these adjustments are unreasonable.
Auckland International Airport Ltd	The Commission's final recommendation for AIAL has equally shocked our external expert advisory panel. Our feeling is that the Commission seems to have had a preconceived view as to its desired outcome and has tailored its analysis accordingly. The apparent approach of the Commission at its conference was that it must conclude the inquiry and be seen to be doing something.
BARNZ (follow up submission)	The airlines consider that the Commerce Commission actually erred on the side of generosity to the airports in its calculation. For example, the Commission: <ul style="list-style-type: none"> • did not include revaluation gains as income in its calculation of future returns • adopted higher alternative use values for land than the airports • significantly increased the WACC from its draft report • allowed new investment to earn a return from when construction begins rather than when facilities first come into use • acknowledged in some circumstances it may be appropriate to take a longer term view of investment.
Auckland International Airport Ltd	AIAL has attempted to rework the Commission's analysis, with the assistance of Deloitte Touche Tohmatsu. With all the errors corrected AIAL estimates average historical excess returns of -\$776,000 compared to the Commission's estimate of -\$239,000. AIAL estimates average projected excess returns of -\$1,643,000 compared to the Commission's estimate of \$3,873,000.
Auckland International Airport Ltd	The Commission has erroneously used forecast growth rates for international aircraft rather than total landings. It has also mistakenly included "other property farm rental income" in its figures for airfield revenues, both projected and historical. This causes significant overstatements of excess returns.
Auckland International Airport Ltd	The Commission has inflated airfield costs by 1.5% per annum over the period 2001-04, but has not inflated costs in the years 2005-07. The selected rate of 1.5% is also questionable, particularly given the majority of AIAL's operating costs are wage related and have been escalating recently at an annual rate of 3.25%. Also failure to inflate costs in 2005-2007 has the bizarre result that expenses in 2007 will be lower than they were in 2001. The combined effect of these errors is to overstate airfield returns by an estimated \$320,000 in 2005 rising to \$326,000 in 2007. Deloitte Touche Tohmatsu also advises that direct expenses listed in the minority view ODRC spreadsheets have not been adjusted for inflation.
BARNZ (follow up submission)	Some of the alleged errors were instances where the Commission used numbers from AIAL's own pricing model. For example, the Commission used inflation figures of 1.5% per annum – the same as AIAL when it set prices.

Auckland International Airport Ltd	The Commission's analysis of excess returns uses point estimates for variables, which are estimated by the Commission and its expert advisers to have broad ranges of possible values. The breadth of the ranges highlights their level of uncertainty. PriceWaterhouseCoopers advised that a more scientific method for assessing variables with associated uncertainties would be to undertake more rigorous sensitivity analysis. It shows that the Commission's analysis is particularly sensitive to the asset beta, the market risk premium, and the value of the operational airfield land. Applying its sensitivity model to the Commission's assumptions, it assesses that there is over a 50% chance of AIAL earning excess returns in 2001-07 and considers that the Commission's judgement to recommend control is reasonable. However, when it corrects the Commission's errors it finds that the probability of AIAL earning excess returns over this period reduces to 20%.
Infratil	The Commission did not evaluate WIAL's actual WACC or operating costs. For operating costs, the Commission arbitrarily decided that WIAL's costs would rise at between CPI and CPI-1% pa. Factors like insurance rates, energy, and age of plant, that are not under the airports control and will impinge on operating costs over time, were not investigated. In fact, Standard & Poors' and BARNZ have singled out WIAL as being highly efficient with industry best costs.
Auckland International Airport Ltd	When calculating historical excess returns in scenario 6, the Commission has used the opening vesting value as the appropriate asset base rather than the annual asset base value. This clearly overestimates excess returns and misleads the Minister.
Calculation of efficiency effects	
Auckland International Airport Ltd	The Commission's spreadsheet has hard-coded its calculations of allocative efficiency and consumer and producer surplus. Therefore it is not possible to assess if these calculations are accurate. The correction of the errors identified is likely to change this estimate.
Christchurch International Airport Limited	CIAL supports the Commission's conclusions that it had no dynamic inefficiencies (10.158).
Wellington International Airport Limited	With correct asset values, there are no benefits to acquirers from price control. As the Commission has not provided formulas for calculating allocative efficiency effects, it is not possible to estimate the impact of the correction on allocative efficiency. However, the Commission's estimate of future productivity gains of between 0 and 1% from control is unrealistic, particularly given WIAL's starting point of already being substantially more efficient than either CIAL or AIAL. In addition, WIAL faces a significant increase in insurance costs since September 11, (from \$700,000 to \$2 million) and its airfield operating expenses are forecast to fluctuate as a result of a required maintenance programme for sealed surfaces. In addition, in an environment where WIAL will fail to cover WACC over 2001-2003 (based on corrected asset values), there will be strong incentives on managers to boost WIAL's productivity. The Commission has concluded there are no dynamic inefficiencies in WIAL's operation.

Christchurch International Airport Limited	CIAL supports the Commission's conclusion that there was little or no cross-subsidisation and that the multi-till approach was appropriate (10.137).
Graham Halstead & Associates	There is little incentive for airports to focus on efficiencies. Airfield activity costs should be more closely examined. For example, why are employment costs at CIAL 50% higher than at WIAL?
Auckland International Airport Ltd	The Commission has forecast cost containment of a 14% drop in expenditure in nominal terms from 2001 levels and a 22% drop in real terms. This represents a dramatic improvement in productive efficiency. If this is assumed, it is then wrong to later assume further productive inefficiencies of between 1% and 3% in their analysis. This is potential double counting.
BARNZ (follow up submission)	Some of AIAL's alleged errors are just different points of view. For example, the Commission found that efficiency improvements of between 1 and 3% per annum were available at AIAL. However, AIAL has sought to characterise the level of operating expenses the Commission included in the model as an error of \$6.2 million.
	Costs of control
Powerco	Insufficient analysis has been undertaken on the costs of control. The Commission's approach is to use a prescriptive formula to determine acceptable revenue based on a regulated asset base, WACC, and determining efficient costs of operation. Any form of control that sought to prescribe these matters would be excessively costly. Insufficient account is taken of the likely implications of control on future investment. Regulation of this kind inevitably leads to a loss of benefits and synergies that would otherwise benefit consumers.
BARNZ (also supported by Qantas and Air NZ)	BARNZ submits that, as a matter of policy (distinct from the Commission's analysis) the costs of imposing control should not be a factor in determining whether a participant who has set out to earn monopoly rents should be subject to control. Otherwise it signals to monopolists that they can earn excess returns up to the cost of control with no threat of control.
BARNZ (also supported by Qantas and Air NZ)	BARNZ submits that the Commission should have apportioned the costs of control equally between acquirers and suppliers. It is unreasonable to apportion the full costs on acquirers.
BARNZ (also supported by Qantas and Air NZ)	The costs of control are overstated. Control should cost no more than the current consultation process.
Major of Christchurch	The Commission's recommendations will result in the imposition of costly and heavy-handed regulatory control by the Commission. While CIAL was not found to make excess returns, it will be a costly and time-consuming business for the company to continue to provide justification to the Commission that price controls are not warranted.

Wellington International Airport Limited	The Commission's direct and indirect cost estimates of control are driven by fairly crude assumptions. In respect of direct costs, there are options for price control that could be both far more costly and far less costly. The estimate of indirect costs excludes the costs to the controlled company of diversion of senior management from other activities. The Commission's method of estimating indirect costs as a percentage of any allocative or dynamic efficiency benefits from control also means that the indirect costs of control could never be negative. WIAL considers this is unrealistic, as regulator error is possible and could impose negative dynamic efficiency effects from control. The key point from uncertainty is that the benefits of control need to significantly outweigh the estimates of costs of control in order to justify the imposition of price control.
	Net benefits to acquirers of control
Wellington International Airport Limited	WIAL submits that the extent of its competitive conditions should be taken into account in considering whether control is necessary or desirable in the interests of acquirers. The Commission's thresholds relating to this factor include assessments of "evidence of the exercise of market power" and the "impact of any market power exerted in relation to other markets." However there is no evidence of the Commission having considered these matters in its analysis. If a higher standard of competitive conditions is not considered then there is the potential that a substantial part of the business sector could conceivably be subject to control.
New Zealand Business Roundtable	Any abuse of market power by AIAL is likely to be small. Demand for landing facilities at AIAL is likely to be price inelastic so that any allocative inefficiencies are small. The Commission estimates net benefits to acquirers of around \$2 million per annum. This is only 4% of total landing charges, and in 2002 is 1% of AIAL's revenue and 3% of its net profit. The \$2 million figure is tentative and trivial in relation to the market risks to profits and revenues of airlines and airport companies.
Air New Zealand	Parliament's intention at the time the consultation and information disclosure requirements in the Airport Authorities Act were put in place was clear. The Bill was intended to protect against monopoly pricing by airport companies and protect consumers and the travelling public. The inquiry under Part IV of the Commerce Act was announced at the same time and was intended to strengthen the regime. It was described as the "sword of Damocles" intended to stop abuse of market power.
BARNZ (also supported by Qantas and Air NZ)	Based on statements made at the time the inquiry was initiated, the purpose of the inquiry from the then Government's point of view was to review the efficacy of the regulation surrounding airports and to determine whether the airport companies were monopoly pricing.
Qantas Airways Ltd (submitted by Minter Ellison Rudd Watts)	Excess charges result in a very significant transfer of wealth from the community (as increased charges to the airlines are inevitably reflected in fares as increased costs affect demand) to the airport company's shareholders. Qantas's role is that of watchdog for the travelling public.

Auckland International Airport Ltd	It is questionable whether the Commission's prime focus should be on the net benefits to acquirers. Section 52 does not outline this viewpoint. An alternative interpretation could be a national perspective, considering whether airlines would pass on any gains to end-users and the foreign-ownership of airlines. This focus is a change from the draft report which used a net public benefit approach.
	Conclusions on the Commission's report
Infratil	Infratil disagrees with the Commission's analysis, findings and concepts in respect of the thresholds used to justify imposing control. The competition threshold would capture a large percentage of New Zealand companies. It does not take into account the significant countervailing market power held by airlines. The Commission does not provide robust evidence of excess returns or operational inefficiencies by WIAL. In addition, there is no meaningful cost/benefit analysis for imposing control. The compliance costs are inferred and unresearched. It assumes all cost savings that result from price caps relate to productive efficiency but has no assessment of distributional impacts, and has not evaluated consequences for dynamic efficiency.
Christchurch International Airport Limited	There is no basis for the imposition of control on any airport. If imposed on any one airport it would have distortionary affects for the industry as a whole. DHC should be rejected. Even if accepted, the anticipated benefits are minimal in the wider scheme of things. The Minister should not create a bureaucratic monster just to appease theory. The inquiry process has been cathartic. The Minister should now call off the hounds. None of the participants – BARNZ included – actually wants price control.
BARNZ (also supported by Qantas and Air NZ)	The Commission has found evidence of sustained monopoly pricing by AIAL in the past and has evidence that this will continue in the future – upwards of \$27 million over the period 2001 to 2007. AIAL has recently announced a record profit. It has also revalued airfield land by between \$35.6 and \$59.2 million. The airlines feel powerless to prevent behaviour of this nature. BARNZ members are firmly of the view that it is necessary for control to be introduced at AIAL.
Wellington International Airport Limited	WIAL opposes price control of AIAL's airfield activities as recommended by the Commission.
Graham Halstead & Associates	Some control on landing charges for AIAL might be necessary but a re-examination of asset values and net incomes would be required before this could be supported.
Powerco	There are sufficient levels of doubt and uncertainty in the Commission's report to warrant the rejection of the recommendations. This doubt includes uncertainty about the costs of control; only a superficial assessment of the impact of control on dynamic efficiency; only a superficial assessment of the impacts of control on investment and the linkage between share price (investor's expectations) and valuation of assets (regulatory control of returns); and 2 of the 5 Commissioners favour ODRC over DHC (which on its own is sufficient to change the recommendation).
Qantas Airways Ltd (submitted by Minter Ellison Rudd Watts)	The Commission's report fairly establishes that price controls at AIAL and at WIAL, subject to the outcome of the current consultation process, are justified in the public interest.

Auckland International Airport Ltd	The Commission's own analysis produces negative excess returns and nil benefits to acquirers within the WACC range in some years. The decision to recommend is based on the Commission's regulatory judgement, but this seems to be another way of saying subjective discretion. AIAL questions how a responsible decision maker, taking all relevant considerations into account, could possibly have come to the Commission's decision to recommend control.
Air New Zealand	Air New Zealand is the single largest user of the three airports. It also has an important watchdog role, as it is required to act as proxies for consumers and the travelling public. Air NZ considers the Commission's report to be a robust and comprehensive analysis confirming that the three major airports are abusing their market power and earning monopoly profits. It is critical the government take all necessary steps to discipline the market participants to ensure the economy can deliver efficient and effective outcomes.
The Special Utilities Investment Trust plc (SUIT)	SUIT submits the Minister should reject the recommendation for control, inform the Commission that its approach to existing investors is cavalier at best, and that its approach in favour of opportunity cost is out of step with world norms and should not be pursued.
Infratil	If control is recommended for AIAL, it will imply the government endorses the Commission's methodology for calculating excess returns. This will result in control by default on CIAL and WIAL with no evidence of its need. It would oblige WIAL to consult annually with the Commission on its acceptable revenue, which would almost certainly require airlines to also be involved. This would be evasive, costly and cumbersome, and additional to extensive controls already placed on WIAL under other legislation.
Wellington City Council	The Commission's analysis has not found overcharging for WIAL, but nevertheless has recommended a regime that would effectively result in WIAL being controlled, with all the associated costs and inefficiencies. The Council is concerned about the unwarranted effect that some of the analysis contained in the report may have on WIAL, WCC, and on economic development in the region generally. WCC recommends the Minister reject the valuation methodology used by the Commission.
BARNZ (follow up submission)	The Commerce Commission has not recommended control at WIAL. It has noted that if airfield charges increased by [] it was likely to recommend control.
Wellington International Airport Limited	WIAL submits that the Minister should: <ul style="list-style-type: none"> • Decide not to impose price control on any airport • Reject the Commission's recommendation regarding WIAL's current consultation process; and • Transmit a section 26 government policy statement which: <ul style="list-style-type: none"> • Confirms the current regulatory framework for airports, • Emphasises the importance of dynamic efficiency in the Commission exercising its functions under the Commerce Act, and • Endorses valuation methodologies that value airport land as an airport and aim to ascertain fair value, and in relation to specialised assets, value at ODRC.

BARNZ (also supported by Qantas and Air NZ)	BARNZ is deeply concerned at the level of prices being proposed by WIAL in the current consultation round. WIAL is unwilling to adopt the Commission's pricing principles. If the proposed [] increase in charges were introduced, the Commission estimates that there would likely be net benefits to acquirers of \$2.5 million per annum. BARNZ does not believe it is appropriate to request the Minister to introduce control at this time, but asks that any final decision on WIAL be delayed until the charges have been set and the airlines have had an opportunity to comment to the Minister.
Alliant Energy	Alliant Energy is a US based energy utility incorporated in Wisconsin and mainly operating in Wisconsin, Iowa, Illinois and Minnesota. Through Alliant Energy International, it has been an active investor in New Zealand since 1994 having a current value of over NZ\$170 million. These investments are primarily in the energy sector. Alliant Energy International also has a 9% shareholding in Infratil. Alliant notes that WIAL had not been earning excess returns to date, but nevertheless the Commission has effectively recommended price control over the airfield, and possibly all aeronautical activities. There is no evidence of WIAL exercising market power.
Wellington International Airport Limited	WIAL opposes the Commission's recommendation that, if WIAL imposes a significant increase in charges as a result of its current consultation with the airlines, the Commission would likely be satisfied that it would recommend the airfield activities be controlled. This recommendation is predeterminative and is based on incorrect analysis. It represents the position of the three Commissioners only and not the full Commission as represented. It appears to extend even beyond the scope of the inquiry to all airport activities. The Minister should reject it.
	General other matters the Minister should consider
Infratil	The inquiry caused WIAL to incur over \$2 million in external costs over the four years. The inquiry occurred at the behest of Winston Peters with no evidence to support the need for an inquiry. It was contradictory to the thrust of the Airport Authorities Act and was conducted in a policy vacuum. The government should now measure the recommendations against policy goals, especially economic growth, as well as scrutinise the correctness of the Commission's findings.
Auckland International Airport Ltd	We submit that you should not accept the Commission's recommendations for AIAL due to the multiple numerical errors which when corrected show that there is not case for price control. In addition, the Minister may wish to take into account other factors, such as the net public benefit, which shows that control on AIAL is not warranted.
New Zealand Business Roundtable	The Commerce Act and the decision whether or not to recommend control should have the single objective of enhancing economic efficiency. In some cases, regulatory constraints on market power may improve economic efficiency, but there should be a presumption in favour of light-handed regulation. Heavy-handed interventions lead to cost plus behaviour, distort entry barriers and competition, and result in bureaucratic capture and regulatory creep. They can also result in unstable swings in prices and investment, reflecting changing political pressures on regulators.

	A credible threat of control
Air New Zealand	The inquiry conducted under Part IV of the Commerce Act and the imposition of control should not be seen as a departure from the light-handed regime. The threat of control is an integral part of the regime and control is the ultimate backstop should the other pieces of the framework (i.e. disclosure and consultation requirements) not achieve the desired result.
Air New Zealand	It is of concern that, notwithstanding Parliament's intention and the inquiry being underway, the Commission has identified evidence that all three airports are pricing above the competitive level. It is vital that, having identified abuse, appropriate action is taken. Lack of such action would undermine the light-handed regime and render the credible threat non-existent or ineffective.
Qantas Airways Ltd (submitted by Minter Ellison Rudd Watts)	The mere existence of the Commission's inquiry has had an impact on the airport companies' tendency to exploit their market power. Unless the Commission's recommendations are accepted and implemented, the light-handed regulatory regime and the requirement for airports to consult will be meaningless.
BARNZ (also supported by Qantas and Air NZ)	The potential for the control of goods or services is a central component of NZ's light-handed regime. The imposition of control is not a decision to move to a more heavy-handed form of regulation, but rather the enactment of the threat. A decision not to impose control would severely reduce the credibility of the threat unless the preferred alternative option of an industry-negotiated mechanism that removes monopoly rents from charges can be agreed.
Christchurch International Airport Limited	The Commission's investigation and report has been a huge undertaking for both the Commission and participants in the inquiry. It has been clear evidence that the current regulatory regime has teeth.
BARNZ (also supported by Qantas and Air NZ)	If the Commission had not been conducting its inquiry, airlines and the travelling public could have been facing even greater increases in charges. WIAL has proposed increases in charges of []. It released a valuation report, not adopted at the present time, which would have increased land values by [] million and resulted in increases in charges by approximately []. AIAL proposed increases of up to [] before finally increasing charges by 12.5% spread over 2 years. It has recently announced it has revalued its land to reflect reclamation costs, which has led to a further [] million increase in land value.
	Alternative market interventions
Christchurch International Airport Limited	The existing regulatory regime should be maintained. It is robust and cost effective. The Commission's methodology should not be used as a precedent for future consultation rounds. The Ministry of Transport's general transportation review should be abandoned.
Auckland International Airport Ltd	A legitimate policy response would be to continue with the current light-handed approach (perhaps with targeted mechanisms that provide greater guidance for dispute resolution), rather than initiate a more interventionist price control, which has the potential to distort market-based outcomes and result in actions that may diminish overall welfare in the medium and long term all for limited short term benefits to a subset of suppliers – the airlines.

New Zealand Business Roundtable	We note that the Australian Productivity Commission favoured reliance on light-handed regulation, not price controls, in respect of the four airports that it found market power. It proposed monitoring those airports on a probationary five year period.
New Zealand Business Roundtable	In the event that the Minister does wish to control AIAL, we urge to recommend against price control. If necessary, enhancement of the current light-handed regulatory regime, through additional disclosure and monitoring, may be an option to address possible concerns.
Wellington International Airport Limited	WIAL considers the Commission went beyond its statutory mandate by creating “generic pricing principles” and to imply that these principles can only be applied by the exclusive adoption of the approaches favoured by either the full Commission or the majority Commissioners. This approach is tantamount to, and predeterminative of, a price authorisation of a controlled service. This is inappropriate. In particular, WIAL disputes the Commission’s application of these pricing principles in relation to the opportunity cost principle, some aspects of the calculation of WACC, and inputs to its net benefit analysis.
Qantas Airways Ltd (submitted by Minter Ellison Rudd Watts)	In the absence of any strengthening of the Airport Authorities Act, such as requiring airport companies to “negotiate” rather than “consult”, the Minister’s power to impose price controls must be credible.
Air New Zealand	Air NZ believes it would be appropriate for the Ministry of Transport to complete its review of the regulatory regime and make recommendations which included the following: <ul style="list-style-type: none"> • Remove the statutory power of airports to set charges as they think fit; • Secure the ability of users to negotiate with airports; • Establish principles for airport pricing consistent with those in the Commission’s final report; and • Establish a form of deadlock breaking mechanism. Of the above the first three are the most important, although they should all be seen as part of an overall package.
Qantas Airways Ltd (submitted by Minter Ellison Rudd Watts)	It is Qantas’s strong view that the pricing principles developed by the Commission provide an appropriate framework for the consultation process provided in the Airport Authorities Act 1996.
BARNZ (also supported by Qantas and Air NZ)	BARNZ supports the pricing principles developed by the Commission. Its preference is that these principles be agreed as a basis for future negotiations without the need for regulatory intervention. If these principles could be agreed, then most if not all of the differences between the airlines and airport companies with respect to airfield charges would disappear. However, the airport companies have not been prepared to do this.
BARNZ (also supported by Qantas and Air NZ)	Control is a last resort if commercial outcomes are not able to produce economically efficient prices. BARNZ has sought to engage AIAL in negotiations based on these pricing principles, but AIAL did not see this as an option.
Auckland International Airport Ltd	Since the release of the final report, both Air New Zealand and BARNZ have signalled that even they do not want price control, which they label as a last resort.

BARNZ (follow up submission)	It is incorrect to claim that airlines (particularly BARNZ and Air New Zealand) do not want control. Our view is “in light of the sustained and large scale nature of the monopoly pricing being engaged in and AIAL’s unwillingness to enter discussions based on the pricing principles articulated by the Commission, BARNZ members are firmly of the view that it is necessary for control to be introduced at AIAL.”
	Incentives on investment and economic growth
Auckland International Airport Ltd	Similarly the imposition of control is a draconian step, which will increase compliance costs, increase perceptions of government interference and will result in the loss of investor confidence in NZ. NZ’s economic development relies heavily on transport infrastructure, of which AIAL is a contributor. The final report has the potential to jeopardise this.
Auckland International Airport Ltd	The logical commercial responses to the Commission’s final report is: <ul style="list-style-type: none"> • Immediately sell all the land currently being held for future development of a second runway, and Wiroa Island the Eastern Approaches land. • Delay repurchase of the second runway land and the development of future infrastructure assets until they are blatantly needed (thereby exacerbating future congestion) • Establish complex sale / lease-back asset ownership structures. • Introduce peak hour slot pricing structures, which would likely produce significant increased cost disadvantages to Air New Zealand’s domestic flight operations.
Christchurch International Airport Limited	A further specific reason for airports to have DHC is cited as investor expectations (5.130 to 5.154). The Commission argues that investors’ expectations at the time of vesting were for normal returns and as such incentives for investment could not be harmed by a return to DHC. This argument is flawed. Normal returns include capital gains and income, and capital gains were explicitly forecast in the DCF models used to derive vesting values. The 1988 DCF spreadsheets for CIAL show a cumulate revaluation of between \$98 million and \$145 million between 1988 and 2000. Therefore expectations of revaluations were part of an implicit regulatory compact, and ODRC would be more consistent with investor expectations. Furthermore, prices were calculated in 1988 implicitly assuming revaluation gains were a component of returns to the intending investors. The Commission’s justification for using DHC is fundamentally inconsistent with the methods used to derive vesting values.
Alliant Energy	We urge you to reject the Commerce Commission’s recommendation, and have no doubt that such an action will improve investor confidence in the New Zealand infrastructure sector.
New Zealand Business Roundtable	The Government should be aware that its decisions on control are likely to unsettle investor expectations unless they are clearly based on sound principles that give predictability to future investor decisions.
Powerco	The combination of price control and a dramatic change in valuation methodology will amount to an expropriation of investors’ funds, which is unfair and unjust, and will stifle future investment.

Infratil	The government's response to the report will have a material impact on Infratil's willingness to invest in New Zealand infrastructure. In 1998, the Crown tendered its 66% stake in WIAL, and in 1999, Infratil bought out its co-investors so that WIAL is now jointly owned 66% by Infratil and 34% by Wellington City Council. Infratil's investment cost \$116.8 million and to date has provided modest returns. Cash returns have been approximately 8% pa. before tax. Growth has been low, as high airfares have reduced demand for air travel. Aeronautical charges were fixed from 1997 to 2002, but during that period the airport invested over \$100 million in terminal facilities which to date has provided nil return. The inquiry has delayed resetting prices.
Auckland International Airport Ltd	A definitive response on the final report is required by the Minister, otherwise the uncertainty and inconsistency created by the report will impact on investment intentions in not only airports but also other crucial infrastructure assets. It will lead to such investor uncertainty and higher costs of capital that some key infrastructure projects may be delayed and jeopardised.
Alliant Energy	We believe the Commission's approach to opportunity cost will be unattractive for long term investors in sunk assets such as airfields. In addition a consistent application of economic principles in regulation is of paramount importance to overseas investors and the absence of consistency is a discouragement to investment in long-lived infrastructure assets.
BARNZ (follow up submission)	It is incorrect to claim that acceptance of the Commerce Commission's report and the introduction of control would result in a loss of investor confidence in New Zealand. Countries such as USA, UK and Australia have not suffered a loss of investor confidence under systems far more interventionist than the Commerce Act.
BARNZ (follow up submission)	Investment is a two-sided coin. Investment is necessary for both infrastructure providers and infrastructure users. Airport users invest in planes. Failure by the government to ensure economically efficient prices by infrastructure providers will accordingly result in reduced investment and use by infrastructure users.
Mayor of Christchurch	The Commission's recommendations disregard the interests of existing equity holders in favour of a notion of economic efficiency.
Mayor of Christchurch	The extension of the principles of the Commission's airports review to other infrastructural assets could result in a major and unjustified loss of value to Christchurch City and to other equity holders throughout New Zealand.

<p>The Special Utilities Investment Trust plc (SUIT)</p>	<p>SUIT is also concerned about the Commission’s desire to change values without due regard to incumbent investors. The comment that Infratil should not be surprised about the valuation change is unfounded. As one of the parties that acquired WIAL from the Crown we can give a first hand report of our view then and our surprise now. In making the acquisition, SUIT was very mindful of future regulatory possibilities. We decided that WIAL’s circumstances were clear and risks reasonably low. The commercial aspects of the airport’s aeronautical activities were well defined by the Airport Authorities Act. A number of High Court decisions had given clarity to valuation and WACC matters. The fact that the incumbent majority shareholder was the NZ Government was also noted relating to relevant corporate governance and policies. Also WIAL had produced low returns and there was no reason to believe its aeronautical charges or returns would draw regulatory attention. The regulatory risks at that time bear no relation to what the Commerce Commission is now recommending. Their justification for a material adverse change on the airport’s asset value is not based on any excess return, but on a highly debatable case that opportunity cost will deliver economic efficiency. This will cause unwarranted harm to investors. SUIT thinks it is also relevant that the recommendation is based on a 3-2 decision.</p>
<p>Infratil</p>	<p>Infratil contends that the Commission’s recommendations on WIAL directly contradict the government’s stated policies for business law. It has rejected the primacy of law, disregarded the equity of its treatment on investors, discouraged investment in assets, increased the cost of capital and is inconsistent with Australian trends moving away from heavy-handed regulation.</p>
<p>The Special Utilities Investment Trust plc (SUIT)</p>	<p>SUIT will follow the Minister’s response to the Commerce Commission’s recommendation with interest. The response will signal the government’s position on investor rights. On the basis of this decision, SUIT will review whether New Zealand is an attractive place to invest. The Minister’s response has the potential to increase the cost of capital in New Zealand. In addition, SUIT will review the need to mitigate the precedent effect of this decision on regulators in other jurisdictions.</p>
<p>Infratil</p>	<p>Infratil advises that if the Commission’s recommendation is not rejected it would be a warning to any investor that the regulatory environment has significant risks for any party looking to commit capital. The Commission did not inquire whether the opportunity cost approach could penalise investors and discourage investment. It recognised that this approach would likely result in Infratil suffering a loss, but considered that Infratil should not be surprised or aggrieved because it knew of the inquiry when it made its investment. However, in purchasing shares Infratil assumed that assets would be valued conventionally and in accordance with the Airports Authority Act as recently interpreted by the High Court (and Court of Appeal) and supported by the Crown as majority shareholder of WIAL at the time. The High Court interpreted the obligation for WIAL to be commercial to mean that WIAL’s assets should be valued as it is as an airport (i.e. market value existing use and not highest alternative use). Infratil would treat the Commission’s views on valuation as expropriation of approximately \$40 million from its investment.</p>

Wellington City Council	The significance that Wellington's unique inner city airport plays in Wellington's success as a tourist destination cannot be underestimated. An undervalued airport will not generate sufficient return to incentivise ongoing investment in maintaining the airport at an appropriate level. WCC would need to reassess whether it is appropriate for the Council to continue to retain an investment in WIAL when the value of the airport's assets may suffer a large loss of value. The Commission's approach may deter incentives for potential investors to invest in infrastructure. Wellington's infrastructure assets are vital to the success of our city and WCC needs private investors to make this happen.
	International obligations
Air New Zealand	International air services are subject to bilateral agreements between the NZ government and various other governments. Included in these agreements are provisions regarding the setting of user charges. For example, Article 7.1 of the Agreement between Australia and NZ (August 2002) requires each party to encourage those responsible for airport services to levy charges on a "reasonable, non-discriminatory and equitable basis" and should not exceed the full cost of providing the facilities used. Similarly, NZ is a party to the Multilateral Agreement on the Liberalisation of International Air Transportation (May 2001) which provides that user charges imposed by the competent charging authorities "shall be just, reasonable, non unjustly discriminatory and equitably apportioned". "Such charges may include a reasonable return on assets, after depreciation. Facilities and services for which charges are made shall be provided on an efficient and economic basis." There is therefore a compelling international dimension to ensuring that the regulatory regime, having identified abuse, is seen to work to ensure that appropriate remedial action is taken. Such action could also be regarded as required in order to achieve compliance with the international obligations entered into by New Zealand in the treaties referred to.
Qantas Airways Ltd (submitted by Minter Ellison Rudd Watts)	The Minister's acceptance and implementation of the Commission's recommendations would be consistent with NZ's obligations arising under relevant international aviation agreements, and ICAO principles and protocols. For example, the Multilateral Agreement on the Liberalisation of International Air Transportation (May 2001) – Art.10 provides that user charges that may be imposed ... shall be just, reasonable, ...and ... may reflect, but shall not exceed, the full cost to the competent charging authorities ... Such charges may include a reasonable return on assets, after depreciation. Other relevant Agreements include the several Air Services Agreements (ASAs) entered into with other States pursuant to the Convention on International Civil Aviation 1944 (the Chicago Convention).
Wellington International Airport Limited	The Commission has included supplements that go well beyond what is relevant to the statutory criteria under section 52 of the Commerce Act. The Commission's inclusion of comment on international obligations is also misleading. The Commission's comment in footnote 449, which states that section 91C of the Civil Aviation Act 1990 provides that provisions of the Chicago Convention have the force of law in New Zealand, is incorrect. Section 91C applies to the provisions of the amended Convention and Guadalajara Convention. Neither of these contains provisions relating to airport pricing. The statement in para 1.1.5 that some of the Air Service Agreements New Zealand has entered into contain provisions dealing with user charges is misleading. These Agreements have not been incorporated into domestic law and do not form part of the regulatory framework governing airport pricing.

	Thresholds for control under section 54 of Commerce Act
Wellington International Airport Limited	WIAL notes that the Commission has identified generalised factors, which it considers relevant to assist the Minister in deciding if the criteria in section 52 are met. However, these factors are not thresholds or capable of being applied as thresholds. WIAL agrees with the Commission's caution in declining to attempt to identify absolute thresholds.
	Forms of control
BARNZ (also supported by Qantas and Air NZ)	BARNZ advises that, if control were declared, it would request that the form of control should be for the Commission to issue pricing guidelines and direct the parties to attempt to agree on prices based on those principles. Once agreed, these prices could be authorised by the Commission.
Auckland International Airport Ltd	The final report recommends control, but seems to not want anything to occur. It notes that the airlines favour commercial negotiation and that any form of control must be commensurate with the level of market power available, the size of the excess returns and the net benefits to acquirers – all of which even on the Commission's disputed approach are assessed to be modest.
Wellington International Airport Limited	WIAL agrees that the form of control is a matter under Part 5 of the Commerce Act and not Part 4. However, WIAL considers that supplement 3 to the report (form of control) is outside the scope of matters for this report.
	International regulation of airports
Wellington International Airport Limited	WIAL considers the Commission's detailed discussion of forms of regulation overseas is both irrelevant and inappropriate. The Commission only briefly acknowledges that the United Kingdom and Australia are moving away from heavy-handed regulation and that a monitoring regime has replaced the price cap regime. It does not refer to the Australian Productivity Commission's report, which in relation to opportunity cost is ambivalent. The Commission also fails to draw attention to the United States rejection of opportunity cost in the Los Angeles Airport case.
	Other airport activities
BARNZ (also supported by Qantas and Air NZ)	A primary concern is that the scope of the inquiry did not consider other airport activities by the airports. CIAL is including proposed new terminal assets having a combined value of \$48 million in its asset base for determining terminal charges. These new terminal assets do not exist at this time. BARNZ recommends a further inquiry or other more direct action to address this problem.
Christchurch International Airport Limited	CIAL supports the Commission when it noted that the discounted cashflow and the building block approach would produce the same results given the same inputs and assumptions (7.20). This is important as CIAL has used a DCF approach in setting terminal charges. The airlines have criticised this and have advocated the extension of the inquiry to terminal charges. The Commission quite properly has resisted this.
	Distributional effects
Major of Christchurch	The Commission's recommendations could result in a wealth transfer from the citizens of Christchurch to, in some cases, overseas-owned businesses.

	Minister's decision – conflict of interest
Wellington International Airport Limited	WIAL notes that the government is a majority shareholder in Air New Zealand and has a financial interest in the outcome of the inquiry. WIAL urges the Minister of Commerce to adopt proper procedures to ensure the process by which she makes her decision can not be influenced by shareholder interests.
	Part IV of the Commerce Act
New Zealand Business Roundtable	The threshold of “competition is limited” is very low, particularly given concentration ratios tend to be high in small New Zealand markets. In addition, section 53 of the Commerce Act requires the Commission to consider whether control is necessary in the interests of acquirers, which it interpreted to include income distribution as well as efficiency effects. This is a serious flaw in the legislation and it should be reviewed with a view to restoring an efficiency focus. It is hard to see any valid reason to presume a benefit to society from regulation that transfers wealth from airport investors to airline investors.