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Dear Ruth

CIAL SUBMISSION ON PROCESS UPDATE – SECTION 56G REPORTS

1 This is Christchurch International Airport Limited's (*CIAL*) submission on the Commerce Commission's consultation document "Airport Services – s 56G Reports: Process Update and Opportunity to Submit on the Review of Auckland International Airport" (6 September 2012).

2 While CIAL does not have any specific comments on AIAL's disclosures, CIAL believes that there are still some framework issues relating to the s 56G reports that need to be resolved. Accordingly, we focus on those issues in this submission.

Review requires assessment of specific incentives and actual market outcomes

3 CIAL agrees with Air New Zealand that "answering the question at the heart of the Commission's s 56G review requires an assessment of both specific incentives faced by regulated suppliers and actual market outcomes".[1]

4 CIAL has maintained throughout this process that an assessment of the effectiveness of information disclosure in promoting the Part 4 Purpose requires not only an assessment of airport performance and behaviour, but also an assessment of whether the information disclosure regime is producing the correct incentives such that airports are influenced to perform and behave consistently with the Part 4 Purpose.

5 CIAL has also highlighted that it is outcomes – in terms of actual performance and behaviour – that is more relevant to the s 56G assessment than the inputs into pricing decisions (although CIAL has acknowledged that inputs remain relevant to the extent that they influence outcomes).

"No manifest intention on the part of Parliament to avoid de facto price control"?

6 Air New Zealand claims that there is "no manifest intention on the part of Parliament to avoid de facto price control".[2] This statement is broadly reflective of the position the airlines have taken throughout this process – that is, the airlines tend to believe

[1] Air New Zealand *Post-Conference Cross-Submission to the Commerce Commission* (17 August 2012), para 16.

[2] Air New Zealand *Post-Conference Cross-Submission to the Commerce Commission* (17 August 2012), para 17.

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that pricing outcomes ought to be wholly dictated by the terms of the information disclosure regime.

7 CIAL has a more balanced view than this, and one which does not undermine the legislation. We know that information disclosure is intended to promote and reinforce conduct that is consistent with the Part 4 Purpose. It does so primarily by making transparent the performance of airports, which combined with the threat of heavier handed regulation, the possibility of adverse publicity, and pressure from customers armed with information, such transparency creates incentives for airports to behave consistently with the Part 4 Purpose.

8 To suggest that Parliament didn't seek to establish a concrete distinction between information disclosure and price control shows a fundamental misunderstanding of information disclosure regulation and its intended impact.

Conclusions will need to be appropriately contextualised

9 Air New Zealand suggests that if the Commerce Commission shies away from making firm conclusions it will be failing to discharge is statutory function.[3]

10 The Commission's statutory function is to report to the Ministers of Commerce and Transport as to how effectively information disclosure is promoting the Part 4 Purpose. CIAL is not suggesting the Commission withholds its view as to how effectively information disclosure is promoting the Part 4 Purpose.

11 What we are saying, however, is that the Commission's view needs to be appropriately contextualised. Because this review comes so early in the life of information disclosure, the Commission needs to acknowledge that the regime has not fully expressed itself and therefore its full effect will not be known for some time. If, for example, views were drawn from airport pricing decisions, appropriate contextualisation would include noting that outcomes from those decisions are contingent on some factors which are largely out of the control of airports.

Role of IMs

12 The airlines continue to misconceive the role of IMs, and to distort CIAL's and the other airports' views on this issue. We make the following brief points in reply:

12.1 BARNZ is wrong to suggest that the airports don't believe the IMs to be relevant to the question whether information disclosure is effective.[4] In fact, CIAL explicitly stated in its submission following the WIAL conference that the IMs are relevant to the review.[5] CIAL acknowledges that the proper role of the IMs is a difficult issue and for this reason we constructively sought to outline a role for the IMs which would assist the Commission, rather than retreating into self-serving statements about how the IMs should be employed.

12.2 CIAL is not aware of anywhere in the Commerce Act or in the information disclosure regime which supports the idea that IMs should be adopted in pricing

[3] Air New Zealand *Post-Conference Cross-Submission to the Commerce Commission* (17 August 2012), para 18.

[4] BARNZ *Post-Conference Submission on Wellington Airport Section 56G Review* (17 August 2012), p. 4.

[5] CIAL *Cross Submission Following Wellington Airport Conference* (17 August 2012), para 9.

unless there are "compelling justifications" to the contrary.[6] The IMs represent the Commission's view as to the most appropriate way to calculate some of the costs of service for airports under Part 4 and, accordingly, CIAL has given serious consideration to the IMs throughout its current pricing consultation. However, making categorical rules for the application of IMs such as the airlines are attempting to do is not helpful, and disregards the flexibility that information disclosure is intended to preserve and is required in the setting of prices. The focus must always be on whether outcomes are consistent with the long-term benefit of consumers.

12.3 Air New Zealand suggests that the IMs should be the "primary basis for assessing whether ID is effectively promoting the purpose of part 4", and the "natural and primary point of reference".[7] The airlines appear to be directing the Commission to assess the effectiveness of information disclosure by a crude comparison of pricing inputs against the IMs. CIAL acknowledges that the IMs are a point of reference in the review, but there is clearly more to this review than the overly simplistic assessment advocated for by the airlines. For instance, such an assessment would not capture any opex/capex efficiencies achieved by an airport over time, nor would it consider the longer term consideration taken into the setting of prices for major infrastructure development, such as our new integrated terminal development which sets prices to recover the required return over the life of the asset. This we believe is a key part of any regulatory regime.

Litigation costs

13 In using s 52T to supports its argument that airports should not seek to recover the costs of litigation, Air New Zealand appears to have misunderstood the legislation.

14 Section 52T(c)(i) covers the regulatory processes and rules IM which is only applicable to DPP/CPP and individual price-quality regulation. The section precludes the IM from treating the costs of merits review appeals as a "pass-through cost" (a technical term defined as a cost that is not within the control of the supplier). This rule does not express a philosophy that suppliers ought not to recover the reasonable costs of a merits review challenge. It merely provides that such costs are not a pass-through cost for the purpose of price control regulation, probably because those costs should be subject to the pressure for efficiencies that treating them as opex provides.

Yours Faithfully

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[6] Air New Zealand *Post-Conference Cross-Submission to the Commerce Commission* (17 August 2012), para 48.

[7] Air New Zealand *Post-Conference Cross-Submission to the Commerce Commission* (17 August 2012), paras 40 and 45.