Reference: RTJ2025/002

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Dear Rob,

IATA COMMENTS - AIRWAYS PRICING CONSULTATION FY2026-2028

The International Air Transport Association (IATA) is the trade association for the world's airlines, representing some 350 airlines and over 80% of total air traffic. We support many areas of aviation activity and help formulate industry policy on critical aviation issues. IATA member airlines include Air New Zealand and many foreign carriers that operate flights to Aotearoa New Zealand and through its airspace.

IATA appreciates the information provided in the consultation paper and will endeavour to provide our comments and recommendations constructively, to ensure that the air navigation services provided by Airways continue to be delivered efficiently and cost-effectively to support a safe and sustainable operation for airspace users.

Proposed Increases

A key concern for IATA and our member airlines is the significant cumulative increases in operating costs and passenger-related charges/taxes for air travel into Aotearoa New Zealand. This proposed increase of 22.8% over three years (FY2026-FY2028) will join a long list of recent and upcoming increases such as airport charges e.g. AKL PSE4, CAA levies, Border Clearance Levy (BCL), International Visitor and Conservation Tourism Levy (IVL) and visa processing fees. Aotearoa New Zealand is alarmingly evolving into a very expensive and unaffordable destination, particularly for international passengers and tourists. This adds to the already very challenging market conditions for airlines that operate in Aotearoa New Zealand and does not support their long-term growth aspirations, further jeopardising Aotearoa New Zealand's economic prosperity.

We request Airways revisits the price proposal and propose alternative options based on its updated modelling following the inclusion of the recommendations from stakeholders in this consultation process. If and when increases are necessary and justified, we request a reconsideration of the proposed front-loading of the increases in the first year, instead, to smooth them out over the three years, or possibly beyond this period where possible.

IATA continues to call for cost restraint by all service providers and adopt disciplined and concerted efforts to reduce the overall pressure on the already price-sensitive market. We will provide our comments and recommendations in the specific sections of this submission which should be considered with the objective of lowering the target revenue and the required increases.

Changes to Base Operating Costs

While IATA appreciates the provided information listing the summary of key increases in Airways' costs, the consultation paper lacks the individual business cases needed to support the assessments thoroughly. In line with global best practice, each proposal should be comprehensively reviewed with stakeholders leading into this pricing consultation process.

To look at similar structures in the region, IATA would like to highlight the positive decision by the Australian Competition and Consumer Commission (ACCC)[1] on the need for Airservices Australia to improve its consultation and engagement with stakeholders to address this same concern – lack of transparency and accountability. In response, Airservices Australia has recently re-established the Pricing Consultative Committee (PCC) of which IATA and other key stakeholders are members. Engagement to this new process commenced in February 2025 to support the new pricing agreement effective July 2027, with more than 2 years' lead time.

> *"The ACCC considers the Pricing Consultative Committee should involve constructive engagement with stakeholders on items such as: (i) the need and design of a risk sharing arrangement; (ii) the appropriate weighted average cost of capital; (iii) the efficiency of operating expenditure and how it relates to service delivery and improvements; and (iv) the efficiency and prudency of capital expenditure, including by providing sufficient information to understand project feasibility, project implementation, commissioning and cost overruns compared to original business cases.*
>
> *The ACCC reiterates its recommendation from its preliminary view that Airservices should implement effective customer engagement programs and share appropriate information. This will enable more effective stakeholder input into pricing and operational matters."*

We would view it as appropriate for Airways to consider these comments made by the ACCC in their ongoing planning around cost structures and associated engagement with the industry.

The increases to operating costs, particularly for FY26 (NZ$40.7m or +16.1%) are exorbitant and warrant closer inspection and more detailed discussions with airlines and users. We note that out of this amount, NZ$27.4m or 67% is to recover the current operating cost base in FY26. IATA has reservations with the proposed approach and believes more can be done by Airways to contain/minimise its impact on users. Given Airways' monopoly status, we would expect the organisation to apply greater control over its cost escalations and moderate the increases over a period, which reflect decisions that would have otherwise been made if it were operating in a competitive environment. Rightfully, Airways should provide in-depth reports of its efficiency and cost reduction initiatives and their results against the agreed targets. This aspect warrants an in-depth discussion with Airways stakeholders.

Similarly, the proposed increase in staffing level to improve system resilience at NZ$9.7m deserves more discussion and review with users. ATC salaries have been a significant component of the last two charges reviews which resulted in very large increases. While it is understandable that Airways wishes to integrate some resilience into its workforce planning for retirements and unplanned departures, the figures indicated are of such a magnitude that they are worthy of a more detailed explanation.

It would be expected that Airways manages resilience through carefully timed and managed recruitment and training, not long-term numbers over and above that required to support operational rosters. Carrying excess numbers for transition projects should be clearly documented in the change program being supported and the calculations for the 'bow-wave' required, including the reason and planned timelines.

Notwithstanding the above, modern ATM Automation Systems and CNS technology enable full functionality during periods of constrained growth in operational ATC numbers. If numbers continue to grow, should the investment in

[1] ACCC Decision on Airservices Australia Pricing Notification October 2024 pg 14-15

modern technology not be delivering the desired benefits or outcomes, then this investment should be reconsidered.

In circumstances where operational resilience is concerned, stakeholders need to understand the detailed analysis that led to the lack of coverage. It is important that stakeholders are able to clearly understand whether this is due to systemic staffing shortages or simply an inability to replace staff at short notice. It would be appropriate for Airways to clearly extrapolate and explain these scenarios.

The increase in base operating cost of NZ$5.2m is significant. While IATA agrees that preventive maintenance is important in ensuring the required system availability and reliability, based on the information provided, we are not convinced that an increase in FTEs to support this area is warranted. This is further underlined through Airways' own reporting that it has delivered very high core systems availability (e.g. 99.99% in FY24). It would be useful to understand the overall mapping of the various maintenance and repair scopes, (i.e. in-house vs outsourced), and an analysis of the cost effectiveness in carrying out these functions. IATA queries whether some of these works be outsourced more economically and, the mix of internal against contracted maintenance. There should be opportunities to further optimise this cost to deliver the same, if not better, outcomes, while ensuring acceptable reliability and resilience of Airways.

Effectively, IATA is of the view that system resilience projects should be modulated more gradually and demonstrate their necessity. We therefore request Airways review its proposed plans and consider a more sustainable way of phasing these projects based on their criticality and overall cost impact on users.

IATA is an advocate for safety and believes there should be no compromise on this aspect. However, an increase to the base operating costs of NZ$1.6mis not insignificant. To support the assessment of the proposal by Airways, we would need to understand the overall safety gaps, the current staffing level by functions and levels (i.e. safety-critical vs support functions), and how these additional FTEs fit within the organisation to deliver the envisioned safety outcomes. IATA queries whether Airways has considered more cost-effective options, such as consultants being employed on a project basis to address specific safety gaps, rather than on a permanent basis.

IATA strongly opposes the loading of Uncrewed Traffic Management (UTM)-related costs on existing users. While we recognise the need for Airways to initiate such initiatives to ensure a safe and seamless integration in the future, such costs should be parked and accounted for separately until the cost recovery mechanism for this new user group is in place (similar to the capitalisation of assets approach – not charged until fully commissioned). Alternatively, there is a role for the Government to step in to directly support the cost of such initiatives through grants etc. Existing airspace users should not be penalised or cross-subsidising such costs. Instead, it should be the owners or users of such uncrewed devices who foot the bill for these costs.

IATA appreciates the clarification by Airways to the question posed during the consultation period about inter-company charges. Our primary concern is the overall growth in these costs without assurance from Airways that the services provided by its subsidiaries are the most cost-efficient approach. Related party transactions such as this ought to be outlined transparently and in line with global best practice governance. This would require the involvement of the industry users who fund these services, in considering the options available.

Inflation Uplift

IATA opines that inflation, and its associated uplifts have no basis at the outset. There is a risk that allowing inflationary increases will dilute Airways' focus on the delivery of efficiency improvements. Going forward, we expect that Airways will work toward lowering the unit cost per [air traffic] movement which would be a better measure to counter any inflationary pressure on costs. It would be useful for Airways to analyse the unit cost and how the proposed unit cost in the upcoming period fares against historical performances (excluding the pandemic period) for each user group.

We further note that Airways has claimed that the cost base increase for some areas is above the Primary Producers Index (PPI), specifically in corporate costs and maintenance. It would be useful for Airways to share more detail about its various maintenance contracts and overall approach in negotiating and procuring these services. This will generate the required confidence that these contracts are delivering value most cost-effectively. The same approach should also apply to corporate costs.

IATA noted that Airways and NZALPA signed a MoU in February 2024 to settle the April 2024 salary increase negotiations and future negotiations at CPI plus 1% with a maximum and minimum which varies each year. IATA questions whether Airways have considered the different scenarios (i.e. MoU vs no-MoU). It would be useful for Airways to state the benefits of signing the MoU and agreeing to the terms (i.e. committing Airways to the CPI plus 1% increase in future negotiations, as opposed to normal/regular salary increase negotiations). We wish to further understand how the maximum and minimum are determined each year, and whether a cap has been agreed upon alongside any conditions set as prerequisites in triggering the increases.

Allocation Methodology

IATA appreciates the additional information provided by Airways concerning its pricing assurance framework and has noted that the 2026-2028 Price Reset will continue to utilise the Manual DCM Model as well as the Adaptive Insights DCM Model. While the Pricing Framework contains the structure and how Airways approaches the allocation of costs and the translation to pricing, IATA is not privy to the more detailed information that would allow us to assess the reasonableness of the approach i.e. allocation ratio etc.

PWC's Independent Assurance Practitioner's report is useful to the extent of ensuring that the costs for non-regulated services were excluded from the input into the revenue calculation. However, it would be useful for Airways to share the details of the non-regulated services and their costs to provide the necessary assurance that the assessment was all-encompassing and comprehensive. For example, how the costs for each non-commercial airline user group are allocated e.g. military and their recovery by Airways. It is pertinent for airlines to be able to detect any existing or potential cost creep or shielding of these costs resulting in unreasonable allocation of the costs (i.e. cross subsidisation).

Charges to commercial airlines should be attributed to the cost of providing these commercial services and not include any cross-subsidy for services to general aviation, military, the State or exempted traffic. IATA would like to seek further clarity on this aspect and the assurance that these non-commercial airlines costs have been allocated accordingly and excluded from the pricing for commercial airlines.

Costs and projects that benefit specific user groups, service or location should rightfully be allocated and recovered from the end users/beneficiaries. For example, the Remote Aerodrome Advisory Service (RAAS) project costs should be demarcated and allocated to the users of the facility (i.e. capital investment costs of NZ$1.5m in FY26-28). If the RAAS concept can be implemented in other locations, a shared cost approach can be considered. It is not clear that this is the case based on the information provided in the consultation paper. We can only assume that the pricing framework addresses this aspect.

IATA noted that Airways International Ltd (AIL) is a subsidiary of Airways providing commercial services. From our experiences in other jurisdictions, we have found that at times the demarcation of costs is weak and has led to airspace users paying costs that should have been fully funded by the commercial entities. Based on this, we request Airways identifies the shared resources and assets and how these costs are allocated. This should include all the subsidiaries under AIL as well, such as AIRSHARE, Airways Training and AEROPATH.

It is also important to segregate the mandatory costs required by Airways in delivering its services against those costs that are nice to have or optional. For example, the costs associated with Airways' involvement to support the State in its global engagements (e.g. ICAO meetings) should be funded accordingly by the State. Similarly, optional costs such as membership fees and others should not be automatically passed through to users. We would expect these optional costs be funded by Airways from its markedly high target returns/profits or by the State. As a rule or starting point, association and membership fees, non-operational/essential travel costs, etc. that have no direct relation to support the provision of services should rightfully be excluded.

IATA appreciates the clarification provided by Airways about the fluctuations in income tax and has noted the reasonings stated. It is regrettable that Airways is affected by the removal of the tax deduction for depreciation on non-residential buildings. Given Airways' SOE status and mandate in providing critical state functions, IATA questions whether Airways has explored the possibility of requesting a dispensation from the Government.

Capital Expenses and Projects (CAPEX)

We noted that Airways is proposing to invest NZ$211.9m in capital projects over the FY26-28 period. Out of this, NZ$142.4m has been included in the pricing calculations for this period for fully commissioned services. Collectively, the planned CAPEX costs constitute a significant amount compared to the projected revenue, which raises the question of whether the approach is sustainable and the right decision to go with. IATA believes that some of these capital projects could be deferred or further optimised. As highlighted earlier in this submission, a robust consultation framework should be adopted by Airways to review the proposed capital investments before any pricing decisions.

Auckland Tower Replacement

IATA has separately responded to the consultation process on this matter in both 2022 and 2024 and maintains that a digital tower should be explored as the preferred solution until and unless it is demonstrated that the option is untenable due to safety or technical considerations.

While we noted that this will not enter the pricing asset base until its forecast completion in FY29 and that Airways has reduced the planned expenditure from (NZ$45.8m to circa NZ$40m) for the construction of a new conventional tower, it is of utmost importance to recognise that the deadline extension to 2035 for the return of the land to Auckland Airport will now allow the decision to be postponed and reconsidered at a much later date. This will also ensure that the Full Digital Option is further investigated to assess its appropriateness as the best option moving forward.

We are disappointed by the announcement on 31 March, that Airways is forging ahead with constructing a new 45-metre tower in lieu of a digital option while this pricing consultation is still ongoing. While we respect that this is the chosen path that airspace users will need to finance, the timing of the decision does not reflect an open and meaningful consultation process

It is well-recognised that the pressing need to consider the replacement/alternative option for the tower stems from the impact on the tower's visual coverage following the planned construction of the new domestic pier (A1). Similarly, we also noted that "*the construction will also render the existing Contingency Tower inoperable, necessitating its replacement*". Of great trepidation to IATA is the lack of planning coordination between AIAL with Airways, confirmed by Airways in its *AKL Tower Replacement Decision Documen*t, where it was highlighted that "*With limited insights into the current terminal expansion...*" concludes that AIAL's planning and coordination has clearly fallen short. Consequently, both the airlines and other airspace users are taking the brunt of the high-cost implications resulting from the lack of effective planning and coordination between AIAL and Airways. As stated in our 2024 submission, we do not believe that airlines should be required to foot the bill for an apparent breakdown in communications between the airport and Airways.

On this basis, we would request that Airways investigate if AIAL is liable for these unplanned costs, either fully or partially, due to its lack of coordination and foresight in the planning of its infrastructure expansion. Put simply, airspace users should not pick up on costs that result from the negligence of another party.

Regional Tower Services

IATA welcomes efforts to further improve and optimise the delivery of regional services by Airways. The costs involved in such initiatives should be allocated to the users of these services which should eventually benefit from the operating cost reductions in the longer term.

Airspace Architecture

Given that the focus of this initiative is domestic surveillance services, IATA would expect that any such costs will be allocated to the users of these domestic services without any unjustified cross-subsidisation by international airspace users.

Primary and Secondary Radar Replacement

IATA does not object to replacement of SSR provided there is a positive business case that demonstrates it is more appropriate than the cost-efficient solution of ADS-B is. While less secondary radar replacements (SSRs) will mean lower costs, caution should be taken to ensure that the remaining SSRs have limited overlap. There should be full utilisation of Mode S capabilities, where feasible, including information provided by downlinked aircraft parameters.

Where SSR and ADS-B provides the same or better coverage, we do not support primary radar replacement for air traffic control surveillance services. Costs of non-cooperative surveillance for the reason of protecting against unlawful airspace intrusion by uncrewed traffic should be borne by this community.

Southern & Auckland Surveillance Upgrade

IATA supports MLAT where operationally necessary and acknowledges the proposals to replace these services in Queenstown and Auckland. Operationally necessary scenarios include, but are not limited to, providing coverage enhancements or acting as gap fillers for SSR or ADS-B, or when used in support of airport ground operations.
IATA supports the approach that users only pay for services once the assets are "fully commissioned" and services provided to airlines.

Target Revenue

The current proposal in its current form is concerning and unjustified. The fact that average price increases are higher than volume growth projected raises a fundamental concern about the imbalanced trajectory of growth vs cost i.e. 8.7% volume growth vs 22.8% average price increase over the FY26-FY28. We would like to seek more information and assurance of efforts in reducing the unit cost by Airways, including the optimisation and rationalisation opportunities highlighted by IATA and the airline community.

Weighted Average Cost of Capital (WACC)

IATA supports the New Zealand Commerce Commission (NZCC) IM decision to target the mid-point WACC and would expect Airways to adopt this rather than targeting the 65th percentile. In the absence of the required justification, we are not convinced that Airways, being the sole air navigation service provider, determines itself to have a higher risk and cost of underinvestment compared to airports. Airways is excessively rewarded by targeting anything more than the mid-point WACC.

Regarding the asset beta, any risk that Airways would have been negated given the application of the price reset mechanism (i.e. risks assumed by users). We do not see how the asset beta would not be affected by Airways passing on risks to users (in comparison to other sole service providers that do not). Any excess revenue or over collection prior to the price reset will not be recognised in the calculation of future pricing.

According to the 2022 McKinsey's value chain study[2], the asset beta for ANSP is considered to be 0.40, while for airports, it is 0.55. We noted that the NZCC applied an asset beta of 0.36 to calculate the WACC for the electricity service providers. From global discussions elsewhere, the ANSP asset beta should be close to the value used for electricity providers. Given that there have been no structural changes to the industry since 2022, IATA recommends capping the value of asset beta for Airways at 0.40, at most, rather than 0.60. Further, the Debt Premium of 1.10% is with airports, rather than the lower-risk ANSP environment.

We recognise that Airways is a State-Owned Enterprise (SOE) and is allowed to target commercial returns despite the Aotearoa New Zealand Government not setting specific profitability targets. IATA does not believe Airways should be targeting returns for its services which are essentially State functions and not commercial services. Airways is proposing an 8.08% return for services that would have been provided by the State in the first instance and rightfully should be done under a pure cost recovery basis (i.e. no WACC). We request that Airways consider the feedback from IATA on this aspect – that the Aotearoa New Zealand Government should rationalise its expectations on returns generated by Airways. Ideally, at most, it should be set on a pure cost recovery basis with nil target returns.

GST on International Air Navigation Services

IATA notes that the air navigation charges related to international flights are subject to the 15% GST. This contravenes Aotearoa New Zealand Government's commitments under the International Civil Aviation Organization (ICAO) policies. The imposition of any levies on international air travel, including the GST, directly contradicts accepted policies on taxation published by the ICAO. Aotearoa New Zealand, as a signatory nation to the Convention on International Civil Aviation (Chicago Convention) and a Contracting State of ICAO, has agreed to be bound by the legal provisions set by the Policies on Taxation in the Field of International Air Transport contained in ICAO Document 8632. These policies state that "each Contracting State shall reduce to the fullest practicable extent and make plans to eliminate (…) all forms of taxation on the sale or use of international transport by air, including taxes on gross receipts of operators and taxes levied directly on passengers or shippers". <u>As such, any GST on services and supplies provided in a Contracting State of ICAO, such as is currently the case for the GST on air navigation charges in Aotearoa New Zealand, should be zero-rated (and refundable, if any)</u>. Since GST and other consumption taxes are often widely cast by fiscal authorities, with only limited exemptions permitted, where GST is imposed on international air transport and related services, IATA urges all States to fully adhere to the ICAO resolutions.

Weight in Charging Formulas

[2] https://www.iata.org/en/iata-repository/publications/economic-reports/understanding-the-pandemics-impact-on-the-aviation-value-chain

It is generally accepted that capacity in terms of movements and time in the system, rather than weight, are the main cost drivers for Air Traffic Control service provision. While charging formulas generally include a weight-related element as a proxy for the 'ability to pay', reflecting the relative productive capacity of different aircraft sizes, ICAO Policies[3] also allows for weight to be disregarded i.e. charging a flat fee.

Airlines operating heavier aircraft generally pay a disproportionate level of the costs and this does not support the equitable allocation and recovery of costs. Small aircraft contribute to congestion but do not generally pay their fair share of the costs. Although any change to the weight element redistributes costs rather than reduces them, it results in fairer and more cost-related charges with non-airline users, including general aviation and business jet operators paying a fairer share of the costs.

While aircraft size and associated wake turbulence is a consideration for airport approach and departure separation, it is less of a consideration for inflight separation. Weight has questionable relevance where service is capacity constrained. Given the increasing marginal costs for creating new capacity, the current pricing system does not incentivise the best use of airspace.

IATA consistently advocates and supports the view that charges should be cost-related and fairly allocated among users. Capacity, in terms of movements and time in the system, is generally accepted to be the main cost driver of ATC service provision. Consideration should therefore be given to the removal of weight, or the reduction of its impact, in charging formulas. We would suggest Airways consider moving in this direction and look at options to gradually remove the consideration of weight in the charging formulas. An initial analysis should be taken to review the feasibility of this option and the overall transition strategy over the medium term.

Long Term Pricing Agreement (LTPA)

In the absence of a pricing determination process by an independent authority for the regulated services, IATA encourages Airways to consider the option of moving towards establishing LTPA with its customers. It is worth examining the recently adopted approach by Airservices Australia as highlighted earlier in this submission that should improve stakeholder engagements, enhance transparency and governance, leading to the finalisation of an agreed LTPA. This will also allow more in-depth discussions of the linkages between costs and service level elements between Airways and its customers.

Given the volatility of economic and geopolitical indicators, we suggest a more balanced approach where major decisions are deferred. To this end, IATA requests that Airways reconsider its proposal and work towards minimising the impact on the users of its services to the greatest extent possible. Greater cost restraint and reassessment of the criticality/priority of the various line items are necessary, with more direct involvement from airlines and users impacted.

In addition, we note that the Services Framework, Pricing Framework and Standard Terms and Conditions have been reviewed recently, resulting in minor changes. It would be useful to understand the process of reviewing these documents and what the changes were. Ideally, we would expect that the proposed changes would be subjected to a transparent consultation process.

It is important to recognise that collective industry efforts are needed, particularly fit-for-purpose policies and cost restraints to ensure that Aotearoa New Zealand remains a competitive, innovative, sustainable, and resilient air hub.

[3] ICAO Doc 9082 Tenth Edition 3.5.2 c)

IATA welcomes further deliberation on the proposal by Airways and the review of the possible options following the consideration of feedback from all stakeholders, including the need for the Aotearoa New Zealand Government to step in to address some of the concerns highlighted in our submission such as neutral target return/pure cost recovery and GST exemption for international overflight services.

Please do not hesitate to contact me at zanarinim@iata.org or Richard Tan, Senior Manager Airport & ANSP Charges at tanr@iata.org should you require clarification on IATA's observations and recommendations.

Yours sincerely,

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