

15 February 2019

Submission from NZ Airports on the Issues Paper - NZ Productivity Commission's Inquiry into Local Government Funding and Financing

Thank you for the opportunity to comment on your Issues Paper. NZ Airports' comments in this submission respond to the following points raised in the paper's summary of questions:

- The extent that tourism growth is resulting in funding pressures and what councils are experiencing the greatest pressure (Question 5)
- The scope for local government to manage cost pressures (Question 12)
- The funding and financing options to help councils facing population decline (Question 39)
- The need for new delivery models involving central government and how to make these effective (Question 40)
- Changes to the local government funding framework that would be beneficial (Question 43)
- Changes needed to address financing barriers (Question 46)
- Central government policies that could support private investment in infrastructure and services (Question 48)

Summary of NZ Airports' submission points

1. Small airports in regions distant from the main centres are a stark illustration of why the current local government funding and financing systems are no longer fit-for-purpose.
2. Our national air network - and the connectivity, tourism and cohesion benefits that it brings to the country – is reliant, at the outer edges of the network, on local government funding. That system is cracking under the strain of its multiple responsibilities.
3. Small airports are inherently unable to operate commercially without subsidisation. While some support for these airports already exists, it is too little, patchy and unfair, with no certainty that enables planning and investing for productive or efficient use of established airport infrastructure.
4. Airports are facing planning, environmental, infrastructure and funding challenges to keep up with growing and changing communities and customers. A recent report for Tourism Industry Aotearoa (TIA)¹ found airport infrastructure is a key hurdle to attracting and managing tourism growth in New Zealand regions. Limited flight options make it harder for visitors, particularly domestic and business travellers, to access regions, and make the best co-ordinated use of all

¹ National Tourism Infrastructure Assessment, Tourism Industry Aotearoa, April 2017

our airport assets.

5. Small airports, mostly owned and funded by councils, are the least able to cope with the financial and funding balancing act of meeting their current obligations. The councils seek to keep their airports open for the wellbeing of their communities. However, they also have to respond to increasing pressures for investing and operating other core, more locally-focused, infrastructure needs such as water and wastewater systems.
6. At least 10 of New Zealand's small airports do not fit a commercial model, and depend on ratepayer funding which is increasingly unsustainable. Many of these airports are in sparsely populated districts, at risk of further isolation and disadvantage. Each small airport serves communities in their catchment that are among the most vulnerable and isolated. They need air access to larger centres and their centralised facilities, such as hospitals.
7. The precarious situation of small regional airports illustrates why New Zealand needs a new local government funding system that is fit for the 21st century. We need a system that will protect and maintain core infrastructure that assists with bringing productivity benefits such as national air connectivity, and at the same time can support small and isolated communities – as well as work for growing and pressurised regions.
8. A new policy and funding approach should include a national, cross-government, pan-regional, investment and planning perspective on core strategic local assets that are part of a linked national network, such as airports.
9. Eligibility criteria should be established to ensure fair access to funding from central government to protect and sustain a national air network. We note the support schemes available in other countries, and described in the attachment and other papers referenced in this submission.
10. We believe that it is neither sustainable, nor desirable, to continue with the current system of local government funding for the aviation component of the national transport system, in those locations where the commercial model is untenable. It places an unfair burden on small communities for ensuring a national network standard of air service and connectivity that has productivity, resilience and other benefits for the entire country.

1. NZ Airports: who we are and why local government funding and financing issues matter to our members

- 1.1. NZ Airports is the industry association for New Zealand's airports and related businesses. Our members operate 36 airports across the country including the international gateways to New Zealand. This infrastructure network is essential to a well-functioning economy and society, and enables critical transport and freight links between each region of New Zealand and between New Zealand and the world.
- 1.2. New Zealand's airports are part of our country's core infrastructure, delivering connectivity that our regions need to succeed. Councils define them as 'strategic assets' under the Local Government Act's significance policy requirements. In the Civil Defence and Emergency Act, airports are listed as 'lifeline utilities'.
- 1.3. Communities own and manage their regional airports, sometimes in partnership with Government, but most often through their local councils². The majority of New Zealand's airports are council-controlled organisations, seeking to be self-sustaining businesses returning value to their cities and regions.

2. Local government funding issues that impact critical infrastructure

- 2.1. As your inquiry's terms of reference point out, local authorities are capital-intensive businesses. This is a description also often used about airports.
- 2.2. Expenditure on fixed assets has grown significantly in recent years. Demand for capital expenditure is unabated, or increasing, due to the maintenance and replacement of ageing infrastructure, earthquake-prone buildings, and the requirements of air safety and security. Growth in air travel and changing aircraft fleets is also requiring investment at many locations.
- 2.3. New Zealand's airports are caught up in this growing local government funding challenge, particularly if they service smaller communities. Airports are a prime example of strategic community assets that provide connectivity, cohesion, emergency management and economic and social benefits.
- 2.4. Airports are facing planning, environmental, infrastructure and funding challenges to keep up with growing and changing communities and customers. These are directly related to the various strategic financing and demographic challenges outlined in your issues paper.
- 2.5. These impacts are being felt across the board by airports to varying degrees, depending on size of airport and the community it serves, and nature of its ownership, funding, debt and management structures.

² The main exceptions are Auckland Airport, a listed company, and Wellington Airport, majority owned by an infrastructure investment firm. Milford Sound Airport is fully owned by the government.

- 2.6. This submission focuses on those small airports, in regions away from the main centres, that are most acutely impacted by the current local government funding system. These councils have limited and diminishing options and resources for funding assets that contribute to a nationally connected air network.
- 2.7. The only on-going government support for small airports is the Joint Venture (joint 50:50 Crown and local government ownership) model, currently applied to five New Zealand airports³. This is a model from the 1950's that has served its time. It is overdue for review in light of growing needs for timely investment and development. And while it is a welcome recognition of the national role of airports at the edge of the air transport network, it is arbitrary in applying to only five airports.
- 2.8. While the Provincial Growth Fund is assisting some airports (e.g. Gisborne, Bay of Islands, with others in the pipeline), this is not necessarily the best strategic and sustainable system for funding core national and local strategic assets on an ongoing basis.
- 2.9. A regional business case bidding process should at least be linked to some level of national policy on what level of minimum airport capability and connectivity our communities need – and how investment should be shared in an equitable manner between national and local funding systems. This is the case with State Highways and land transport, through the NZ Transport Agency's financial assistance rates (FARs) system for local government.

3. Small and isolated airports – need an urgent and important policy focus

- 3.1. NZ Airports believes that the current statutory framework, including local government funding and financing of airports, is no longer fit for purpose.
- 3.2. Specifically, the statutory imperative⁴ to operate as a commercial entity cannot reasonably apply to airports whose passenger or flight volumes are too low to generate the necessary revenue.
- 3.3. In our view, is it appropriate for government to allocate dedicated funding to core infrastructure that has national connectivity benefits. That would assist small councils to focus more of their limited resources on other local infrastructural challenges such as water and waste systems. Local airports are not for local trips – like the national highway system, they provide connections between regions and between towns and cities.
- 3.4. We see airports as national strategic assets that together form a network that central government needs to take greater responsibility for at a NZ Inc level, given their clear role in delivering connectivity, and enabling economic

³ Whangarei, Whakatane, Whanganui, Taupo and Westport Airports

⁴ Airport Authorities Act, section 4 (4) "Every airport operated or managed by an airport authority must be operated or managed as a commercial undertaking"

growth, emergency support and resilience.

- 3.5. These are issues that are clearly related to the funding and financing of local government and the issues that you are investigating. They highlight a lack of equality with other forms of transport in the national funding mix. At the same time, we acknowledge that the commercial airport model envisaged in the Airport Authorities Act is working well for the busier domestic and international airports – which in many cases provide a financial return to their owners.
- 3.6. In the NZ Airports' position paper *Linking the long white cloud* (2017), attached to this submission, we put forward a number of possible policy approaches. These relate to a rationale and mechanism by which government could fund a national minimum standard of airport infrastructure, and ensure essential services.
- 3.7. We note that the challenge for small and isolated airports is growing, as large airlines pull out of more of our smaller communities, due to their own commercial imperatives. This leaves councils with less revenue for airport infrastructure, yet at the same time adds funding demands – in addition to the airport itself some councils and development agencies already underwrite air services to ensure essential air connectivity to their towns and regions⁵.

4. Need for national consistency

- 4.1. There is no national air network policy recognising the value of air connectivity, and no national consistency or policy rationale for the limited support to small airports.
- 4.2. The Crown retains half share ownership of five small Joint Venture airports, but similar airports have no government support. At least 10 airports do not fit a commercial model, and depend on ratepayer funding which is increasingly unsustainable. These include Chatham Islands, Hokitika, Kaitaia, Westport, Whangarei, Whakatāne and Whanganui.
- 4.3. It is inequitable to leave small numbers of ratepayers to shoulder this responsibility. Any downgrading of air services will have a further detrimental effect on the ability of these regions to retain existing businesses and jobs, let alone grow and promote tourism, a key economic driver. This will also affect the country's national air connections – aviation is, and will remain for the foreseeable future, New Zealand's only national rapid transit system.
- 4.4. The Auditor General's report to Parliament in 2016⁶ described the situation:
“The revenue that airports generate is critical to their ongoing viability.”

⁵ For example, when Sounds Air introduced Taupo-Wellington flights replacing a withdrawn Air New Zealand service, the council decided to underwrite the first three seats of each flight, and Development West Coast made finance available to Sounds Air to purchase an extra aircraft for flights between Westport and Wellington

⁶ Controller and Auditor-General, *Local Government: Results of the 2014/15 audits*, April 2016

Although this can be said of many small- to medium-sized enterprises, airports form part of New Zealand's national transport network. Airports play a valuable role in New Zealand's connectivity. The failure of an airport can have a negative effect on the economic vitality and connectivity of the community it services.

New Zealand's airports vary greatly in size and passenger volumes, but all have costly and sometimes unavoidable infrastructure requirements. Some of these requirements are not dictated by airport capacity. The smaller airports can struggle to meet these infrastructure needs from limited revenue streams.”

4.5. In Australia, Canada, the USA and Europe, governments fund airport infrastructure and also underwrite essential air links. Australia invests at both the national and state level in regional aviation to ensure social cohesion and connectivity. The Ministry of Transport recently received a report from consultants Market Economics on the economic contribution of regional airports⁷. This report includes a literature review of international support models for airports.

5. The costs of running an airport for small councils and communities

5.1. Airport owners must not only financially cross-subsidise their airports, they also face a complex task in maintaining and operating the assets.

5.2. Staffing a basic airport with no pressing maintenance issues can run to \$250,000 per annum. Much of this cost is associated with staff – ensuring the airport meets all operational and safety regulatory requirements.

5.3. Airports with less than 2000 regular passenger flights each year are also ruled out of Airways NZ's national service levels and pricing structures⁸. They must reach separate agreements (including payment) with Airways, or, more commonly, ensure maintenance of the specialised infrastructure themselves.

6. The impact – less resilience and ability to respond to disasters

6.1. The national contingency plans pulled together in the aftermath of the 2011 Christchurch earthquake assume access to all current airports, airstrips and aerodromes in the event of a future natural disaster.

6.2. Frequent runway maintenance is essential to ensure access for heavier lift aircraft that can be used to move response services and equipment into place rapidly in the event of natural disasters.

6.3. Runway, taxiway and apron maintenance programmes could be defunded by local councils once small and isolated airports lose their regular passenger services. Experience in Australia has shown that those aerodromes not

⁷ Regional Airport – Economic Contribution, ME Consulting, October 2018, for Ministry of Transport

⁸ Airways NZ, a state owned enterprise, is the national provider of air traffic control and air navigation services

receiving federal maintenance grants have fallen into disrepair.

6.4. We note that the government recognised the link between disaster response/recovery and regular air services to smaller towns in its unsuccessful talks with Air New Zealand to resume services to Blenheim following the 2016 Kaikōura earthquake.⁹

7. In conclusion

7.1. Ageing infrastructure and the associated operating and capital costs can be a heavy burden to local governments operating New Zealand's smaller, non-commercial airports.

7.2. Yet councils are obliged to keep airports open for the economic and social wellbeing of their residents, including the frequent air transport of hospital patients and medical specialists to and from small centres.

7.3. Unlike other developed countries, New Zealand has no regional aviation assistance scheme (apart from the historical Joint Venture airports). All airports are mandated to operate as commercial entities. However, small essential airports are inherently unable to operate commercially without subsidisation. The Provincial Growth Fund is not targeted to ongoing maintenance and operation of infrastructure.

7.4. The support that does exist for small and isolated centres is too little, and inequitable between similar airports. The current policy and funding environment does not support productivity or well-being for communities or the country.

Meeting request: NZ Airports would welcome the opportunity to meet with Productivity Commission staff to discuss in detail the issues raised in our submission.

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Attachment: *Linking the long white cloud – a position paper, NZ Airports, July 2017*

⁹ See <https://www.stuff.co.nz/business/86789718/government-will-talk-to-air-new-zealand-about-marlborough-return>