

10 October 2024

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### **Review of Auckland Airport's 2022 – 2027 Price Setting Event 4 (PSE4) – Consultation paper: Air New Zealand (Air NZ) Cross Submission**

Air NZ welcomes the opportunity to provide cross submissions regarding the Commission's consultation paper for the review of Auckland International Airport's (AIAL) PSE4 pricing.

Air NZ considers that there is a clear consensus across submissions that the regulatory regime does not incentivise AIAL to act in a manner that is consistent with the Part 4 purpose, and as a result:

- AIAL has overwhelming commercial incentives to target, and has again targeted, an excessive WACC and excessive profits;
- On multiple relevant metrics, AIAL's Terminal Investment Programme, particularly the Domestic Jet Terminal, is over-sized;
- There is significant evidence that AIAL has failed to consult meaningfully; and
- AIAL is clearly not incentivised to innovate.

Taking each of those points in turn:

#### ***AIAL has overwhelming commercial incentives to target, and has again targeted, an excessive WACC and excessive profits***

AIAL contends that the Commission should simply disregard its two scenarios for assessing the cost of capital, in favour of AIAL's own re-estimation of WACC that is inconsistent with the parameters of both the 2016, and the 2023, input methodologies (IM) determinations. AIAL's re-estimation has departed from every 2016 IM parameter by a substantial margin.

We consider this symptomatic of one of the key issues articulated in our submission – AIAL has significant commercial incentives to target an excessive WACC which in turn creates a powerful incentive for AIAL to over-invest, which is clearly evidenced by AIAL's excessive capital plan for PSE4 and PSE5.

Air NZ continues to support the Commission's first scenario (adoption of the 2016 IM parameters) as the appropriate framework to calculate an appropriate cost of capital and to thus review AIAL's pricing and profitability. Scenario 1 reflects the IMs prevailing at the commencement of the PSE4 pricing period and is consistent with the framework proposed by the other regulated airports when setting prices during and after the pandemic.

***AIAL's Terminal Investment Programme (TIP), particularly the Domestic Jet Terminal (DJT)<sup>1</sup>, is over-sized.***

AIAL continues to defend the scale of its new domestic terminal despite considerable evidence presented in submissions from multiple parties that it is significantly over-sized. In particular, it is over-sized when assessed against each of the following highly relevant metrics:

- The size of terminals serving similar domestic traffic in the same region;
- The cost of these terminals, expressed as:
  - Cost per square metre (sqm);
  - Cost per gate; and
- The appropriate IATA Levels of Service (**LoS**).

Air NZ maintains that many of the data points and benchmarks used by AIAL are inappropriate, such as benchmarking the size and cost of an NZ domestic terminal to international terminals which, by nature of their operations and customer base, require a higher LoS.

AIAL also continues to claim Air NZ / Arup's alternative terminal is not viable. This is incorrect. Both terminals provide for 15 Code C jet stands, with the Air NZ / Arup 'Alternative Domestic Terminal' (**ADT**) provided at a cost of \$1.1bn and AIAL's DJT at \$2.2bn when costed on a like-for-like basis.

Air NZ continues to evidence that the ADT is not only viable, but also one that all airline customers could have supported with alignment on the phasing of construction, as confirmed in Qantas's submission.

***There is significant evidence that AIAL has failed to consult meaningfully***

Qantas described AIAL's 'consultation' as "a series of discussions designed to create the appearance of consultation". Air NZ agrees. As is abundantly clear from the submissions, AIAL has not listened to its customers. Air NZ maintains that if AIAL had been willing to meaningfully consult on alternatives after the terminal cost escalated substantially, it could have amended its design to something more closely resembling the size of Air NZ's proposed ADT. Air NZ rejects AIAL's suggestion that it was somehow incumbent on the airlines to present viable alternatives to AIAL during consultation. Rather, it was always incumbent on AIAL to ensure that its proposed investment was efficient.

Airlines have different business models and customer propositions, so there will always be a range of airline views about the scale of airport capital expenditure required. This is why it is critically important for airports to adequately consult airlines on LoS and ensure the actual LoS is aligned to the needs of the customers using airport infrastructure. There is no "one size fits all" approach, and, as IATA states, the business case should be clearly articulated and agreed

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<sup>1</sup> AIAL has referred to this terminal under various names in PSE4 consultation and review documents, including: Integrated Domestic Terminal (IDT), Domestic Processor (DP) and, most recently, the Domestic Jet Terminal (DJT). What Air NZ refers to as the DJT in this paper, was also referred to as the DP in our original submission to the PSE4 review.

on before any investment proceeds. The submissions clearly show that AIAL did not consult with airlines on LoS.

Both Qantas and Air NZ agree that the terminal should be materially smaller than AIAL has proposed. Both airlines agree that staging the investment in the terminal to align with passenger demand is important to minimise price shocks and that the capacity freed up in the existing domestic terminal building (**DTB**) remains a valuable asset.

Air NZ considers AIAL's submission demonstrates the same approach to the responses airlines received throughout the consultation process, especially from 2021 onwards. Where airlines gave feedback that the terminal was too big and therefore too costly, and suggested what might be looked at to change this, AIAL simply sought to explain why the airlines were wrong, rather than to meaningfully consider and incorporate this important feedback into their plans. The impression was that once the decision was made to proceed with Paheko East<sup>2</sup> in 2021, based on flawed cost assumptions, AIAL was resolved to proceed regardless of airline objections and proposed alternatives. The extensive description of the so-called consultation provided by both Air NZ and Qantas attests to this.

#### ***AIAL is clearly not incentivised to innovate***

Air NZ notes that both the NZ Airports Association (**NZAA**) and AIAL seek clarity on how to define innovation. They can see an example of this in the submissions of their airline customers. Air NZ submitted a viable alternative to save significant cost through a terminal redesign. Qantas has further iterated on this idea by suggesting staging the development to align more closely with demand triggers given, as IATA notes, demand forecasts are almost always wrong. Airlines consider that flexibility to bring forward or delay investment to align with demand is critical for an efficient investment programme.

Air NZ considers that true innovation occurs when airlines and airports work together in an open and collaborative process, where the requirements of all parties are well defined, and a joint (often bespoke) solution is developed. The costs and benefits should be clearly articulated for all airport users, particularly the airlines who are responsible for selling the cost of aeronautical infrastructure to end consumers in airfares. The TIP reflects a missed opportunity for AIAL to be innovative, and to invest efficiently for the long-term.

#### ***The regulatory regime does not incentivise AIAL to act in a manner that is consistent with the Part 4 purpose***

Air NZ remains of the view that the current information disclosure (**ID**) regime has failed to constrain AIAL's over-investment and excess profit-taking or to encourage AIAL to take stock of its substantial customers' valid concerns. As detailed in multiple submissions on the draft decision, this is a well-supported view that is not held by Air NZ alone. There is consistency across submissions that:

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<sup>2</sup> The Paheko East Terminal Integration Pathway was AIAL's design concept (2021) for integrating a new domestic terminal to the east of the existing international terminal.

- AIAL is consistently targeting excessive profits;
- AIAL's capital plan exceeds multiple reasonable benchmarks;
- AIAL is failing to meaningfully consult its substantial customers;
- AIAL is not sufficiently incentivised to innovate; and
- the resulting outcomes are not consistent with the outcomes of a competitive market.

Air NZ is encouraged by the many suggestions from airlines and other interested parties on how the regime can and should be amended, including recommendations on the form of regulation that should ultimately apply. Air NZ continues to advocate for a section 56 (**s 56**) inquiry as the appropriate forum to decide which different type of regulation would best serve the long-term interests of consumers.

In the interim, Air NZ also supports Qantas's submission that a baseline for efficient capex needs be established as a matter of urgency, so that AIAL is given clear guidance that inefficient capex will not be allowed into the Regulated Asset Base (**RAB**) in PSE5. AIAL could then use this information to appropriately guide the capex decisions it is making today, knowing that investment above a reasonable LoS will not be recoverable from the airline sector and ultimately from the traveling public.

Regards



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**Air New Zealand**



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## Air NZ's cross submission on responses to the consultation paper

### Section 1: Cost of Capital

1.1 AIAL's submission includes seven conclusions on cost of capital. For ease of reference, we list these below, together with Air NZ's response, with more detail provided in the remainder of this section.

AIAL Conclusion	Air NZ Position
Conclusion 1: Scenario 1 should be disregarded in the final report	Air NZ disagrees. Scenario 1 is the appropriate framework to consider AIAL's pricing as it reflects the prevailing Input Methodologies at the time of price setting and is consistent with the approach adopted by other regulated airports (and accepted by the Commission) setting prices for PSE4 in 2021 and 2022.
Conclusion 2: coding error understates baseline asset beta	The airports have appealed certain aspects of the 2023 Determination, with these appeals to be heard in 2025. These issues should not be litigated via this PSE4 review process. Pending the outcome of the appeals, which can only succeed if the Court is satisfied that the amended or substituted IM is materially better in meeting the purpose of Part 4, the 2023 IMs apply.
Conclusion 3: coding error understates Flint method pandemic uplift	
Conclusion 4: 2016 IM sampling criteria is the most reasonable to apply to the PSE4 sampling decision	
Conclusion 5: 2023 IM equity beta does not provide a reasonable basis to assess the PSE4 pricing decision and should be disregarded by the Commission in its final assessment	
Conclusion 6: Adopting a TAMRP input parameter of 7.5% is reasonable	Air NZ disagrees. AIAL is "cherry picking" a set of WACC parameters that maximise its return. We agree with the Commission that AIAL's use of a 7.5% TAMRP is not reasonable and that AIAL was " <i>inconsistent by not updating the TAMRP when it chose to update other WACC parameters.</i> "
Conclusion 7: Scenario 2 should be disregarded in the final report	Air NZ considers that Scenario 1 is the appropriate reference point for the Commission's PSE4 review.

### **Scenario One is the appropriate reference point for the Commission's PSE4 review**

1.2 AIAL has submitted that neither of the scenarios considered by the Commission as reflecting the appropriate range of the cost of capital are appropriate for reviewing AIAL's PSE4 pricing decision. Air NZ disagrees.

- 1.3 Scenario 1 is the appropriate framework to consider AIAL's pricing as it reflects the prevailing Input Methodologies at the time of price setting and is consistent with the approach the Commission has taken with respect to its assessment of the other airports regulated under Part 4 of the Commerce Act. AIAL's stance ignores the fact that the Commission's starting mid-point cost of capital is 6.98%, and Scenario 1 already provides an uplift to this starting point. AIAL has provided no adequate explanation as to why there should be a departure from the approach adopted by CIAL.
- 1.4 When making its decision on pricing for the PSE4 period, AIAL was acutely aware of the fact the Commission was undertaking a review of the Input Methodologies, and that cost of capital was a key issue for review. Nevertheless, AIAL chose to calculate its own cost of capital parameters. As it stands, and as previously submitted, AIAL's target WACC for PSE4 places undue emphasis on the pandemic period and inflates returns above a competitive level. Air NZ supports the Commission's draft conclusion that AIAL *"has implicitly assigned an unreasonably high probability to the likelihood of another COVID-19-type disruption occurring over the PSE4 period. In doing so, our draft conclusion is that Auckland Airport has calculated an equity beta that is inconsistent with the objectives in s 52A(1)(a) to (d)."*
- 1.5 Air NZ submits that AIAL had alternative options when setting PSE4 prices that would have resulted in better outcomes for consumers and substantial customers<sup>3</sup>, including:
- 1.5.1 AIAL could have set prices for PSE4 based on the prevailing Input Methodologies and sought to have a re-opening provision so that it could update its target cost of capital once the Commission had reached its conclusions at the end of the 2023 IM review; or
- 1.5.2 Alternatively, AIAL could have adopted a position similar to that which WIAL reached in its PSE5 decision regarding the airport appeals of the 2023 IM Determination, whereby it is able to introduce a carry-forward adjustment for PSE6, if appropriate.

***AIAL seeks to justify a higher target WACC based upon "cherry-picking" parameters chosen to maximise its return***

- 1.6 AIAL suggests in its submission that it was entitled to pick and choose from a range of WACC parameters when setting a target WACC for PSE4 and the prices that would apply from 1 July 2023.
- 1.7 AIAL refers to its November 2021 offer to freeze prices for the first year of PSE4, which stated that *"Auckland Airport's target return for the full five year PSE4 pricing period shall be determined during the PSE4 consultation period retrospectively as at 1 July 2022 (the*

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<sup>3</sup> AIAL's practice is to set prices too high, and then refund years later once the Commission makes an excess profit determination. Whilst this approach may be net present value (NPV) neutral for the airport, it is NPV negative for airlines, which have much higher costs of capital than AIAL.

*commencement of PSE4) by applying the relevant input parameters as at that date (e.g. including the observable interpolated 5 year risk free rate)”<sup>4</sup>.*

- 1.8 Air NZ’s understanding of this letter was that AIAL would use the prevailing WACC parameters from the 2016 IM determination and update the risk-free rate. There was no suggestion in this letter that AIAL was considering calculating its own estimates for asset beta and leverage, which Air NZ would not have supported.
- 1.9 Air NZ agrees with the Commission that given AIAL elected to recalculate its own estimates of equity beta and leverage, it should also have recalculated the TAMRP and as a result should have used a value of 7.0%. AIAL’s approach of combining its own updated estimates of equity beta and leverage with an out-dated estimate of TAMRP is a clear example of an unprincipled approach to selecting WACC parameters on the basis of maximising return.
- 1.10 We note that NZAA has argued that AIAL *“sought to apply and update the 2016 WACC IMs in its price-setting decisions, rather than depart from them”* (para.14). Air NZ agrees with TDB Advisory, which points out in its cross-submission that this statement is disingenuous because AIAL *“has departed from them in every parameter and by a substantial margin”*.
- 1.11 We also note that NZAA has argued that AIAL’s approach *“is consistent with the approach that all regulated airports adopt in their pricing decisions”* (para. 14). Air NZ strongly disagrees with this statement, and notes that both Wellington and Christchurch airports essentially adhered to the prevailing WACC IM in effect at the time they set their prices for PSE4 and, in Wellington’s case, PSE5.

### ***AIAL did not set prices in PSE4 to achieve a premium to its mid-point target WACC***

- 1.12 AIAL, aided by CEG, goes to some lengths to explain why it considers a premium on the mid-point WACC is justified. Air NZ notes that at no time during the consultation did AIAL indicate that prices would be set to achieve a premium on its mid-point target WACC. Indeed, AIAL’s PSE4 disclosure explicitly notes that the target return was based on its mid-point WACC estimate.
- 1.13 If AIAL was intending to target a return above the mid-point WACC, Air NZ would have expected the airport to explicitly consult on the reasons for seeking a WACC premium and disclose this in Schedule 18 of its PSE4 disclosure. AIAL did neither. Consequently, Air NZ does not see any relevance in the arguments proffered by AIAL and CEG suggesting the airport may have been entitled to target a WACC premium.
- 1.14 Moreover, Air NZ does not accept that any of the reasons put forward by AIAL or CEG justify a WACC premium at price setting. We agree with TDB’s observation that the Commission has *“recognised both the conceptual and practical difficulties of taking such [asymmetric] risks into account and has explicitly determined not to adjust the WACC for*

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<sup>4</sup> Auckland Airport, “Proposal on PSE4 price reset delay” (November 2021).

*them*". In all cases Air NZ submits that there are alternative risk mechanisms that AIAL could adopt that are consistent with the Input Methodologies and would result in better outcomes for consumers and substantial customers. We note the following:

- 1.14.1 With respect to asymmetric pandemic risk, AIAL has downside protection in the form of the two-way revenue adjustment mechanism which compensates AIAL in the event of under-recovery of revenue resulting from a demand shock;
- 1.14.2 If AIAL is genuinely concerned about asymmetric risk, it could consider seeking insurance cover to offlay various types of risk, including establishing a captive insurer as several New Zealand electricity distributions businesses have done. A captive would ensure that any additional charges levied on customers with a view to insuring against asymmetric risk were ring-fenced by the business for this purpose, rather than distributed to shareholders, which would be likely to occur if AIAL was able to charge a WACC premium for this purpose;
- 1.14.3 If AIAL is genuinely concerned with inflation risk, it should embrace the RAB indexation mechanism, which is consistent with the Input Methodologies and utilised by other airports for this purpose.



## **Section 2: Expected Profitability**

***AIAL is justifying over-charging domestic passengers by 21-26% and regional passengers by 33-42% over PSE4 on the basis that it is only over-charging each passenger by \$1.90-\$2.22***

- 2.1 Air NZ welcomes the Commission's draft conclusion that AIAL is targeting excess revenues of \$193-227m over PSE4. We disagree with AIAL's contention that the Commission has not established a reasonable estimate of a mid-point WACC for PSE4. Air NZ believes the Commission has clearly established that AIAL is targeting an excessively high target WACC in PSE4.
- 2.2 AIAL attempts to defend excess profits of \$193-227m over PSE4 on the basis that the excess only amounts to "*\$1.90 to \$2.22 of revenue per passenger over PSE4*".<sup>5</sup> An excess profit of \$1.90 to \$2.22 of revenue per passenger over PSE4 is equivalent to AIAL overcharging domestic passengers by an average of 21-26% over PSE4 and overcharging regional passengers by 33-42%. That AIAL believes it is entitled to overcharge customers by this amount is another clear demonstration that the regulatory regime does not incentivise AIAL to act in a manner that is consistent with the Part 4 purpose.

***The Commission should not consider AIAL's return across all aeronautical assets (priced and non-priced) unless it is prepared to undertake the wider analysis over multiple regulatory periods that it suggested in PSE3***

- 2.3 AIAL considers the Commission should give additional focus to the overall regulated return, "*as this is the most fulsome measure of Auckland Airport's aeronautical activities*".<sup>6</sup> As Air NZ has previously submitted, given the nature of the non-priced aeronautical assets and the way these are priced, the Commission needs to undertake this analysis over several regulatory periods, as it suggested in the PSE3 review. The focus on AIAL's priced return in this review is appropriate given the decisions taken in the PSE4 process related to priced activities.
- 2.4 If the Commission does determine this wider analysis is relevant, Air NZ would appreciate the opportunity to provide evidence for this assessment. When negotiating leases for non-priced assets, AIAL has in recent years consistently set lease charges on [REDACTED]. As an example, AIAL has set the proposed lease rate for the expanded Air NZ International Lounge based on achieving an [REDACTED] return over a [REDACTED] term.

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<sup>5</sup> AIAL submission - p.46

<sup>6</sup> Ibid - p.47

***AIAL has not shared sufficient information to enable substantial customers to make an informed view as to the merits of tilted annuity depreciation***

- 2.5 As stated in our submission, Air NZ supports the Commission’s conclusion that a tilted annuity approach to the recovery of depreciation is likely to better promote the objectives of Part 4.
- 2.6 AIAL contends that it consulted with airlines on alternative depreciation methods that could be adopted. This ‘consultation’ consisted of a short slide pack shared with substantial customers on 3 May 2023, just one month before AIAL announced PSE4 prices on 8 June 2023. Air NZ considers that this consultation was superficial, hurried and designed to give the appearance of consultation only. Furthermore, the only substantial proposal AIAL made was to bring PSE5 revenue forward into PSE4 and increase PSE4 pricing to offset concerns regarding the high level of indicative PSE5 pricing.
- 2.7 AIAL did not share with substantial customers any analysis as to the merits of tilted annuity depreciation as it may apply to its asset base in PSE4 and beyond. The only analysis shared by AIAL was an example where a usage-based depreciation approach was applied to a hypothetical \$1b airfield investment. AIAL repeated the same cursory analysis in its submission on the Commission’s draft report. Air NZ recommends the Commission direct AIAL to undertake a detailed analysis of the impact of applying tilted annuity depreciation to all new long-dated assets commissioned in PSE4 and PSE5. Absent this analysis it is very difficult to have an informed view on the merits of adopting such an approach in PSE4 or PSE5.

***Other evidence of AIAL’s excess profits***

- 2.8 AIAL relies heavily on the idea that its prices are in-line with other comparable airports in PSE4 and asserts that this demonstrates that the PSE4 prices do not present an affordability concern for consumers. Air NZ considers this is irrelevant in the context of the Part 4 purpose. AIAL’s prices should be set at a level that recovers the cost of its investment in the airport and reflects anticipated volume forecasts. Given the scale of operations at Auckland, and the existing level of investment, AIAL’s prices could be expected to evidence a substantial discount to “comparable” airports.
- 2.9 Qantas’ submission highlights that the over-collection of revenue is not just due to an excessive WACC, but also arises “*with regard to opex, sunk costs and other aspects of depreciation.*”<sup>7</sup> Air NZ agrees with this and detailed several additional sources of over-recovery in our initial submission. Qantas also highlights the principle that “*only assets that are efficient should be included in the regulatory asset base.*”<sup>8</sup> Air NZ wholeheartedly agrees with Qantas and as highlighted in our initial submission, considers the DJT to be significantly inefficient.
- 2.10 Air NZ supports Qantas’s conclusion that AIAL is targeting excess profits well above the Commission’s assessment of \$193-227m over PSE4. Qantas estimates the actual

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<sup>7</sup> Qantas submission – p.2

<sup>8</sup> Ibid – p.20 (section 4.4.2)

excess profits targeted by AIAL over PSE4 at \$463m (and likely to rise to ~\$2.4b in PSE5).<sup>9</sup> In its submission on the Commission's Process and Issues paper and on the Consultation Paper, Air NZ concluded that, in addition to the excess profits determined by the Commission, AIAL was also targeting excess profits over PSE4 of \$120m in relation to inefficient capex, \$20m due to tax losses and ~\$110m in relation to excess allocation of corporate overheads, giving total excess profits of \$443-477m, similar to Qantas's total excess profit assessment. The addition to Air NZ's calculation of excess profits in relation to inappropriate recovery of depreciation over PSE4 (as Qantas has done<sup>10</sup> and Air NZ supports) would increase Air NZ's estimate of the excessive PSE4 profit well above that of Qantas.

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<sup>9</sup> Qantas submission – p.12

<sup>10</sup> Ibid – p.11 (section 4.1)

### **Section 3: Investment**

- 3.1 The overwhelming consensus emerging from the submissions is that while investment in AIAL's infrastructure is considered necessary, the scale, cost, and efficiency of AIAL's capital plan is highly problematic. On this basis, we strongly encourage the Commission to update their draft conclusions relating to AIAL's investment, given the updated information provided.
- 3.2 In summary, key information in the submissions includes:
- use of inappropriate benchmarks to justify the size and cost of the Capital Plan;
  - further evidence that more efficient investment options were available to AIAL, if they had been sufficiently incentivised to work with airlines to find them;
  - evidence of critical flaws in the consultation process; and
  - a clear unwillingness by AIAL to change approach or consider alternatives and to press on regardless with their investment plans.
- 3.3 AIAL's submission is similar in approach to the responses airlines received throughout the consultation process, especially from 2021 onwards. Where airlines gave feedback that the terminal was too big and too costly and suggested what might be done to change this, AIAL simply sought to explain why the airlines were wrong, rather than consider and incorporate this important feedback into their plans. The extensive description of the so-called consultation provided by both Air NZ and Qantas attests to this.
- 3.4 Air NZ provides its response to several of the claims made by AIAL regarding investment, in Appendix 1. We summarise our overall response below.

#### ***AIAL uses inappropriate benchmarks to justify the size and cost of the Capital Plan***

- 3.5 Consistent across submissions from Air NZ, Qantas and IATA is the theme that AIAL's benchmark airport examples are not appropriate and are being used to overstate the scale of the required infrastructure. An analysis using more comparable airports (based on region, number of services, and aircraft size) provides greater insights into the overdesign and resulting high cost of delivery.
- 3.6 AIAL has stated that Christchurch (**CHC**) and Wellington (**WLG**) terminals are the "smallest in the world"<sup>11</sup> and should not be used as a benchmark. For this comment, they are referencing a graph originally supplied by Air NZ/Arup<sup>12</sup> and copied below for reference (figure 1).

In this graph, the DJT is referred to by its previous name the Integrated Domestic Terminal (**IDT**).

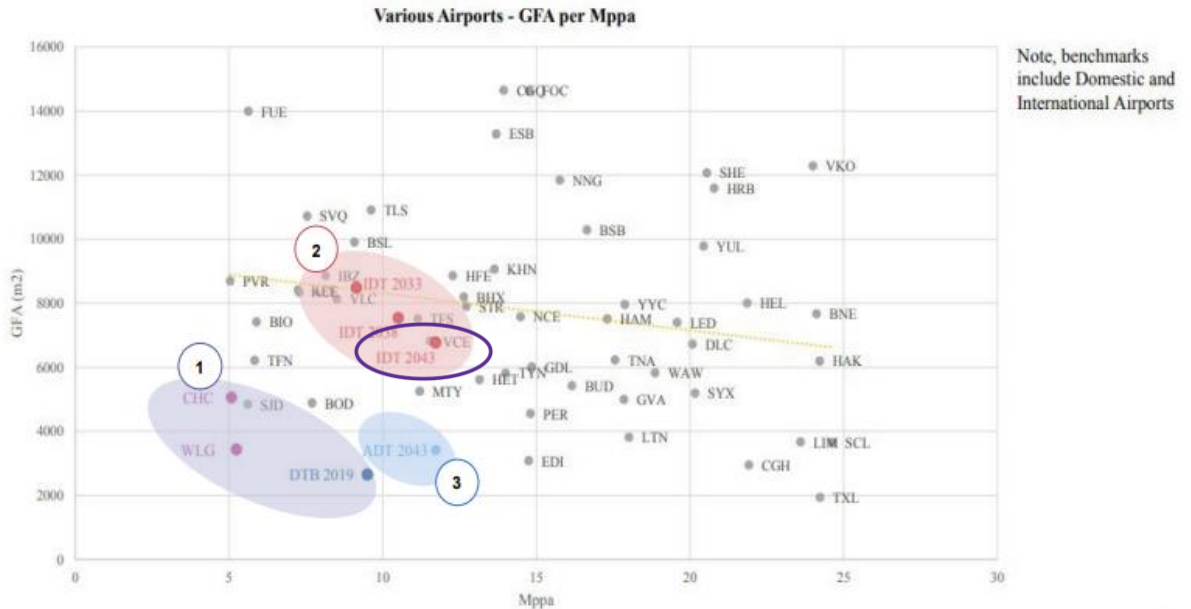
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<sup>11</sup> AIAL submission – p.57

<sup>12</sup> Ibid - p.58

Figure 1: Air NZ / Arup Benchmarking, with AIAL and Air NZ annotations

**Benchmarking**



- 3.6.1 The graph depicts only airports which have capacity for 5 million pax per annum or higher (the current DTB is ~6 million pax) and therefore excludes all airports which are smaller than this, of which there are many.
- 3.6.2 AIAL’s comment suggests it has missed the key information depicted in the graph: the terminals around or above the trendline represent terminals built with a higher LoS (international IDT and/or hub terminals).
- 3.6.3 Contrary to AIAL’s view, using WLG and CHC as benchmarks helps illustrate the domestic and international service requirements here in New Zealand and therefore what an appropriate LoS may look like for an NZ domestic terminal. This context should be part of the consideration for AIAL rather than being dismissed on the basis that other global international airports, which have a different customer base, are bigger.
- 3.6.4 The graph demonstrates very clearly that AIAL’s proposed DJT aligns mostly with large international airports, with international customers, serving international routes. These airports require a much higher LoS than a NZ domestic terminal. For example, in the graph the DJT (‘IDT 2043’) tracks closely with Venice Airport (**VCE**), circled in purple in the graph.
  - VCE has one terminal and supports 93 routes, of which only 5 are domestic and 87 are international. 11 of the 87 international routes are long-haul to USA, Canada, Middle East, China and South Korea (average route length of 3,700 nautical miles (nm)).
  - VCE experiences greater seasonal variation with sustained higher peak periods, which drives the size of airport infrastructure required. NZ domestic traffic is not highly seasonal and therefore infrastructure investment is accordingly designed for much lighter peak traffic.

- In comparison, the proposed DJT will initially support the handful of domestic routes (up to 750 nm) with the traffic to warrant larger jet aircraft (currently AKL to CHC, WLG, DUD, IVC and ZQN), with no international processes such as emigration, immigration and customs/quarantine, which add time and require passengers to show-up earlier and dwell longer.
- 3.6.5 Furthermore, Air NZ believes there are several items which should change the position of the DJT on the current graph. These are:
- 3.6.5.1 The size of the proposed DJT does not include space for check-in, as this is incorporated in the existing international check-in space. All other terminals include this space and including it for the DJT would add ~200m<sup>2</sup> per mppa in 2033 (~600-800 sqm in total) and would push the DJT to be even higher on the chart than the international airports it is compared against.
  - 3.6.5.2 The DJT will also need an additional pier by 2043 to accommodate the 17 Code C contact stands required by that horizon so the 'IDT 2043' dot would be higher on the graph when taking into account the additional pier area.
- 3.6.6 In summary, the analysis clearly shows that the proposed DJT tracks closer to international airports and justifies Air NZ's submission that the LoS provided for in the DJT is well above what should have been considered reasonable by AIAL for an NZ domestic terminal.
- 3.7 Flights within the immediate region (New Zealand, cross-Tasman and to/from the Pacific Islands) represent almost 85 percent of the flight movements at Auckland airport. This market and these destinations therefore offer appropriate airport benchmarks for comparisons on infrastructure size and capital cost.
- 3.7.1 On this basis, the cost benchmarks provided by Qantas of Perth, Melbourne, Gold Coast, Newcastle and Sydney provide reliable comparable overseas domestic-service airports for the Australian market.
  - 3.7.2 Air NZ endorses the assessment provided by Qantas for costs per sqm, cost per gate and terminal footprint. This aligns with Air NZ's assessment that the size and resulting cost of constructing the DJT are simply too big and too high, respectively, for the market in which AIAL predominantly operates.
- 3.8 Air NZ reiterates its submission that the proposed terminal is approximately double the size required and the excessive costs align with this scale.

***More efficient options were available to AIAL if they had been willing to seek them***

- 3.9 As stated in Air NZ's submission, the Air NZ/Arup proposed design revealed that there were options to deliver increases in both domestic jet and regional turbo-prop operations with lower levels of capital investment. AIAL has made several statements in its submission which we summarise from paragraph 3.14 and respond to in detail in Appendix 1.
- 3.10 In contrast, AIAL states in its submission that the DJT will provide "26% additional capacity gate capacity [sic], plus a further 10% capacity through bus lounges and 44%

*additional check-in capacity*".<sup>13</sup> Air NZ is unable to reconcile this extra 26% capacity given AIAL is only adding 2 new contact jet stands and reducing remote stand provision by 1. Additionally, Air NZ reiterates that increasing terminal or processing capacity does not substantially unlock airport passenger growth in the absence of meaningful capacity increases in additional gates and airfield capacity. Put another way, a 44% increase in check in space might speed up the time it takes for customers to reach their plane, but it does not increase the number of planes that can be accommodated and therefore does not drive growth. Furthermore, the majority of the additional space in AIAL's design is 'airside' rather than 'landside', with the latter housing much of the required passenger processing functions.

- 3.11 Both substantial users of the terminal have been consistent across their submissions that the DJT exceeds customers' expectations and requirements. Qantas states: *"the concept proposed by AIAL inefficiently exceeds industry benchmarks"* and *"the proposed capital plan far exceeds what is needed, adding significant pressure in an already high-cost New Zealand operating environment."* Air NZ agrees.
- 3.12 This compounds the view that, having failed to consult meaningfully, AIAL's design has been driven by factors other than what its customers have been asking for, which is an affordable design that meets the airlines' LoS expectations based on customer demands. Having pushed ahead with a design the airlines do not support, AIAL has disregarded the need for agreement on the fundamental business case of the new terminal, instead proposing a solution that the airlines and their passengers cannot afford. As IATA notes in its submission, any assessment of the airport's investment should include *"a clear Business Case and return on investment for users funding these projects. Inefficient capital investments must not be allowed."*<sup>14</sup>
- 3.13 Airline customers all propose a more efficient ongoing re-use of the existing DTB rather than AIAL's premature demolition and rebuild, and this feedback was provided during the consultation process. Opportunity exists to repurpose this asset alongside additional capacity created elsewhere in the airfield.

#### Response to AIAL's submission on Air NZ / Arup Alternative Design

- 3.14 This section summarises the content of Appendix 1. In summary, Air NZ and Arup do not agree with AIAL's submissions regarding the Air NZ / Arup alternative design and maintain that this concept, albeit in an earlier phase of design, has always been a valid and viable alternative - an alternative which AIAL could have sought themselves if they had been willing to meaningfully consult with airlines on alternative affordable options from 2022, or even earlier if they had reached an early agreement with airlines on an appropriate LoS, as recommended by IATA:

"The critical point to recognise is the need to establish the appropriate level of service values in consultation with the airline community and other stakeholders from an early stage in the planning process. This is a fundamental requirement to capture Users'

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<sup>13</sup> AIAL submission - p.66

<sup>14</sup> IATA submission - p.6

requirements and work towards consensus and informed joint decision-making, and that the associated costs are affordable.”<sup>15</sup>

3.15 AIAL states that the Arup design is a similar size to the existing DTB<sup>16</sup> on a per passenger basis. This is incorrect and ignores that only part of the current DTB is used for domestic jet operations.

- The existing DTB is 25,000sqm for combined domestic jet and regional traffic (9.6 mppa<sup>17</sup> in 2019)
- Air NZ/Arup’s ADT would be 35,000sqm for domestic jets only (for 9.3 mppa in 2033 and 11.4mppa in 2043), with the option of additionally utilising space in the existing DTB rather than remote gates.

3.16 AIAL incorrectly claims that the Arup design was “*incomplete*”.<sup>18</sup> The level of detail in the drawings is at functional design-level and includes calculated space for each element that AIAL claims is ‘missing’. Arup included and designed for appropriate mechanical and electrical plant space and sufficient space for an appropriately sized bus gate lounge. It is noted that AIAL’s DJT provides enough space in its bus lounge to accommodate the passengers from 3 x Code C A321 Jets at the same time, which is unlikely to occur in practice and therefore the space provision is excessive.

3.17 AIAL has incorrectly stated the capital cost of the Air NZ / Arup ADT option is effectively the same as the AIAL DJT option, because it has added together both comparable and incomparable costs to reach a figure of \$2.03bn<sup>19</sup>. AIAL’s approach is not a like-for-like comparison, as we outline below.

3.17.1 Planning forecasts generated by DKMA for AIAL indicate a need for 15 Code C domestic jet stands by 2033. The costs for accommodating this capacity for each design option are referred to as “comparable costs”<sup>20</sup>.

- Air NZ / Arup’s ADT option shows 12 Code C contact stands on a new pier and 3 contact stands on the existing DTB. This capacity is provided at a capital cost of \$1.1bn.
- AIAL’s DJT option shows 12 Code C contact stands on a new pier and 3 remote stands adjacent to the DTB. This capacity is provided at a capital cost of \$2.2bn.

3.17.2 “Incomparable costs”, by contrast, include the costs of delivering capacity outside the scope (domestic jets only) and timeline (to 2033) of the DJT. These costs are related to delivering regional (turboprops) growth, additional domestic jet growth from 2033-2043, and other airfield investment required between 2033-2043. These costs are not included in the \$2.2bn cost of the DJT.

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<sup>15</sup> IATA submission - p.5

<sup>16</sup> AIAL submission – p.57

<sup>17</sup> Mppa = million passengers per annum

<sup>18</sup> AIAL submission - p.59

<sup>19</sup> Ibid - p.60

<sup>20</sup> Air NZ / Arup, “Affordable Pathways Phase 3 - Final Report” (October 2023) - p.79



- *Regional growth:* DKMA's forecasts indicate a need for incremental stand capacity of 4 regional (turboprop) stands by 2033, and a further 1 stand by 2043.
- *Domestic jet growth post-2033:* DKMA's forecasts indicate a further 2 domestic jet stands are required by 2043.
- *ATC tower:* A new ATC tower will be required before 2043.<sup>21</sup>

The total cost of the above is estimated as \$0.852bn, with approximately half for new capacity, and half for the ATC tower. AIAL's addition of these costs to the Air NZ / Arup ADT option but not to its own design is misleading, as a like-for-like comparison would either exclude these costs for both options or include them in both options.

- 3.17.3 The quoted figure of \$2.03bn is Air NZ / Arup's estimated cost for providing full capacity needs for domestic and regional flights to 2043 – less than AIAL is proposing to spend on the DJT alone to fulfil only domestic jet capacity requirements to 2033. Air NZ's understanding is that, additional to the DJT, AIAL will need a separate [REDACTED] and an additional [REDACTED] to deliver appropriate stand capacity to 2043.
- 3.17.4 The above is further evidence of the limits of considering a multi-decade investment plan within the construct of an ID regime that looks at discrete 5-year pricing blocks only and a 10-year capital plan. It further emphasises why best practice for airports globally includes having an up-to-date master plan, renewed at least once every five years, to reveal the true pathway for capacity expansion and allowing for the associated costs to achieve this to be estimated by interested parties.
- 3.18 AIAL states that its gate lounge assessment against IATA LoS provisions suggests that its design is right-sized.<sup>22</sup> Air NZ reiterates its submission that AIAL has incorrectly measured the gate lounge space provision. A correct application of the IATA methodology reveals these gate lounges are oversized when compared to IATA's proposed LoS.
- 3.19 AIAL refers to 'space efficiency' benefits of the integrated baggage system<sup>23</sup> but ignores the fact that the existing DTB baggage system will continue to be used to facilitate the ongoing operation of the DTB which could extend for another 10 years and that this also takes up space. It fails to recognise that its own design pathway includes a future [REDACTED] that requires its own [REDACTED] which, again, will take up additional space.
- 3.20 Regarding the size of AIAL's DJT by comparison, AIAL's submission appears to quote Arup out of context as saying the new processor is "sized for [the] appropriate number

<sup>21</sup> Note this capital cost would be borne by Airways and charged to airlines through Air Navigation Charges levied by Airways, not by AIAL through aeronautical charges. Therefore, Air NZ would consider this outside of the scope of AIAL capital consultation, unless the impact of AIAL's capital planning were to materially amend the expected timeline or cost of a new ATC tower.

<sup>22</sup> AIAL submission - p.64

<sup>23</sup> AIAL submission - p.65

*of domestic passengers*".<sup>24</sup> This reference is taken from the option scoring rationale for the potential of a terminal processor to provide appropriate passenger processing capacity. The scoring acknowledged that the DJT does provide capacity, but this is at a higher IATA LoS than is necessary. The same option scoring goes on to score the DJT negatively in terms of the costs of including significant non-processing elements such as additional retail, dwell and back-of-house space. For AIAL to cite this as an 'endorsement' ignores the context in which it was written.

- 3.21 AIAL has referenced this one line to try to justify the size of the DJT which is misleading. The criterion that captures over-design relates to the cost that AIAL refuses to acknowledge as being double that of the ADT.

### ***AIAL's submission details further flaws in the consultation process***

- 3.22 AIAL has welcomed the Commission's comment that "*extensive consultation can lead to delays in the delivery of planned capital investment*"<sup>25</sup>. By contrast, Air NZ considers that if AIAL had taken the opportunity in 2021 or 2022 to meaningfully consult with airlines on a more efficient design once costs spiralled, a less costly and appropriately staged approach to construction could have been agreed. It is reasonable to expect this would have resulted in a less complex construction programme, with stand capacity being delivered earlier than currently forecast, and with fewer operational disruptions.
- 3.23 Therefore, Air NZ disagrees with AIAL's assertion that "*further delay to the delivery of this essential infrastructure is only expected to make it more expensive to build*".<sup>26</sup> This statement ignores the benefits of a less complex and appropriately staged construction programme, as well as the considerable cost savings generated from choosing a more efficient long-term path. As Air NZ has highlighted in paragraph 3.17.3, full domestic and regional capacity needs as far as 2043 could cost less than the cost of delivering only domestic jet capacity to 2033 in the DJT alone. Air NZ encourages AIAL to share with the Commission its own projections of the full cost of delivering both domestic jet and regional capacity to 2043 to enable a true comparison with the Air NZ/Arup proposed pathway, rather than repeating unsupported assertions about the relative costs.
- 3.24 AIAL refers to a history of "*options assessment*" in its submission.<sup>27</sup> However, presenting options without the provision of accurate cost implications is meaningless, particularly when these options result in a materially changed business case for the airport's customers. AIAL failed to provide accurate costs and aeronautical pricing implications for its options. Airlines cannot have been meaningfully consulted on any option where the most important underlying assumptions were materially incorrect.
- 3.25 As a comparison of good practice, the New Zealand Treasury's 'Better Business Cases' (BBC) Detailed Business Case methodology<sup>28</sup>, (used by NZ Government to objectively assess project value) allows for better comparability and transparency and enables

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<sup>24</sup> Ibid - p.47

<sup>25</sup> Ibid - p.55

<sup>26</sup> Ibid - p.68

<sup>27</sup> AIAL submission - p.56

<sup>28</sup> <https://www.treasury.govt.nz/sites/default/files/2019-08/bbc-options-framework-analysis.pdf>

decision makers to form smart investment decisions that maximise value. The options assessment utilised by AIAL would have been rejected if measured against this methodology given a lack of comprehensive option development and a lack of assessment and inclusion of weighted criteria for cost. Had AIAL's assessment taken these factors into account, its preferred option would have been discounted for requiring excessive capital investment, with the cost materially exceeding the associated value to consumers.

- 3.26 To reiterate, when finally presented with the full cost implications of both the terminal and the wider Capital Plan, Air NZ and other substantial airline customers immediately withdrew support for the design. Air NZ asserts that under either competitive market conditions or under government-led infrastructure investment, the project would not have proceeded.

***AIAL should not be permitted to recover from airlines the cost of proceeding with an inefficient investment decision that they did not support***

- 3.27 AIAL's submission criticises Air NZ for not considering the sunk costs of the Eastern Hall construction works, including the work started during the PSE4 review process in July 2024<sup>29</sup>. Air NZ originally provided "conditional support" for the Eastern Hall enabling work in August 2022 on the basis it would support on-time delivery of needed baggage hall capacity and the planned Air NZ international lounge expansion. Air NZ had been assured that solutions would be designed to meet minimum requirements needed and would avoid or minimise "regret spend". Air NZ's conditional support was lost when subsequent over-design and forecast pricing for the DJT was significantly higher than previously indicated by AIAL.
- 3.28 This highlights a pattern of behaviour whereby AIAL leverages earlier works to justify future projects having ignored the assurances given and the concerns raised at the time of the earlier works. It also supports Air NZ's assertion throughout the PSE4 consultation process that there has never been any real 'optionality' in AIAL's plan, and that support for one smaller element of the plan is effectively used as a 'Trojan Horse' by AIAL to claim wider endorsement of the overall plan.
- 3.29 Air NZ maintains that many of the 'sunk costs' suggested by AIAL for proceeding with an inefficient design are irrelevant – AIAL made their own decision to proceed with an inefficient investment for which their substantial customers had formally withdrawn support. AIAL should bear the financial risk of this decision.

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<sup>29</sup> AIAL submission – p.62

## **Section 4: Innovation**

- 4.1 The submissions in response to the Consultation Paper (including those of AIAL and NZAA) reinforce Air NZ's view that AIAL is not demonstrating innovative practices, and that the ID regime is not providing AIAL with an incentive to innovate.
- 4.2 Air NZ notes that AIAL (and NZAA) seek clarity on how to define and measure innovation, with AIAL requesting clarity on *"how the Commission will be assessing innovation and how this interacts with efficiency, quality and incentives to invest"*.<sup>30</sup> The inability of AIAL and NZAA to define innovation or understand how innovation should be measured, despite being subject to Part 4 regulation for over 15 years is of concern. As Air NZ has noted in previous submissions, innovation does not appear to be an issue for WLG or CHC airports to date. Air NZ considers this illustrates that the ID regime does not incentivise innovation when applied to an airport with overwhelming monopoly power.

### ***What is innovation?***

- 4.3 Air NZ agrees with the Commission's view on innovation as set out in the Consultation Paper:
- "the discovery and use of new information, leading to the development of new goods or services, and/or more efficient production techniques, and that innovation is not the same as the adoption of industry best practice from New Zealand or overseas."*
- 4.4 True innovation is not simply the introduction of new technology but ensuring that the best and most efficient use is made of resources and infrastructure that are available. This can only occur when airlines, airports and other key airport stakeholders work together in an open and collaborative consultation process, and where the needs and pain points of all parties are clearly articulated and a joint solution is worked on. As recognised by the Commission in its series of 2013 section 56G reviews, the ability of airports to facilitate innovation, as recognised by airline stakeholders, is a key factor in any assessment of whether the Part 4 purpose is being met.

### ***Assessing innovative performance***

- 4.5 The Commission has previously considered the following factors as important when assessing innovation:<sup>31</sup>
- evidence of innovation occurring at Auckland Airport, comparisons with innovation at other airports, and awards for innovation; and
  - whether Auckland Airport enables or facilitates innovation through collaboration.

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<sup>30</sup> AIAL submission - p.81

<sup>31</sup> Final report to the Ministers of Commerce and Transport on how effectively information disclosure regulation is promoting the purpose of Part 4 for Auckland Airport, Section 56G of the Commerce Act 1986, 31 July 2013, paragraph B8.

- 4.6 Based on the evidence presented during the review process to date, AIAL fails on all measures.
- 4.7 In the Consultation Paper the Commission requested that AIAL provide more evidence of innovative practices. The examples provided by AIAL in response to this request fail to demonstrate a commitment to innovation:
- 4.7.1 Several ‘innovations’ listed by AIAL are simply initiatives required to meet regulatory requirements, responses to identified problems, or the implementation of long overdue upgrades to meet industry standards. For example, it is incumbent upon every airport to develop a plan to reduce the risk of bird strike and to develop a plan based on the unique features of that airport. Nothing in AIAL’s description suggests it is doing anything innovative compared with other airports.
  - 4.7.2 The stormwater treatment ponds are required to prevent a repeat of the flooding of the airport in January 2023, which exposed significant vulnerabilities in the existing storm water infrastructure. This is essential infrastructure not innovation.
  - 4.7.3 Improvements to the arrival process only occurred when the arrivals process had reached a crisis point, had been amplified by stakeholders, and was covered by media, prompting a call to action by Air NZ CEO Greg Foran.
  - 4.7.4 Finally, while it is pleasing to see AIAL re-purposing concrete and setting targets to divert waste from landfill, this practice is commonplace with these types of projects.
- 4.8 As the Commission notes (see paragraph 4.3 above), there is a difference between being innovative, and simply introducing something new to replace something old, no longer working, or obsolete. Several examples provided by AIAL are directly connected to the introduction of technology or systems into the DJT, such as the Eastern Baggage Hall, new air conditioning, and common use Automated Bag Drops (ABDs). These are all examples of business-as-usual technology uplift associated with a new build, and common practice at other airports. It would be extremely unusual if AIAL did not implement more modern technology as part of the terminal rebuild. True innovation would involve introducing more effective and efficient processes to reduce the size and cost of the Capital Plan.
- 4.9 Other examples of innovation provided by AIAL are (or appear to be) appropriations of initiatives or practices developed by third parties. To the extent that these are innovative, it is difficult to reconcile how they are examples of innovations by AIAL. For example, AIAL’s support of and participation in the Girls in Infrastructure Programme should be commended, however Air NZ understands this programme was established in 2019 by an employee of BECA.<sup>32</sup>

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<sup>32</sup> See <https://www.girlsininfrastructure.org.nz/about-5>

- 4.10 AIAL cites its Level 4 Airport Carbon Accreditation from the Airports Council International (ACI). However, this does not set it apart from other New Zealand airports. Ten New Zealand airports currently have ACI Carbon Accreditation, with five airports having an equal to or higher accreditation than Auckland airport.<sup>33</sup> Internationally, most of the world's busiest airports hold a similar or greater level of accreditation. Sixty-four airports worldwide have a higher accreditation than AIAL's Level 4. This is just one example of how far AIAL is back in the pack relative to innovation at other New Zealand airports, as covered in more detail in Air NZ's previous submission.
- 4.11 In its 2013 s56G review, one of the reasons the Commission found that AIAL was innovating appropriately was that airlines supported the view that AIAL enabled or facilitated innovation through collaboration. This is no longer the case. Airlines do not see AIAL as innovative, or as a facilitator of innovation. In a truly innovative airport environment Air NZ would expect AIAL to work with airlines and key airport stakeholders in an open and collaborative consultation process. AIAL's unprecedented capital programme is an ideal opportunity to incorporate the knowledge and experience of airlines to maximise the efficiency of new facilities and technology (see Air NZ's submission of 2 Sept 2024 at paragraphs 4.7 – 4.8 for examples of where this could have been put into practice). Unfortunately, AIAL has shown little inclination to meaningfully engage with Air NZ and innovate to improve operational processes, or even to facilitate Air NZ's own innovations.

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<sup>33</sup> CHC - Level 5; NPE - Level 4+; ZQN – Level 4+; PMR – Level 4; HLZ – Level 4.

## **Section 5: Assessment of the Regulatory Regime**

5.1 Air NZ remains of the view that AIAL's behaviour is not consistent with the purpose of Part 4 and that the current regime has failed to constrain AIAL's behaviour or encourage AIAL to pause and take stock of their substantial customers' valid and well-supported concerns. As detailed in submissions from multiple parties on the draft decision, this is a view that is not held by Air NZ alone.

### ***AIAL continues to 'push forward' with its Capital Plan despite demonstrated inefficiencies and disregard for consumer demand***

5.2 Previous reviews by the Commission of the ID regime have concluded that, when determining efficiency of investment, "stakeholders were generally satisfied with proposed investment plans for the next pricing period"<sup>34</sup>. It is well documented that this is not the case in respect of this generational capital plan over both PSE4 and PSE5. Despite this, AIAL continues to forge on, publicly announcing on 16 September that "our infrastructure development programme continues to accelerate with the signing of the Hawkins contract, a key element in our capital investment programme"<sup>35</sup> and at the same time announcing a capital raise to assist with the funding of AIAL's capital investment programme over both PSE4 and PSE5.

5.3 In an associated media release<sup>36</sup> made by AIAL, it is noted that a key contract for approximately \$800 million has been signed but, as the footnote explains, this \$800m figure is only an estimate, with a fixed price lump sum amount for the works expected to be provided by mid-2026 following a competitive tender process. This amplifies Air NZ's concerns that AIAL does not have a handle on the costs for this capital spend. AIAL is simply forging ahead partly because they do not perceive there to be any threat of stronger regulation.

5.4 While all parties agree that a level of investment is needed to address capacity constraints and challenges with legacy infrastructure, AIAL's customers do not agree that there is any urgency to rush to construction of a capital plan that they neither agree with nor support. It appears AIAL are manufacturing an artificial timeline – the truth remains that, given the integrated terminal will not immediately unlock capacity, there is no benefit in rushing forward when AIAL does not have the support of its key stakeholders.

5.5 If acting consistently with the Part 4 purpose, AIAL should be focused on ensuring that efficiency gains are shared with customers, leading to lower prices and (as stated above in Section 2) not trying to justify over-charging passengers in PSE4 and arguing that such over-charging needs to be "*considered in the context of the total price of domestic and international airfares*".<sup>37</sup>

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<sup>34</sup> Para 4.2.1 "Effectiveness of Information Disclosure Regulation for Major International Airports – August 2014" by Ministry of Business, Innovation and Employment

<sup>35</sup> ['Ageing infrastructure' - Auckland Airport announces \\$1.4b equity raise \(1news.co.nz\)](https://www.1news.co.nz/2019/09/16/ageing-infrastructure-auckland-airport-announces-1.4b-equity-raise/)

<sup>36</sup> [Building for the long haul: Auckland Airport to partner with Hawkins on construction of new domestic jet terminal | Auckland Airport](https://www.aucklandairport.co.nz/news/2019/09/16/building-for-the-long-haul-auckland-airport-to-partner-with-hawkins-on-construction-of-new-domestic-jet-terminal/)

<sup>37</sup> AIAL submission - p.46

***This is an unprecedented build with significant impacts into future price setting events yet we can only look to PSE4***

- 5.6 NZAA in its submission encourages the Commission to focus “*on the long-term benefit of all consumers and to continue to carefully test the views of participants focused on their short-term interests*”<sup>38</sup>. NZAA goes on to suggest in its submission that airline operators are opposing decisions that do not suit their short-term interests. By contrast, Air NZ notes the submissions by IATA, Qantas, A4ANZ and Air NZ all call for an assessment of the longer-term benefits to consumers, by considering the efficiency of the capital plan and the associated impact of allowing inefficient investment to impact pricing beyond the PSE4 period. As stated in our earlier submissions, Air NZ considers that this regime (where the review process considers only five-year increments) is inefficient in respect of a capital programme of this size which spans multiple pricing periods without providing any significant capacity growth.
- 5.7 Therefore, we continue to encourage the Commission to have regard to AIAL’s full capital expenditure and investment plan – particularly where, as stated by BARNZ, “*work in progress in one price period will impact prices for the next*”<sup>39</sup>.

***AIAL’s behaviour is not in the best interests of consumers***

- 5.8 NZAA has stated that “*in this country, the lack of competition in the airline market...means that domestic airfares are likely to significantly increase regardless of comparatively small increases to airport charges*”<sup>40</sup>.
- 5.9 This statement is misleading. Aeronautical charges are one of the largest single cost categories of airlines operating in NZ, and this cost line is due to increase by [REDACTED] by 2032 based on AIAL’s own indicated pricing.
- 5.10 Demand studies provided to the Commission to date show the cumulative impact that AIAL’s plan will have on passenger growth and, as stated by LGNZ, “*further increases don’t just have a direct impact on consumers in the short term. They could represent an existential threat to smaller airlines...*”<sup>41</sup>. This is not just true for smaller regional players but also is likely to have an impact on international carriers looking to operate services to/from Auckland, some of whom have already made decisions to exit the market since the start of the PSE4 pricing period.

***This is the fourth price setting event and AIAL continues to target excessive returns***

- 5.11 The purpose of regulation is to provide airport businesses – which in New Zealand are natural monopolies – with the right incentives to act in a way that benefits consumers over the long term.

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<sup>38</sup> NZAA submission – para. 13, p.4

<sup>39</sup> BARNZ submission – p.9

<sup>40</sup> NZAA submission – para. 13(c), p.5

<sup>41</sup> LGNZ submission – p.2



- 5.12 NZAA has stated in its submission regarding the Commission’s finding that AIAL is targeting excess profits, *“this is not a case of an airport disregarding the regulatory settings. It is not a sign of regulatory failure”*<sup>42</sup> because AIAL will respond and *“adjust its pricing – just as it did in PSE3”*<sup>43</sup>. Air NZ agrees with the statement made by BARNZ in its submission that *“it would be more remarkable had AIAL not targeted excess profits. Airlines have come to expect that Auckland Airport will target an excess profit when setting prices. The only question is, how much?”*<sup>44</sup>.
- 5.13 Furthermore, as Air NZ noted in our own submission – adjusting its prices to reduce the WACC only impacts static inefficiency, and not the dynamic inefficiency of AIAL’s excessive capital plan.
- 5.14 Air NZ contends that if the regime was working as intended, the findings of the Commerce Commission for PSE4 would have concluded that AIAL was, in fact, targeting an appropriate return. They did not.

#### ***Flexibility is not a unique characteristic of the ID regime***

- 5.15 In its submission, NZAA state (para. 11) *“A key benefit of the airport regulatory regime is that it provided airports and their customers with flexibility to appropriately respond to the disruption and volatility caused by the COVID-19 pandemic”*. Air NZ contends that this is not a unique feature of the ID regime - the same flexibility exists under a negotiate/arbitrate regime and could also reasonably exist under a price path regime. There have been multiple global examples of airports under various regulatory regimes and their airline customers working together to respond to the significant uncertainty that existed at that time. As many of these arrangements were confidential, Air NZ would be prepared to discuss these in confidence with the Commission with the appropriate approvals from relevant airport partners.
- 5.16 Investment of the scale proposed by AIAL is just as unprecedented as the nature of the COVID-19 pandemic – “flexibility” cannot be considered a benefit when AIAL is able to unilaterally determine the scale of the investment when the impact of such will be felt by New Zealand for generations to come. An urgent section 56 inquiry would be the right mechanism to consider whether a move to a more balanced form of regulation for airports is required in the face of these considerations.

#### ***After four Price Setting Events, it is concerning that airports need to clarify the definition of innovation***

- 5.17 The submissions confirm our view that the ID regime is not providing AIAL with an incentive to innovate. AIAL and NZAA’s lack of clarity on what innovation is and how it will be assessed may be due, in part, to the fact that it has been over ten years since the Commission last undertook a substantive review of AIAL’s incentives to innovate in its

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<sup>42</sup> NZAA submission – para. 7, p.2

<sup>43</sup> Ibid - para. 16, p.6

<sup>44</sup> BARNZ submission - para 2, p.2

2013 section 56G review, despite several PSE reviews during that period. Effective regulation requires a more consistent, in-depth review of this limb of the Part 4 purpose.

- 5.18 Notwithstanding the above, Air NZ considers this an example that the regime itself and the threat of heavier handed regulation is not sufficient to ensure that AIAL is incentivised from the outset to innovate and to make this a core part of how they operate.

***A s 56 inquiry is needed urgently***

- 5.19 Air NZ remains of the view that there is a pressing need for, and supports the call made by several other submitters for, a fast-tracked inquiry into airport regulation under s 56 of the Commerce Act.
- 5.20 Air NZ is encouraged by the many suggestions from submitters on how the regime could be improved to ensure that this scenario (where AIAL presses ahead with an inefficient and unsupported capital programme) is never able to occur again. This reinforces the need for an inquiry to determine what different type of regulation would be in the best interests of consumers.
- 5.21 Airlines for Australia and New Zealand (A4ANZ) deem the Commission's view that it cannot have regard to AIAL's full investment proposal and PSE5 pricing as evidence of the need for a s 56 inquiry. Air NZ supports that assessment.
- 5.22 Qantas's submission further evidences the considerable time and resource expended by airline customers to limit the risks to the sector and the wider economy associated with AIAL's inefficient design.<sup>45</sup> Air NZ concurs and considers if AIAL were incentivised to seek better outcomes for consumers in line with the Part 4 purpose, they would have sought to benefit from the airlines' willingness to invest their own resources in finding better solutions. Air NZ also considers that the considerable expense that substantial customers have incurred should be considered an inefficient cost of the ID regime. For PSE4, Air NZ's costs are already running at several million dollars. This demonstrates why a s 56 inquiry is the appropriate process to determine which regime offers the best outcomes for consumers balanced against the true cost of administering each regime.
- 5.23 Air NZ agrees with Qantas's observations that the regulatory process itself is inefficient and failing consumers and requires urgent review under s 56.
- 5.24 Similarly, we agree with IATA's assessment that while tweaks to the current ID regime would be welcomed, a s 56 inquiry is the appropriate pathway to adequately assess what alternative regime would be in the best long-term interests of consumers.

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<sup>45</sup> Qantas submission - para. 6.2

## Appendix 1 – Section 3 Investment – Detailed Comment

Pg	AIAL comment	Response
	<a href="#">Ref - Arup analysis for Air New Zealand</a>	
57	Auckland Airport considers that many of the findings contained in the Arup analysis validate the approach that has been adopted by Auckland Airport in designing the Domestic Jet Terminal. We set out below further comments on these three phases of work.	In principle, we agree that a terminal in a similar location to the DJT offers advantages. However, this terminal needs to be appropriately sized for the NZ domestic context, with essential processor and pier infrastructure, retail appropriate for short passenger dwell times and only necessary integration that provides efficiencies rather than adding cost and complexity.
	<a href="#">Ref - Assessment against global benchmarks</a>	
57	Arup has benchmarked the proposed design of the DJT against other airports globally. This analysis, with Auckland Airport annotations, is shown below in Figure 8. This shows benchmarks of gross floor area by annual passenger volumes, which demonstrates that:	See next comments below:
	1. The existing Domestic Terminal Building at Auckland Airport, and terminals in Christchurch and Wellington, are the smallest in the world when benchmarked against terminals globally.	These terminals reflect the NZ domestic context which should also be the context for DJT which will be a <u>NZ domestic</u> jet facility. It is inappropriate to compare this, for example, to the size of a global international hub terminal in Singapore or New York.
	2. The DJT (labelled IDT) in the below, is in-line with global comparators in the 2033 design year, reducing out to the 2043 design year.	Air NZ disagrees. The chart does not represent reasonable comparator airports. This chart was generated to show the difference between the NZ domestic context and international comparators and instead should be used to demonstrate where the appropriate LoS for an NZ domestic terminal might be.  AIAL's DJT aligns with <u>international</u> airport examples such as Venice which has one terminal and supports 93 x routes, of which only 5 are Domestic, 87 are international (average route length of ~3,700 nm). 11 of the 87 international routes are long-haul to USA, Canada, Middle East, China and South Korea (average route length of 3,700 Nm). In fact, the DJT will only support a handful of domestic routes (AKL to CHC, WLG, DUD, IVC and ZQN – with potentially a few further routes added over time) so up to 750 nm with no international processes

		<p>such as emigration, immigration, customs/quarantine which add time and require passengers to show-up earlier and dwell longer.</p> <p>Moreover, the size AIAL has provided for the DJT does not include check-in which would add ~200m<sup>2</sup> per mppa in 2033 and would push DJT to be even higher on the chart than the international airports it is compared against. Furthermore, the DJT will itself need an additional pier to 2043 to accommodate the 17 Code C contact stands required within that time horizon so the circle shown would be higher by this time horizon when taking into account the additional pier area.</p>
	<p>3. The Arup developed alternative Adjacent Domestic Terminal on a per passenger basis would be smaller than global comparators, and on a per passenger basis would be a similar size to the existing Domestic Terminal Building. It is well recognised by all users of the Domestic Terminal Building that it is at capacity and is not delivering a good customer experience.</p>	<p>Air NZ disagrees. This statement ignores that the existing DTB includes both domestic and regional traffic. This existing DTB is 25,000m<sup>2</sup> (for 9.6 mppa in 2019 Dom + Reg) and ADT will be 35,000m<sup>2</sup> (for 9.3 mppa in 2033 and 11.4mppa in 2043, Dom only). Note the ADT proposal also considers use part of the DTB (3 stands in 2033 and 5 stands in 2043) so total area provision per mppa across both terminals is higher than shown in the chart by making use of these existing assets.</p> <p>AIAL has taken this chart out of context.</p>
<p>58</p>	<p>It is important to be mindful that this benchmarking analysis is against existing airport terminals at a point in time. The airports benchmarked are now open and in operation, so their benchmark measure will decrease over time as passenger numbers grow into the existing facility – i.e. these benchmarks would have been higher when they first opened. This dynamic will also apply to the DJT over different demand horizons from 2033 to 2043 (red shaded area “2” in the diagram above).</p>	<p>See next comments below:</p>
	<p>Accordingly, it is standard practice for a new terminal to start higher on these benchmarks and decrease over time. This further supports that the DJT has been designed to an appropriate size and the ADT would be too small.</p>	<p>Air NZ’s ADT also achieves this. We have added the 2033 ADT area per mppa to show how this provides more capacity than DTB.</p>



	<p>The Arup analysis also considers that the DJT has been designed and sized appropriately. When scoring of the shortlisted terminal options including the DJT, it noted the following about Auckland Airport’s design: “New processor sized for appropriate number of domestic passengers”</p>	<p>This quote has been taken out of context. The scoring mentioned is on the potential of a terminal processor to provide appropriate passenger processing capacity which, in theory, the DJT does, however this is at <u>a higher IATA LoS than is considered necessary</u>. The DJT includes significant additional retail, dwell, gate lounge and back-of-house space (i.e. non-processes) which inflate its size and which are not appropriate or necessary in an NZ Domestic context. Seeking out this one line in an evaluation table to try to justify the size of the DJT is misleading.</p>
<p>Alternative options considered</p>		
	<p>Arup developed and scored 14 different options for providing domestic terminal services at Auckland Airport. This was then reduced to a shortlist of four alternative terminal options, of which the Adjacent Domestic Terminal option was favoured by Air New Zealand. The other three shortlisted options all included a remote operation of Pier A1 which provided the new Domestic Jet capacity, with passengers required to be bussed to the remote pier, resulting in a complex operational solution, and a poor passenger experience.</p>	<p>Of the 14 options, a range of terminal variants were considered including processor/pier, remote gate lounge, northern Domestic terminal, expanding DTB with relocation of JUHI etc. The ADT processor and pier arrangement scored the best of these 14 options.</p>
	<p>Accordingly, of the 14 different options identified by Arup for Air New Zealand, the Adjacent Domestic Terminal alternative was presented by Air New Zealand as the viable alternative.</p>	<p>This statement significantly oversimplifies the evaluation that was undertaken. The ADT was not the only viable option, it was the <u>preferred</u> option which scored most highly across a number of metrics <u>which included cost</u>. Air NZ did not discard all the other options, we simply chose one preferred option to take to the next stage of costing and analysis.</p> <p>If, at this next stage, the cost of the terminal had changed the option’s ranking in the underlying scoring system, another option would have been chosen as the higher ranking option. Air NZ notes that in AIAL’s own options selection system, cost/business case for users was not a major feature, which was a critical flaw.</p>

Alternative Adjacent Domestic Terminal	
<p>Auckland Airport undertook an assessment of the information that was shared by Air New Zealand on the proposed alternative design. That analysis and assessment has since been published by the Commission as part of this review. As noted by the Commission, this assessment found that the design was incomplete, did not meet the requirements to be a fully functional terminal, would result in poor customer experience, lacked an operational model, and offered a low level of integration.</p>	<p>Air NZ notes that the Commission did not complete its own independent review to come to this conclusion, and this incorrect assertion that the ADT is "incomplete" and not fully functioning was provided by AIAL. Air NZ and Arup maintain that the ADT is a viable alternative to the DJT and is confident an independent review would reach the same conclusion.</p>
Cost estimates	
<p>The Air New Zealand submission focused on a cost of \$1.1 billion for the Adjacent Domestic Terminal. Auckland Airport has previously outlined why this does not provide a valid cost comparison, including its exclusion of financing costs, unrealistic escalation assumptions, and the exclusion of fundamental requirements in the design. Auckland Airport maintains that a more accurate cost gap between the two solutions on a like-for-like comparison is \$100 million, rather than the \$1 billion suggested by Air New Zealand.</p>	<p>ADT is fully functioning and has been costed by a well-regarded international QS with experience of costing at AIAL. The QS costed the ADT at \$1.1bn. We comment below on the flawed basis upon which AIAL asserts the gap is around \$100m.</p>
<p>Despite Auckland Airport advising Air New Zealand of these differences in cost estimates in December 2023, its submissions on cost have continued to mislead this review, claiming that its \$1 billion cost difference reflects costs that are estimated on the same basis (when they are not):                      Estimated on the same basis, the cost for AIAL's DJF came out at ~\$2.2bn which is the same cost AIAL has disclosed for the DJF portion of the Integrated Terminal Programme.                      The Arup materials indicate that there are an additional \$852 million of capital costs, over and above the \$1.1 billion in costs cited by Air New Zealand for the Adjacent Domestic Terminal solution – these have been described as 'incomparable costs'.                      Inclusion of these costs results in the total capital cost of the Adjacent Domestic Terminal of \$2.04 billion.</p>	<p>The same QS costed AIAL's proposal as part of Air NZ's own due diligence on DJT and these QS costings came out at the \$2.2bn that AIAL had advised.</p> <p>The additional \$852 million costs stated relate to the expansion required for Regional turboprop services to 2033 (in DTB) as well as growth to 2043 (i.e. in PSE 6/7) for Domestic and Regional services, as well as the construction of a new ATC tower before 2043. This level of required growth has not been included in AIAL's \$2.2bn and are therefore incomparable costs.</p> <p>Including these incomparable costs is incorrect and not a 'like-for-like' comparison – they either need to be included or excluded for both. The like-for-like comparison is between the DJT and ADT in 2033.</p>

<p>These additional capital costs were not shared in the materials that were provided by Air New Zealand when it proposed the Adjacent Domestic Terminal option in October 2023. Inclusion of these costs would not appear to address many of the issues Auckland Airport has identified with the costings that have been presented by Air New Zealand. This indicates the overall costs of this alternative could well be materially higher than Auckland Airport's current proposal. Further detail on these costs would better inform the Adjacent Domestic Terminal proposal.</p>	<p>This is incorrect for the reasons stated above.</p> <p>If AIAL were to also include the cost of the Regional pathway to 2033 as well as the need for Domestic and Regional growth to 2043 it would be much higher than \$2.2bn it has quoted.</p> <p>It could be argued that AIAL has been remiss in not providing an updated master plan with clear indications of longer-term investment required in PSEs beyond 2032 to meet passenger demand, which will lead to an additional cost burden for Substantial Customers.</p>
<p><b>Evaluation and scoring</b></p>	
<p>Arup as part of its analysis evaluated and scored the different options it developed as alternatives, including the 14 different options on its long-list, and the four shortlisted options it then investigated further. These evaluations and scores included the Auckland Airport DJT design.</p>	<p>See next comments below:</p>
<p>In its evaluation of the short-listed options, Arup scored the functionality of each solution, and then compared this alongside the estimated capital costs of these solutions. Excluding capital costs, Arup evaluated its Adjacent Domestic Terminal proposal with a total score of 30, compared to a score of 28 for Auckland Airport's solution. These were both materially higher than the other shortlisted options, that scored between 17 and 24 on operational measures.</p>	<p>Based on the criteria selected, ADT and DJT were the higher scoring options. However, DJT scored materially worse on cost because of the inefficiencies that have been identified. The assessment did not include a category for "over-design" in the evaluation as none of the options developed for Air NZ were over-designed. The only criterion that captures this over-design is the cost which AIAL refuses to acknowledge as being double that of the ADT.</p>
<p>Arup provided the same scores for the two solutions across all functional areas of assessment except for operational impact, where it scored its Adjacent Domestic Terminal 5/5, compared to 3/5 for the Domestic Jet Terminal design. This difference is explained by Arup: Single Code C taxilanes provide risk of significant delay from stands on east side of pier and overall airfield.</p>	<p>Airfield modelling commissioned by Air NZ shows increased airfield delay with a single taxi-lane to the east of Pier A1.</p> <p>AIAL's own modelling consultant also identified delays on the east side of Pier A1 when using a 2023 schedule, let alone a future flight schedule.</p>

<p>Auckland Airport has set out in detail in its response to the materials provided by Air New Zealand why a single code C taxi-lane as designed for the DJT is not expected to have the operational impacts assumed by Arup. Accordingly, Auckland Airport considers that a score of 5 on operational impacts would be more accurate. Further, given the operational concerns identified by Auckland Airport with the proposed Adjacent Domestic Terminal we consider that the score of 5 should be revised downward. We also consider that high level analysis of the other scores indicates that the airside score of Integrated Domestic Terminal should increase from 4 to 5, to align with its assessment of 'Regional Headhouse' option (which was scored 5). These changes alone would result in a higher score for the DJT, than the Adjacent Domestic Terminal. Auckland Airport considers further critical analysis of the other scoring criteria would likely identify additional changes that would widen the gap even further between the evaluation of these options.</p>	<p>Based on AIAL's own modelling and Air NZ's independent modelling, we disagree in terms of airfield congestion and delay. Air NZ's independent modelling suggests that a dual code C taxi-way lane simply provides greater capacity and operational flexibility than AIAL's single taxi-lane design. This investment in the airfield provides ongoing flexibility for the use of the DTB, and subsequently for Pier 2 in the future.</p>
<p><b>Current development not included in Arup alternatives</b></p>	
<p>The Arup proposal does not consider the progress that has been made on the delivery of the first packages of works for the Terminal Integration Programme. In particular, the East Terminal Enabling project is well underway, as is shown in the photo below, with baggage systems now in operation.</p>	<p>Forecast pricing for the DJT remains significantly higher than previously indicated by AIAL and a stated concern for Air NZ. This highlights AIAL's behaviour of leveraging earlier works to justify future projects having ignored the assurances given and the concerns raised.</p>
<p><b>Figure 9: Construction of East Terminal Enabling project, July 2024</b></p>	
<p>Auckland Airport consulted with airlines ahead of making commitments in the 2023 financial year on the early packages of works for the Terminal Integration Programme, including the East Terminal Enabling project. Auckland Airport proceeded with these projects, with explicit support from one Substantial Customer to commit to \$470 million of works under the Terminal Integration Programme for the 2023 financial year. This support to proceed with these capital commitments was provided in August 2022,</p>	<p>Air NZ previously provided 'conditional support' for the Eastern Hall enabling work in August 2022 on the basis it would support on time delivery of the baggage hall and the planned Air NZ international lounge expansion, subject to assurances that solutions would be designed to meet minimum requirements needed and avoid or minimise "regret spend".</p> <p>Forecast pricing for the DJT remain significantly higher than previously indicated by AIAL and a stated concern for Air NZ. This highlights AIAL's behaviour of</p>



	following which Auckland Airport has proceeded to deliver these projects.	leveraging earlier works to justify future projects having ignored the assurances given and the concerns raised.
	By not reflecting these committed projects in its design, the Arup proposal simply ignores the cost of these projects, the services that can be provided with these facilities, and the operational interface with the alternative proposals it has developed. Auckland Airport considers that this further reduces the usefulness and relevance of these alternatives.	See point immediately above re: Forecast pricing for the DJT remaining significantly higher than indicated.
	<i>Ensuring the Domestic Jet Terminal was appropriately sized</i>	
	Through its design process, Auckland Airport took many steps to ensure the new terminal was designed to appropriate specifications.	See next comments below:
	<ul style="list-style-type: none"> <li>gate lounge areas are higher than expected because it appears it is assumed there are more passengers at the gate (i.e. an early call to gate model has been adopted);</li> </ul>	The Programme of Requirements (PoR) assumes a standard call-to-gate model whereas AIAL has assumed both a late call-to-gate model (large retail and dwell area in the processor) and a standard call-to-gate model (gate lounges plus casual seating in the pier) - so essentially a double-up in area provision.
	<ul style="list-style-type: none"> <li>airside retail maybe over-provisioned – but it does align with peer airport benchmarks, kitchen and food dwell spaces have not been included in the retail provision; and</li> </ul>	Airside retail in DJT aligns with benchmarks with major terminals serving <u>International</u> destinations which therefore have higher passenger numbers and dwell times.
	<ul style="list-style-type: none"> <li>the pier design appears to be wider than necessary (Perth T1 is cited as a case study). Auckland Airport sets out our response to these claims below.</li> </ul>	AIAL cite pier width for DJT benchmarks with pier widths for terminals serving <u>International</u> destinations which require more space than required by domestic passengers.
	<i>Brownfield constraints for integrated terminal design</i>	
	The DJT has been designed based on the Paheko East Terminal Integration Pathway, that was endorsed Air New Zealand and BARNZ in 2021. This design concept, for integration with the existing international terminal, introduces a number of brownfield factors that have influenced the design of the facility, including its size. These include:	See next comments below:
	<ul style="list-style-type: none"> <li>terminal integration dictates the departing passenger journey from west to east - this influences the passenger circulation space that is required, due to:</li> </ul>	Noted for circulation space only. Provision for passengers could be a simple connecting link between International and Domestic terminals.

<ul style="list-style-type: none"> <li>- common security screening point – the integrated design has contemplated security screening for domestic passengers will be located next to the existing international screening point (with potential for harmonised screening in the future);</li> </ul>	Noted and not the biggest concern raised in the assessment of DJT.
<ul style="list-style-type: none"> <li>- master planned pier alignment – the Auckland Airport Master Plan sets out the location of future piers to ensure long-run capacity can be delivered, and existing international operations on Pier A are not impacted – this dictates the location of Pier A1 in the east;</li> </ul>	The Master Plan is 10 years old and has not been refreshed. Note the pier alignment has changed since the Master Plan was produced and could change again to reflect an improved airfield operation - hence the pier in the ADT proposal.
<ul style="list-style-type: none"> <li>- baggage system influences headhouse floorplate – the combined international and domestic baggage system has been designed to deliver the required capacity on the ground floor of the facility, this has been a key influence of the size of the floorplate on the ground floor.</li> </ul>	Yes, at ground level, however, this does not require a multi-level structure with retail and F&B as proposed.
While these brownfield factors have influenced the design, the size of the terminal remains appropriate as has been demonstrated by the terminal layouts benchmarking by Arup for Air New Zealand (presented above), and the IATA level of service guidelines that have been incorporated into the design.	AIAL has incorrectly interpreted the IATA guidelines and benchmarking commentary which is referred to previously through ‘global benchmarking’ points above.
These brownfield factors are a reason why the PoR approach to determining terminal size can be problematic. Such an approach to determining the size requirements is based on mathematics but does not take into account the physical brownfield constraints and other factors that need to be considered when designing an airport terminal.	PoR sets the minimum requirements, in particular for aeronautical processes. Brownfield may mean a larger build but does not justify building excessively and at the cost of substantial airline customers. It is entirely possible to have the bag hall extension at ground level and simple link for passengers between the two terminals above this.
Further, under the Auckland Airport Master Plan, the terminal headhouse will ultimately provide processing capacity for future domestic pier A2.	As will the ADT whilst making use of the existing DTB and at a lower level of utilisation so as to reduce the stress on that asset.
Pier and gate lounges	
Auckland Airport considers that the new domestic pier has been appropriately sized, comparable to piers at other airports, with its design informed based on in depth engagement with airlines.	Air New Zealand (and other substantial customers) disagree on both the sizing of the new domestic pier and the statement that “in depth” engagement with Air NZ was undertaken, when critical consultation on items such as LoS and the business case for airlines was insufficient.

	<p><b>Pier benchmarks</b></p>	
	<p>Air New Zealand and Arup have submitted that the design of the pier at 33 metres appears to be too wide, citing benchmarks of other airports. Auckland Airport also sought advice on benchmarks for pier width during 2019, which included the following mix of domestic and international piers:</p>	<p>Most of these piers are International. MEL T1 is from 1970 i.e. pre-IATA guidance. AIAL have failed to mention MEL T4 Domestic which opened in 2015 and is a comparable pier. As key comparator, AIAL shows that the International pier at Auckland is 36m, only 3m wider than this new Domestic pier. This shows that the Domestic pier has been over-sized to serve <u>International</u> routes.</p>
	<p><b>Table 2: Pier width benchmarks</b></p>	
	<p>The above benchmarks indicate that there is no standardised pier width across global comparators, but that the pier design of 33 metres appears to be reasonable and in the mid-range of these benchmarks.</p>	<p>Same point as made immediately above re: utilisation of international piers as benchmarks.</p>
	<p>Further to this, benchmarking of pier width undertaken by Airbiz was provided to Air New Zealand in December 2023 in response to the Adjacent Domestic Terminal proposal. These benchmarks do not appear to have been incorporated into Air New Zealand's submissions to this process.</p>	<p>This benchmarking shows the DJT pier is the widest except for MEL T1 which opened in 1970 i.e. before IATA guidance and therefore supports Air NZ's position that this domestic pier is oversized.</p>
	<p><b>Provision of services in ground floor of the pier</b></p>	
	<p>In designing the pier, the services provided on the ground floor are also an important consideration. The ground floor of the pier includes a bussing lounge to enable the bussing of passengers to remote aircraft, plant rooms, and operational facilities for airline and ground handlers' staff, these facilities also influence the floorplate of the facility. As Auckland Airport has engaged with airlines and ground handlers on the provision of these operational facilities, this has identified requirements for additional space in close proximity to the apron, resulting in an additional mezzanine area to fulfil these requirements.</p>	<p>The AIAL design includes provision for a [REDACTED] bus gate lounge which can accommodate passengers from 3 x A321s at remote gates at the same time, which in practice is unlikely to happen. This is a significant facility and not necessary given the DTB could also provide contact stands.</p>

	<b>Gate lounge provision</b>	
	Gate lounges have been designed within the footprint of the pier and reflect the provision of seating. Informed by airline feedback, the provision of gate lounge provision area has been designed for 50% occupancy.	Boarding facilities have not been included in AIAL's gate lounge area estimates, understating the total provision and there are multiple additional areas of "casual seating" that have been provided but not declared.
	As noted by the Commission, the gate lounge provision is below the IATA level of service benchmarks at 1.1m <sup>2</sup> per passenger (compared to 1.5-1.7m <sup>2</sup> per passenger).	Same point as immediately above. The total provision is approximately 2.7m <sup>2</sup> per passenger.
	<b>Perth Terminal 1 as a case study</b>	
	Perth Terminal 1 is cited as a case study by Air New Zealand. Auckland Airport does not consider Perth Terminal 1 provides a useful comparison, as this facility provides a service for materially lower passenger numbers.	Perth T1 is a reasonable comparator. Pier sizing is not based on busy hour numbers. It is based on the number of gates and size of aircraft which dictates the gate lounge provision for those gates. AIAL's comparisons of actual Auckland and Perth domestic traffic in FY18 is not particularly relevant – the Perth example has a <u>total capacity</u> similar to that of the DJT, which makes it a relevant comparator from a design perspective.
	Previous analysis by Auckland Airport has found that in FY18, while there were 6.6 million domestic jet passengers flying through Auckland Airport, there were 2.5 million passengers using Perth Terminal 1. On a busy hour basis, Auckland's domestic jet busy hour was 61% higher than Perth Terminal 1.	AIAL's comments only further illustrate the value of Perth's pier – for ~AU\$400m, Perth airport constructed a domestic pier that would accommodate decades of growth before reaching capacity. AIAL is spending multiples of this to produce a replacement terminal that its own forecasts indicate would be nearing capacity within a few years of the time of its opening.
	Given the much higher volumes of passengers that are forecast to use the DJT, any comparison with Perth Terminal 1 should be treated with caution.	
	<b>Retail provision</b>	
	Auckland Airport notes that the Arup study identifies that the retail provision is in-line with global benchmarks. Importantly, airlines are not charged for the cost of providing retail facilities, as these costs are allocated based on usage, with retail costs excluded for airline aeronautical charges.	The Arup study identifies retail provision as being in-line with benchmarks for terminals serving International routes with longer passenger dwells. As per response on benchmarking above, this is an over provision for a domestic terminal.
	Auckland Airport is yet to set its allocation rules for the DJT. To inform consultation, Auckland Airport provided a set of rules to allocate costs of the terminal development which were estimated based on an earlier iteration of design. These allocations were indicative and no decisions on allocation rules for the DJT have	While, technically, PSE5 remains 'subject to consultation', it is reasonable to expect AIAL's internal business case and ROI for the terminal to be heavily reliant on these allocation rules and assumptions as they stand today. Therefore, Air NZ would suggest these 'estimations' provide a very strong indicator of AIAL's future allocation intentions. Air NZ would also point to AIAL's responses to airlines'

	been made. Auckland Airport will consult again with airlines ahead of setting PSE5 prices before determining the allocation rules to be used for PSE5.	objections on terminal cost during the PSE4 consultation, and consider as things stand today that AIAL would follow a similar approach in PSE5 for cost allocation.
	<b>Security screening</b>	
	Space provision for security screening has been informed by Avsec screening requirements, the space provision required for screening equipment, and peak hour departing passenger volumes. See page 33 of Auckland Airport's analysis of the Arup Terminal Options presentation for further detail.	Security is an important passenger process. The analysis merely identifies that this is larger than might be expected but recognises the east-west and brownfield nature of the terminal geometry.
	<b>Baggage system</b>	
	Auckland Airport has found that the design of the integrated terminal, including the decision to integrate domestic and international services into a single baggage system, creates efficiencies and reduces the overall floorplate required relative to two stand-alone baggage systems required under the alternatives presented by Air New Zealand and Arup. It is not clear from the materials available, the basis for its conclusion that this integration is driving higher cost.	In comparison to the simple baggage system required for a pure Domestic operation (such as the DTB), the integrated baggage system is complex and will add cost on top of what is required for just a Domestic operation.
	<b>Capital plan review considered headhouse floorplate reductions</b>	
	As part of the capital plan review undertaken in late 2022, Auckland Airport identified seven separate opportunities to reduce floorplate in terminal head house or pier of the new DJT. Aside from one proposal to reduce the amount of plant included in the design (which was adopted), the remaining initiatives to reduce the floorplate in the design were not supported by airlines during consultation.	Actual proposed reduction by AIAL was ~\$70m and, while important, did not have a significant impact on the proposed \$2.2bn build.

<p>Generally, feedback received on these changes during consultation continued to raise concern over the overall cost of the programme, but without providing any viable alternative solutions. Specific feedback indicated that the impact of the reductions in floor plate outweighed the cost savings that could be realised from the reductions. Auckland Airport concurred with this conclusion, and aside from the changes to the provision of plant, the floor area of the headhouse and pier was carried forward.</p>	<p>Air New Zealand has proposed the ADT as a viable solution with continued use of the west side of the DTB for Code C jets (as an alternative to remote stands), albeit less intensively than current operations given known capacity constraints.</p> <p>AIAL has failed to meaningfully entertain alternative options that seek to reduce the scale and cost of the proposed build.</p>
<p><b>Service quality in-line with consumer demand</b></p>	
<p>In considering whether Auckland Airport's investment plans will meet service quality that consumers demand, the Commission has considered future capacity needs and service levels.</p>	<p>See next comments below:</p>
<p><b>Capacity needs</b></p>	
<p>The Commission noted in the draft report:</p>	<p>See next comments below:</p>
<p>Airlines broadly agree that there are capacity issues with the existing DTB as well. We consider that in general, additional capacity enables new airlines to enter markets and promotes competition, which benefits consumers.</p>	<p>In principle, yes.</p>
<p>We are supportive of the Commission's conclusion on capacity needs. The DJT will address existing capacity constraints in the existing Domestic Terminal Building, by providing 26% additional capacity gate capacity, plus a further 10% capacity through bus lounges and 44% additional check-in capacity. This is critical, as Auckland Airport expects that if no further capacity investment is made, by 2026 the number of days over capacity would increase to 58 days per year, and by 2033 it would be near continuous at 296 days per year. The new Pier A1 is designed with flexibility in mind: all gates are A321 capable and, thanks to the Multi-Aircraft Ramp System ("MARS") larger code E aircraft such as B787 can be parked as required.</p>	<p>We are unable to reconcile the 26% capacity figure, however the base on which this increase occurs is important: \$2.2bn (\$3.9bn if including enabling works) for just <u>two</u> additional contact stands is not considered efficient or appropriate.</p> <p>AIAL's reference to improved (and unproven) check-in capacity sits outside of this PSE in another project and would therefore attract additional costs over \$2.2bn. Air NZ considers these stated capacity benefits misleading and would recommend AIAL provide Substantial Customers and the Commission with the appropriate detail to interrogate how they are arrived at.</p>

	<p>These capacity uplifts are provided whilst replacing the existing domestic jet capacity at the Domestic Terminal Building – capacity which will be lost when contingent runway operations are required to allow for renewals on the main runway.</p>	<p>The three domestic jet stands on the west side of the DTB are not impacted by Contingent Runway and could still be used, while the remainder of the DTB could still be used by Regional turboprop services with Contingent Runway. The DTB does not need to be prematurely demolished as proposed.</p>
	<p>As a replacement facility this also enables a pathway to long-run capacity growth indicated in demand forecasts, the existing Domestic Terminal Building acts as a hard constraint on this long-run capacity expansion pathway.</p>	
<p><u>Service levels</u></p>		
	<p>The Commission's draft conclusion on service levels is as follows:</p>	<p>See next comments below:</p>
	<p>Overall, our draft conclusion is that the service levels that Auckland Airport is targeting for the design of the new domestic terminal do not appear to be excessive, in comparison to the IATA Optimum Level of Service standards or the average peer airports.</p>	<p>Air NZ disagrees and so does IATA. A specific and appropriate LoS within the optimum range was not agreed with airlines in advance. DJT includes more than just key processes required by the IATA standards but also includes significant additional retail, dwell, gate lounge and back-of-house space which inflates its size and is not appropriate or necessary in a NZ domestic context.</p>
	<p>We welcome this conclusion. We have set out further detail above, in previous submissions, and in our regulatory disclosures on how we have used the IATA level of service guidelines to inform the design of the DJT.</p>	<p>Noting this is a draft conclusion and one which Air NZ has challenged for the reasons described above and in its evidence to the Commerce Commission.</p>
	<p>These investment plans are intended to help address service quality concerns raised by consumers. A study undertaken earlier this year confirmed that Auckland Airport's investment is supported by consumers, including:</p>	<p>See next comments below:</p>
	<ul style="list-style-type: none"> <li>· 76% of travellers want development at Auckland Airport</li> </ul>	<p>Air NZ has consistently supported appropriately sized and staged development.</p>
	<ul style="list-style-type: none"> <li>· 81% want airport investment that futureproofs against weather events</li> </ul>	<p>As immediately above.</p>
	<ul style="list-style-type: none"> <li>· 90% of travellers supported building more airline capacity to keep fares in check.</li> </ul>	<p>Note that the proposed DJT will come at a higher cost than is either necessary or efficient. That cost will be passed onto NZ consumers through airfares so the DJT is not the right answer to meet the needs of the 90% of travellers seeking capacity increases to keep fares in check.</p>

	<b>Capital cost estimates</b>	
	We note the Commission's draft conclusion on capital cost forecasts:	See next comments below:
	We welcome the Commission's draft finding on the robustness of our capital expenditure forecasts. Significant effort, analysis and rigour is applied to ensure that our cost estimates are accurate and robust. We appreciate that the Commission has recognised this in its draft report.	Air NZ's position continues to be that the DJT is oversized and therefore the cost is too high.  WT costed DJT at \$2.2bn with escalation – which is consistent with Air NZ's position.
	<b>Investment timing</b>	
	We welcome the Commission's draft conclusion on investment timing:	See next comments below:
	Our draft conclusion is that there appear to be operational and financial reasons for Auckland Airport to proceed with the TIP now. The enablement of an efficient contingent runway operation would not only benefit the main runway pavement renewals, but also improve the resilience of the runway operations in general. If the investment is deferred because the cost to build and associated increases in airport charges are considered too high, postponing the same investment into the future is unlikely to address this concern.	The three domestic jet stands on the west side of the DTB are not impacted by Contingent Runway and could still be used, while the remainder of the DTB could still be used by Regional turboprop services with Contingent Runway. The DTB does not need to be prematurely demolished as proposed.
	Auckland Airport therefore agrees with the Commission's draft finding that there are operational and financial reasons for Auckland Airport to proceed with the DJT now. The contingent runway is an important resilience project and therefore a relevant key driver of the timing of the DJT – the need to realign taxiway Bravo to enable efficient contingent runway operations has also been recognised by Arup in its analysis.	Air NZ has shown that that contingent runway works can be independent of the DJT and options relating to this have not been fully considered.  This continues to demonstrate AIAL's approach of building without agreement from Substantial Customers.
68	We also concur with the Commission on the financial impacts of delay - while construction costs can be volatile, they rarely fall, but rather just increase at a slower rate. Further delay to the delivery of this essential infrastructure is only expected to make it more expensive to build.	Proceeding with a more expensive option will still result in higher spend than pausing temporarily and developing a cheaper terminal proposition in line with the airline community's requirements, including continued use of the existing DTB. There is no reason to believe that a smaller and less complex option could not enable earlier delivery of stand capacity than is currently forecast for the DJT.
	<b>Investment delivery</b>	





	<p>We note the Commission’s draft conclusions on delivery of investment at Auckland Airport:</p>	<p>See next comments below:</p>
	<p>When viewing PSE2, PSE3 and the beginning of PSE4, Auckland Airport has largely delivered on its investment goals, except for the beginning of PSE3 which followed a period of over-spend relative to its forecast, delivering additional capacity demanded by market growth. The significant under-investment over the COVID affected period in PSE3 ought to be treated as an outlier and not reflective of regular practice. Overall, we do not have significant concerns over planned over and under-investment historically; under-delivery risk in PSE4 is also mitigated by the one-way capex delivery wash-up introduced by Auckland Airport.</p>	<p>Air NZ disagrees - in FY19 (mid PSE3) AIAL were behind forecast capital spend (50% - the capital spend was \$330m out of \$760m).</p> <p>Air NZ refers to its previous submission regarding the significant underspend required before the capex-delivery wash up would be triggered.</p>