6 Airports

6.1 In this Part, we discuss the public entity airports that we audit. They include airports that local authorities wholly or partly own and airports operated as joint ventures between local authorities and the Crown.

6.2 Some airports fall outside our mandate because private interests own most of their shares.

6.3 Some local authorities own airports that an in-house business unit manages. We do not audit them separately from the local authority and have not included them in this Part.

6.4 Airports, particularly small regional airports, have experienced some challenges lately, with some losing airline services. We decided to take a closer look at the airports within our mandate, given their value to local communities.

Our role in auditing airports

6.5 The Auditor-General audits 19 airport authorities and airport companies (for simplicity, we call them airports). These include six airports jointly owned by local authorities and the Crown. These are referred to as joint-venture airports.

6.6 The Crown and each local authority manage joint-venture airports in partnership. Each owns 50%, but the Crown plays no role in the airport's day-to-day operations. The Crown and the local authority share the cost of infrastructure investment in, for example, airport buildings and runways. The parties might share any deficits equally, and it is usual for surpluses to be retained within the business. The Ministry of Transport oversees the Crown's interest in joint-venture airports.

6.7 The Crown partly owns Christchurch International Airport Limited, Dunedin International Airport, and Hawke's Bay Airport Limited.

6.8 Local authorities wholly own seven airports.

6.9 Eastland Group operates Gisborne Airport Limited under lease from Gisborne District Council. Gisborne Airport Limited is required to prepare financial statements and have them audited under the Companies Act 1993.

6.10 Invercargill Airport Limited is 97.2% owned by Invercargill City Holdings Limited, a subsidiary of Invercargill City Council. The remaining shares are held by Hokonui Research and Development Limited (0.7%), Oraka-Aparima Runaka Incorporated (0.7%), Te Runaka o Awarua Charitable Trust (0.7%), and Waihopai Runaka Holdings Limited (0.7%).

6.11 Omarama Airfield Limited is 50% owned by Waitaki District Council and 50% owned by an incorporated society.

Overview of financial performance

6.12 Figure 6 provides an overview of the financial performance of the airports that we audit. These airports vary significantly in size.

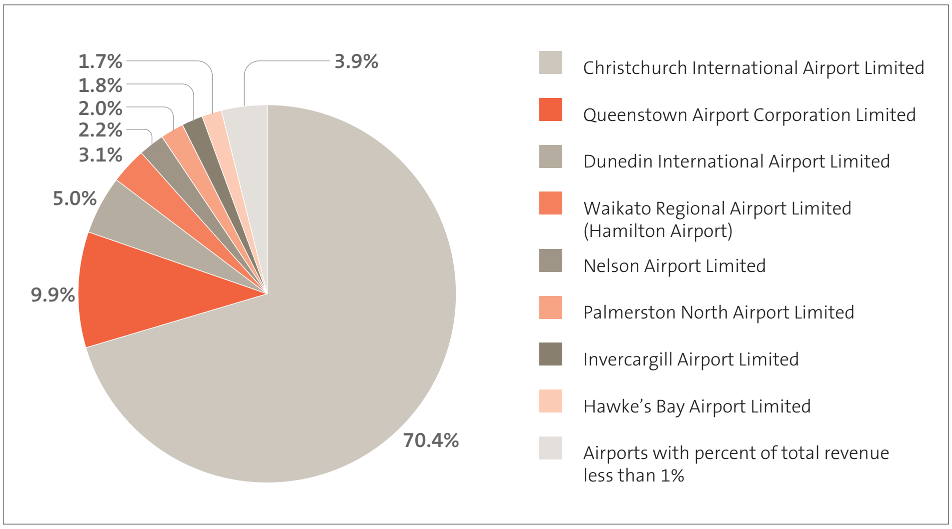
Figure 6
Summary of airports' 2014/15 financial results and financial position

Entity name	Revenue $000	Pre-tax surplus or (deficit) $000	Equity $000	Total liabilities $000	Total assets $000
Joint venture airports					
New Plymouth Airport Joint Venture	2,006	(164)	22,885	5,233	28,118
Taupo Airport Authority	444	(200)	9,914	1,088	11,002
Whanganui Joint Venture Airport	450	(324)	7,587	382	7,969
Westport Airport Authority	137	(147)	3,616	84	3,700
Whakatane Airport Authority	194	(232)	890	878	1,768
Whangarei District Airport	571	120	4,626	79	4,705
Wholly local authority-owned airports					
Hokitika Airport Limited	661	115	2,773	632	3,405
Marlborough Airport Limited	1,618	6	1,264	5,782	7,046
Nelson Airport Limited	5,403	2,161	11,350	1,815	13,165
Palmerston North Airport Limited	4,943	911	49,305	12,238	61,543
Queenstown Airport Corporation Limited	24,836	11,506	161,060	39,067	200,126
Rotorua Regional Airport Limited	2,322	50	1,740	1,229	2,969
Waikato Regional Airport Limited (Hamilton Airport)	7,765	289	59,669	18,874	78,543
Crown- and local authority-owned airports					
Christchurch International Airport Limited	177,383	50,205	766,766	446,029	1,212,795
Dunedin International Airport Limited	12,722	2,477	45,920	26,813	72,733
Hawke's Bay Airport Limited	4,381	1,830	27,065	7,768	34,833

Entity name	Revenue $000	Pre-tax surplus or (deficit) $000	Equity $000	Total liabilities $000	Total assets $000
Partially local authority-owned airports					
Invercargill Airport Limited	4,435	1,094	17,769	7,480	25,249
Omarama Airfield Limited	170	42	1,350	11	1,361
Other airports					
Gisborne Airport Limited	1,379	634	2,558	966	3,524
Total	**251,819**	**70,373**	**1,198,108**	**576,448**	**1,774,555**

6.13 At the end of 2014/15, these airports had total assets of $1.77 billion. Their total equity was $1.20 billion. They reported total revenue of $251.8 million, 85% of which was earned by three airports (see Figure 7).

Figure 7
Share of total revenue, by airport



6.14 The airports listed in Figure 6 reported total pre-tax profits of $70.4 million, 88% of which was earned by two airports. Five airports, all joint ventures, reported a deficit.

6.15 The operating revenues and pre-tax profits reported in 2014/15 were up from reported results in 2013/14.

6.16 Seven of the airports paid dividends to their shareholders in 2014/15 totalling $16.6 million. Dividends ranged from $10,000 to $9.9 million. Most of the$16.6 million was paid to the shareholders of Christchurch International Airport (60% of the total), Queenstown Airport (26%), and Dunedin International Airport (7%). The remaining 7% was paid to the shareholders of Hawke's Bay, Nelson, Hokitika, and Palmerston North Airports. In 2013/14, the same seven companies paid dividends totalling $12.6 million.

Airport revenue

6.17 The Airport Authorities Act 1966 specifies that an airport company is to be managed as a "commercial undertaking".[35]

6.18 All of the airports in our mandate, except for Gisborne Airport Limited, are held in a council-controlled trading organisation (CCTO). They are run at arm's length from a local authority and governed by a Board. The Local Government Act 2002 defines CCTOs as CCOs that operate to make a profit.[36] However, many local authorities see their airports as an essential public service, and aim to achieve no more than a break-even financial position.

6.19 Because airports are commercial entities, they are self-funding. Airport infrastructure decisions are commercial investment decisions, largely funded by airports and recovered through airline fees.

6.20 The revenue that airports generate is therefore important to their viability and sustainability.

6.21 In 2014/15, only three airports, two of which are joint ventures, received capital contributions from shareholders. These contributions totalled $7.3 million. In 2013/14, the same three airports received capital contributions totalling $1.1 million. Such contributions are often for runway maintenance and resurfacing.

6.22 Airport revenue includes aeronautical revenue, which is the income an airport receives from landing fees and passenger service charges, and other revenue that can be generated from car parking fees, retail leases, property leases, and advertising.

6.23 Airports' landing fees and passenger service charges and how they calculate the charges are not regulated, although Auckland, Wellington, and Christchurch International Airports are subject to information disclosure requirements under the Commerce Act 1986. Under the Airports Authorities Act 1966, airport companies with revenue of more than $10 million a year must consult with the

35 Airport Authorities Act 1966, section 4(3).

36 Local Government Act 2002, section 6(1).

major airlines[37] that use their services every five years and whenever they propose changes to aeronautical charges.

6.24 We were told that, because of the importance of airlines to the connectivity and sustainability of their communities, airports will often compromise when they consult on proposed landing charges and set lower-than-desirable fees to ensure that the airlines continue to serve their airport. This could mean that airports have to increase their revenue stream from other sources to make up for the shortfall.

6.25 Our analysis showed that aeronautical revenue varies considerably between airports and appears unrelated to the size of the airport facilities or passenger volumes. The reported information shows that aeronautical revenue as a percentage of total revenue varied from 23% to 68%. Because each airport discloses aeronautical revenue slightly differently, with some separately disclosing landing fees and others including fees such as airfield rental, it was difficult to identify any clear patterns.

Airport infrastructure challenges

6.26 Airports typically complete master plans as part of the long-term planning for their major infrastructure. Some airports (Auckland, Wellington, and Christchurch International Airports) are required to carry out separate consultation about capital expenditure for projects that exceed 20% of aeronautical assets. Smaller airports are not required to consult on capital expenditure proposals,[38] but most usually do.

6.27 Airports experience resistance from the dominant airlines to proposals for infrastructure development that the airlines see as unnecessary and that could result in increases to airport charges.

6.28 Some infrastructure investment requirements can affect an airport's long-term viability. Accessing funding for such investments can be challenging, and some airports do not generate enough revenue to fund major works. We were told that joint-venture airports find it difficult to obtain loans because they do not have a capital structure.

6.29 Many of the costs of maintaining airport infrastructure are the same, no matter the size of the airport facilities, passenger volumes, or revenue. For example, the cost of overlaying the runway at Palmerston North Airport was $3 million, while full replacement can cost $20 million. This would be a significant investment for that airport, which has total assets of $61.5 million. Invercargill Airport is currently replacing its terminal at a total cost of $12 million, and New Plymouth Airport is looking at upgrading its terminal building with an estimated cost of $11 million.

37 Those that contribute 5% or more of aeronautical revenue.

38 Section 4C of the Airport Authorities Act 1966.

6.30 Maintaining and renewing airport infrastructure can be costly, but it is often needed to meet Civil Aviation Authority standards. For example, if an airport operates at night, it needs landing lights and navigation facilities whether it receives one flight a week or 10 flights a night.

6.31 Joint-venture airports are in a slightly different position. They might receive some funding from the Crown and the local authority shareholder. The Crown funding is subject to the Minister of Transport approving a capital programme. In 2013/14, the Crown provided total funding of $116,000 to two joint-venture airports.

6.32 Airports need to keep up with technological advances. Often, this means having to invest in new infrastructure to remain competitive. For example, the air navigation system is changing from ground-based navigation aids to the satellite-based global positioning system, the certification regulations for aerodrome safety are being re-assessed, and security requirements might be reviewed. All these could require further infrastructure investment.

6.33 The challenges that airports face reinforce the need to carefully consider long-term investment needs and the implications and consequences of not completing required infrastructure works.

Airports' importance to regions

6.34 Our recent report on the 2015-25 long-term plans[39] showed that the populations of most districts outside the major centres will grow slowly or remain relatively static. A few districts are likely to have fewer residents in 2025 than today. Local authorities see economic development as important to the long-term prosperity of their regions, with many local authorities including economic development initiatives in their long-term plans.

6.35 Airports form part of New Zealand's air transport network and are seen as an important contributor to a region's economy. Airports connect New Zealanders and businesses by enabling people and cargo to move between different cities and towns.

6.36 A study last year by Business and Economic Research Limited into the effect of stopping flights between Wellington and Taupo suggested that the short-term effect on business spending in Taupo was about $1.8 million a year, with much larger longer-term implications.[40]

39 Controller and Auditor-General (2015), *Matters arising from the 2015-25 local authority long-term plans*, Wellington.

40 *Cessation of Wellington-Taupo air service* – note prepared for Taupo District Council by Business and Economic Research Limited, March 2015.

6.37 In 2013, the New Zealand Airports Association[41] commissioned another study. The results indicated that Marlborough Airport made a direct contribution to the region of $1.5 million a year. Its total contribution, including enabling imports and exports to the region, was $197 million.

6.38 Local Government New Zealand has acknowledged that regional growth is important for national economic and social prosperity. It is looking at the transport factors that contribute to regional economic development. It encourages decision-makers in central government to work with local authorities to ensure that transport decisions do not have negative effects on the regions.

6.39 The Government recognises the importance of all transport modes to the national economy in its 2015 National Infrastructure Plan.[42] Strong links between road, rail, shipping, and aviation are vital for moving people and freight around the country and overseas.

6.40 Last year, the Ministry of Transport announced its "Futures Visions". These visions identify potential drivers of change with the aim of enabling organisations to plan how they might respond to a different future. The Ministry of Transport hopes that the visions will stimulate debate and generate ideas on how New Zealand's transport system might change in the long term.

6.41 The Ministry's vision for the future of domestic air travel in New Zealand involves people living outside the main urban centres and commuting into the cities by air for work. Cheaper and faster travel will allow for growth in regional centres. The Ministry states:

> *In our vision, New Zealand remains one of the most connected of countries, from our metropolises to our regional centres.*[43]

6.42 We note that the Futures Visions work is intended only to start conversations about how the transport system might evolve. Regional centres thriving as a result of cheap and efficient flights to the main cities is one of many possibilities.

6.43 It is encouraging to see central and local government stakeholders considering the role and future of airports within the transport sector. The Ministry of Transport and the New Zealand Airports Association are working together to investigate the future of the domestic air network. They seek to identify the main matters affecting the network's future development. They will ultimately report their findings and that report should provide some useful analysis to inform future thinking.

41 The New Zealand Airports Association is the industry association for airports and related businesses.

42 National Infrastructure Unit (2015), *National Infrastructure Plan 2015: The Thirty Year New Zealand Infrastructure Plan*, The Treasury, Wellington.

43 See www.transport.govt.nz/futures.

Commercial undertaking or social infrastructure?

6.44 As well as connecting people and places, and contributing to a region's economic profile, airports also provide an important service for the health sector. Patients are transferred by air in emergencies or for specialist treatment in the larger hospitals. Depending on the level of criticality, patients are transferred using scheduled airline flights or chartered air ambulance aircraft.

6.45 For more remote communities, quick access to urgent medical services that are not available locally can sometimes be the difference between life and death. Without a local airport, patients would face a longer journey by road.

6.46 However, despite contributing important economic benefits and vital social services to their communities, airports are first and foremost required to operate as commercial undertakings. This is a requirement of the Airport Authorities Act 1966.[44]

6.47 This statutory obligation confirms the primary objective of airports. However, in reality, many local authorities choose not to seek a full return on their investment. Instead, local authorities take the view that their community gets many other benefits from the air connections that the airport provides.

6.48 Air New Zealand is often the only airline servicing regional airports. If the airline stops flying to an airport, that airport's viability is at risk unless another operator picks up the route.

6.49 Airlines decide where they will provide direct services based on viability. Passenger numbers, costs to operate the aircraft, air navigation service costs, and airfares affect viability. Smaller airports are typically serviced by smaller aircraft. This is in part because of small passenger volumes but also because of the shorter runways. Smaller aircraft are, relative to seat numbers, more expensive to operate than larger aircraft.

6.50 The costs of air navigation services can affect whether an airline services a particular airport. A decreasing number of flights into an airport spreads the airport's costs between fewer users, increasing the cost for each flight.

6.51 In November 2014, Air New Zealand announced the gradual removal of the 19-seat Beech aircraft from its fleet by August 2016 and an increase in its 68-seat ART-72 fleet. Some routes operated by the Beech aircraft have already ended. The larger 50-seat Bombardier aircraft, which usually flies less often, has replaced the Beech aircraft on other routes.

44 Section 4(3).

6.52 Air New Zealand's decision meant that the airline no longer serviced several small regional airports, including Westport, Kaitaia, and Whakatane. Many local authority owners of airports are concerned about the effect on their communities.

6.53 Several independent operators have since stepped in to provide replacement services, largely because of the efforts of the local authorities. Sounds Air operates a Westport-Wellington service and a Taupo-Wellington service. Air Chathams operates a Whakatane-Auckland service. Sun Air now flies from Whakatane to Gisborne and to Hamilton. Barrier Air operates a Kaitaia-Auckland service. Kiwi Regional Airlines has announced its intention to cover a route network including Dunedin, Queenstown, Nelson, and Hamilton.

6.54 The ability of these smaller operators to continue providing these services in the long term is uncertain. Barrier Air is already reported as struggling to attract enough passengers to make its route viable. It might have to stop the service if passenger numbers do not increase. Buller District Council underwrites the Sounds Air Westport-Wellington service.

Concluding comments about airports

6.55 Airports operate in a challenging environment. The commercial priorities of airlines and airports can sometimes conflict with the wider objectives of local authority shareholders for their airports to play a role in the economic and social wellbeing of their districts. Although airports are required to make a profit, some airports keep their airport charges low to ensure that airlines continue to provide flights. Because they are largely self-funding, airports must find alternative revenue streams from activities such as car parking and retail leases.

6.56 The revenue that airports generate is critical to their ongoing viability. 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.

6.57 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.

6.58 Of the 19 airports we audited, just two earned 88% of the total surplus in 2014/15. Five airports reported pre-tax surpluses of less than $250,000, and five reported a deficit.

6.59 Despite the important role they play in regional economies, the ability of some airports to continue servicing their communities depends on the airlines. What the airlines do is largely dictated by market forces and the viability of the route, which the smaller regional airports have little to no control over.