

7 December 2012

Regulation Branch
Commerce Commission
P O Box 2351
Wellington 6140

Attention: Ruth Nicholls Ruth.Nichols@comcom.govt.nz

Dear Ruth

Review of Wellington International Airport Limited (WIAL) Land Valuation Methodology

We refer to your email of 26 November 2012 which advised that the Commerce Commission ("Commission") had engaged Darroch Limited ("Darroch") to undertake a review of WIAL's Market Value Alternative Use ("MVAU") land valuations prepared as at 31 March 2009 and 31 March 2011. In this email you advised that you were seeking comment from WIAL on the draft Darroch reports by 7 December 2012.

Compliance with Input Methodologies

For the Commission's information, we have set out below the process that WIAL undertook in preparing the land valuations.

WIAL instructed the valuers Telfer Young ("TY") to prepare a valuation of WIAL's land holding in accordance with Schedule A of the Commerce Act (Specified Airport Services Input Methodologies) Determination 2010. TY in turn commissioned urban planners Boffa Miskell ("BM") to develop a master plan identifying potential land use options.

TY and BM undertook an extensive process to determine the highest and best alternative use in accordance with the Commission's input methodologies ("IMs"). TY confirmed to WIAL in its valuation reports that the valuations provided were compliant and WIAL considered this and relied upon the expert advice from TY and BM.

WIAL also notes that this valuation process included extensive consultation with its substantial airline customers and the Board of Airline Representatives of New Zealand Inc ("BARNZ"). The extent of this consultation is set out below for the Commission's reference and highlights not only consideration of the feedback received but a reduction in the final MVAU valuation recommended by TY.

In short, WIAL adopted a professional and robust approach to its land valuation with advice from relevant expert advisors. As a consequence, WIAL is concerned to read the reports by Darroch that whilst they consider that the valuations are in general compliant with the IMs, there are a number of areas of non-compliance.

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WIAL notes that the comments regarding non-compliance made by Darroch appear to represent either a difference in valuer judgement and/or refer to insufficient information being available. WIAL has provided the Darroch reports to TY for their review and comment. A copy of the response from TY is attached to this letter.

WIAL also notes that a couple of the Darroch comments relate to potential land use and zoning. In this context TY worked with BM as expert town planners and formulated potential land use options. For Darroch's reference we have also attached copies of documents previously prepared by TY and BM for consultation purposes which should address the comments that they have made.

TY have reconfirmed in its advice to WIAL that they consider that the valuations have been prepared in accordance with the IMs and have provided additional comments to the matters raised in the Darroch reports.

Consultation under the Airport Authorities Act 1966

WIAL relied upon TY's advice in establishing the valuations. However, due to the consultation requirements in the Airport Authorities Act 1966 ("AAA") the valuations were subject to extensive review during the pricing consultation, to establish prices for the period commencing 1 April 2012. This included considerable exchanges of views between TY, BM and the airline valuation advisers during the consultation. Changes were made to the valuations in response to the feedback received from the airline advisers.

For the Commission's information we detail the engagements that occurred during the consultation as well as the changes that were made to the valuation below:

Date	Communication	Comment
7 June 2011	Preliminary 2011 MVAU and Market Value Existing Use ("MVEU") land valuations prepared by TY dated 31 May 2011, together with land Master Plan Report prepared by BM, provided to substantial customers	Initial draft MVAU valuation prepared for airline comment and feedback <u>MVAU recommended by TY = \$166 million</u>
21 June 2011	Meeting attended by WIAL, TY, BARNZ and airline valuation advisers Property Advisory Limited ("PAL") to discuss the draft valuation	
30 June 2011	Meeting attended by WIAL, TY, BM and airline valuation advisers PAL and Zomac to discuss the draft land use plans and valuations	
5 July 2011	WIAL met with its substantial customers to present the asset valuation paper, dated 7 June 2011, and draft valuation reports. TY and BM were in attendance.	
14 July 2011	BARNZ provided a response to the draft land valuations accompanied by reports from Zomac and PAL	The BARNZ advisers queried a number of aspects of the land valuation with Zomac addressing issues concerning land use and PAL addressing the valuation calculations



17 August 2011	WIAL provided updated valuations to the substantial customers including: <ul style="list-style-type: none"> • A report from BM dated 1 August 2011 commenting on issues raised by the airline advisers • A revised BM Master Plan report dated August 2011 • A report from TY dated 12 August 2011 commenting on issues raised by the airline advisers • Updated MVAU and MVEU valuations prepared by TY dated 12 August 2011 	<u>MVAU recommended by TY = \$153 million</u> Land use plan amended to: <ul style="list-style-type: none"> • Reduce provision for business park by approximately one third • Increase allowance for residential and roading to compensate
18 August 2011	WIAL's Initial Pricing Proposal provided to substantial customers	Illustrated the pricing asset base from application of the 12 August 2011 valuation reports
10 & 14 October 2011	Substantial customer responses to WIAL Initial Pricing Proposal including further valuation report from PAL Air NZ submitted that 2002 asset base should be rolled forward.	PAL continued to provide alternative land valuation. Development costs for MVAU land scenario provided by Rider Levitt Bucknell.
22 November 2011	WIAL's Revised Pricing Proposal provided to substantial customers	Also included: <ul style="list-style-type: none"> • Further report from BM with supporting plans dated 14 November 2011 responding to BARNZ comments • Further report from TY dated 15 November 2011 responding to PAL comments • Report from Opus addressing Rider Levitt Bucknell comments. Opus substantially increased development cost recommendation. • Updated TY MVAU valuation report. <u>MVAU recommended by TY = \$141 million</u>
6 December 2011	WIAL met with its substantial customers to discuss the key consultation issues, including land valuation	
23 December 2011	Substantial customer responses to WIAL Revised Pricing Proposal including PAL response to TY report (included with Revised Pricing Proposal)	Airline adviser's views unchanged from initial 14 July 2011 advice.
1 March 2012	WIAL's Final Pricing Document provided to substantial customers and prices established for period commencing 1 April 2012	<u>MVAU recommended by TY = \$141 million</u>

The extent of the exchange of views between WIAL, its substantial customers and their respective advisers is evident from this chronology. Furthermore, WIAL published all of the key consultation documents on its website providing complete transparency of the information exchanges and in particular the in depth consideration given by WIAL's advisers to the feedback received.



WIAL recognises that the land valuation is a critical input to its pricing calculations and as such made considerable efforts to ensure that the valuation adopted was robust. In particular, WIAL:

- Engaged high quality valuation advisers in TY and BM to provide valuation advice;
- Ensured that airline adviser feedback was considered in depth by TY and BM;
- Facilitated direct discussions between WIAL’s advisors and the airline’s advisers;
- Published the consultation documentation to ensure full transparency of the exchanges of views.

It is also evident that WIAL’s advisers responded to the feedback received with the initial land use plan recommended by BM being altered and the MVAU land valuation being reduced by \$25 million, or 15%, from the initial value proposed by TY. By contrast the airline advisers did not alter their views at all from their preliminary advice.

WIAL recognises that the MVAU valuation is a hypothetical valuation that requires considerable professional judgment to be exercised by the valuation advisers. However, as demonstrated above, WIAL considers that it undertook a professional, extensive, and robust process to achieve a MVAU valuation that complied with the IM requirements.

Reconciliation of Land Areas

We refer to Darroch’s comment in paragraph 3.16.6 of their report reviewing the 2011 valuation that *“As it is not possible to determine just which land parcels or location of the parcels make up the 86.3 Ha relative to the total 103.2 Ha valued then I cannot provide any definitive answer.”*

WIAL has previously provided a breakdown of the land areas included in the valuation to the Commission and also the composition of the land value included in the Regulatory Asset Base per WIAL’s 2011 annual information disclosures.

This information was provided in WIAL’s response to the Commission’s queries dated 15 August 2012. We have extracted the relevant tables from this response for Darroch’s reference below:

Land Included in TY Land Valuation

	Hectares	Value \$000
Land in Telfer Young 31 March 2011 MVAU Valuation	103.2	141,000
Other land already valued at alternative use	6.5	31,200
Moa Point Road land not included in valuation	1.9	0
Total WIAL Land Holding	111.6	172,200



Breakdown of 31 March 2011 Physical Land Area

	Hectares TY Valuation	Hectares already at AU	Total Hectares
LAND IN RAB			
Airfield	76,5	1.2	77.7
Aircraft and freight	3.0		3.0
Terminal direct land	0.1		0.1
Terminal common land	1.5		1.5
Other shared land	4.0		4.0
Total MVAU Specified Airport Services	85.1	1.2	86.3
LAND NOT INCLUDED IN RAB			
Future Use Assets ¹		2.4	2.4
Land for unregulated services	18.1	2.9	21.0
Land not included in valuation		1.9	1.9
Total WIAL Land Area	103.2	8.4	111.6

Composition of 31 March 2011 Regulated Asset Base Land Value

	Unallocated RAB \$000	Share of Common Land	Allocated RAB \$000
Airfield	104,491		104,491
Aircraft and freight	4,124		4,124
Terminal direct land	86		86
Terminal common land	2,071	75.0%	1,554
Other shared land	5,430	73.6%	3,995
Total TY MVAU Valuation¹	116,202		114,250
Add land already valued at AU ²	5,025		5,025
Total RAB Land Value	121,227		119,275

Note 1: All MVAU land is valued at \$136.57 per square metre. Note the rounding of the land areas to 0.1 of a hectare produces variable rates if the calculations are performed directly from the tables above. For example the actual terminal direct land area is 0.0629 hectares which has been rounded to 0.1.

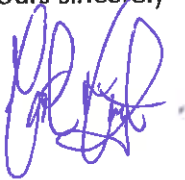
Note 2: This land is for the Bridge St residential properties which are valued at rateable value. These properties are included in aeronautical due to their proximity to the runway. WIAL is in the process of requesting the tenants to relocate to enable demolition of the houses on these properties as part of WIAL's noise management obligations. BARNZ agreed with the inclusion of this land in the asset base for charging purposes in the price setting event.

These tables should provide the necessary information for Darroch to understand the composition of the 2011 valuation. The allocation of land to particular services, for example airfield, is undertaken on a detailed basis which considers the use for discrete areas of land. This was presented to airlines in consultation with a plan provided as part of the Second Information Pack on 23 May 2011. A copy of this plan is attached.



We trust that this letter assists the Commission further in its review of WIAL but would be happy to provide any further explanation of this information should this be required.

Yours sincerely



Martin Harrington
Chief Financial Officer

Attachments:

1. Review of Land Valuation Methodology – Darroch Limited Land Valuations 2009 and 2011 report prepared by Telfer Young dated 7 December 2012
2. Copies of WIAL consultation documentation under the AAA:
 - BM memorandum dated 1 August 2011
 - Revised BM Master Plan report dated August 2011
 - TY letter dated 12 August 2011
 - BM memorandum (including supporting plans) dated 14 November 2011
 - TY letters dated 15 November 2011
3. WIAL Airport Plan 23 May 2011

