



## **CITY OF PORIRUA NEW ZEALAND**

**Jenny Brash JP**

**OFFICE OF THE MAYOR**

14<sup>th</sup> August 2006

John Macilree  
Ministry of Transport  
PO Box 3175  
**WELLINGTON**

Dear Mr Macilree

**RE: PROPOSED CODE-SHARE ARRANGEMENT BETWEEN  
AIR NEW ZEALAND AND QANTAS**

You have separately received a submission from the Wellington Mayoral Forum on the proposed Code-Share arrangement between Air New Zealand and Qantas. You have also been advised that I am not a party to that submission. This letter is to make clear to you my position as Mayor of Porirua City and as a member of the Wellington Mayoral Forum.

I do not necessarily disagree with my Mayoral colleagues on the substantive issue of whether or not the proposed Code-Share arrangement should be supported. Neither I nor the Wellington Mayoral Forum have taken a position to support or oppose the Code-Share at this stage. However, I consider that the submission starts at the wrong point. It starts at the question of jurisdiction. The question of to what extent the matter will be dealt with by the Minister of Transport under s 88 of the Civil Aviation Act 1990 and to what extent the Commerce Commission will be involved in the examination, is a legal question. I would expect that the Ministry of Transport will get advice from Crown Law on this issue.

The reason that I did not support the Mayoral Forum submission is that I considered that the submission should have started with a set of principles for consideration of the Code-Share Proposal. The particular contribution that the Mayoral Forum can make is around questions of the regional interest, and how the Code-Share Proposal might be evaluated against principles relating to the regional interest. We are concerned with the outcome of what is best for the region. Like my Mayoral colleagues, I am passionate about the Wellington Regional Strategy and its goal of

increasing the region's international competitiveness. The question that requires rigorous and objective analysis is whether or not the Code-Share proposal should be supported or not in the light of that goal.

It is perhaps helpful to clarify my concerns if I list my understanding of the respective positions of the Wellington International Airport Limited, Air New Zealand / Qantas and the Wellington Mayoral Forum submission, as follows:

- **Wellington International Airport Limited**

The Wellington International Airport Limited has submitted [1] that the Minister should reject the application by Qantas and Air New Zealand for the Code Share. They believe that the Cartel proposal by the Airlines is unnecessary and extraordinary. They argue that the Tasman Networks Agreement is more a cartel or merger than a Code - Share and is outside the scope of the Minister's authorisation discretion. They submit that the operation as a joint business as envisaged by the airlines is not what was intended when the Minister was given powers under s 88 of the Civil Aviation Act 1990. They also submit that the application to the Minister is a "last ditch attempt to have a collusive arrangement authorised outside the purview of the Commerce Commission". They submit that prices will rise, seats will be harder to get in lower fare categories and there will be a reduction in travellers on the Tasman.

- **The Air New Zealand case**[2].

Air New Zealand has said that the proposed Code-Share is very different from the previous Alliance proposal it took to the Commerce Commission. It is strictly limited to the Trans-Tasman market. The Code-Share involves only international routes and therefore the proper process in New Zealand is to apply to the Minister of Transport. Section 88 of the Civil Aviation Act 1990 was created by the Ministry of Transport to provide a separate competition regime governing international air carriage agreements. It has been the basis of approval for a number of Code-Shares including the Air New Zealand / Singapore Airlines alliance in 1998, the Air New Zealand / United Airlines Alliance in 2002 and the Qantas / British Airways joint service agreement in 2003. All of those agreements included provision for agreeing prices and capacity and all were approved in corresponding jurisdictions under their respective competition regimes. Air New Zealand also argues that *"the rationale behind the Code-Share is simple. There is too much capacity in the Tasman market, 6,300 seats remaining empty every day ... The airlines benefit from reduced costs, not from pushing up fares. If we tried to do so, we know Emirates, Virgin Blue and others are there to step in – and that is fine – that is called competition"*.

- **Submission by Wellington Mayoral Forum**

The submission by the Wellington Mayoral Forum takes the following position. The submission acknowledges the constraint on the Minister of Transport (or delegate) to focus principally on the matters nominated in the Civil Aviation Act 1990 in deciding

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1[1] Submission on the application by Qantas and Air New Zealand for specific authorisation of a Tasman Networks Agreement pursuant to Part 9 of the Civil Aviation Act 1990, Wellington International Airport Limited, 31 July 2006.

2[2] "The Air New Zealand – Qantas Code-Share", address by John Blair, General Counsel, Air New Zealand, Aviation Industry Association Conference Rotorua, 28 July 2006.

on any Code-Share approval under the Act. However, it says the Forum is also aware of the view that some matters relating to competition should not and cannot be considered under the Act, and therefore should fall under the jurisdiction of the appropriate competition authority, that is the Commerce Commission. In this regard, it quotes the legal opinion from Auckland Barrister Professor Michael Taggart. The Forum submission also argues that the intent of the Civil Aviation Act is to provide exemption for minor or one - off proposals whereas the Air New Zealand – Qantas proposal is a wide Code-Share arrangement affecting all 25 routes and 242 flights weekly between the two countries. The Forum Submission says that the Code-Share proposal raises competition issues not covered by the Civil Aviation Act, and these aspects should be investigated by the Commerce Commission on their own account or on the recommendation of the Ministry of Transport. It says that scrutiny of the potential impact on competition should happen either under the discretion afforded by the Civil Aviation Act, or under current competition legislation, or both. It says that the appropriate forum for the examination of competition issues is the Commerce Commission.

My concern is that the Mayoral Forum submission appears to have started at the wrong point. It has started at the question of jurisdiction, but it should have started with a set of principles to assist consideration of the Code-Share proposal. I would have thought that a principle might be:

- *“that the proposed Code - Share does not act to the detriment of the interests of the region, compared to viable alternatives”*

If we start with the above principle, then the issues to be examined regarding the proposed Code - Share would include:

- quality of service
- price
- sustainability of the service

I have seen the submission by Wellington International Airport Ltd, the document on “Benefits and costs to the public of the proposed Air New Zealand and Qantas Code-Share, Trans- Tasman services to Wellington” prepared by LECG Ltd, and the legal opinion from Professor Michael Taggart . Those documents appear to be arguing that the code share arrangement would lead to a reduced service, a significant (16%) price increase and reduced leisure and business travellers of 24% and 11% respectively, and therefore is not in the public interest.

In the absence of any critical analysis with an alternative viewpoint, I would note the following, with regard to the criteria I suggested above:

- *Quality of service:* The standard of service would not necessarily go down under a Code - Share arrangement. I understand that many Air New Zealand and Qantas flights arrive or depart at a similar time. This phenomenon is well known in the economic literature where two competitors will tend to converge. Under a Code-Share arrangement, there is likely to be a rationalisation of schedules, which would be likely to lead to an increased number of timeslots in which aircraft would arrive and depart. That is, although there would be fewer planes flying, there would be a greater

number of timeslots available to consumers, and therefore consumers would have greater choice

▪ *Price:* I note that the *Competition and Regulation Times*, July 2006 said that it found that the Hirschman-Herfindahl measure implies that routes served by just one carrier have prices around 20% higher than duopoly routes do. They also suggested that the Tasman market is “more competitive” than other airline markets. This could mean it has lower prices because of the presence of Pacific Blue and/or Emirates. The threat of market entry by other airlines would restrain the increase in fares. Also, if any regulator considering the application in New Zealand and Australia concluded that fares would rise significantly as a consequence of the Code-Share, they are unlikely to approve it.

▪ *Sustainability of the service:* On the question of sustainability, Air New Zealand has made it clear that it cannot sustain the millions of dollars of losses in operating the current levels of service to Wellington. There must be a risk if the Code - Share is not approved that Air New Zealand could withdraw from the Tasman route through Wellington, which could do significant harm to the Wellington region.

In summary, I have not taken a position for or against the Code-Share proposal, but I would like to see a rigorous and objective analysis of the pros and cons when evaluated against the regional interest. I believe that we should start by defining principles relating to the regional interest in this Code-Share proposal, not on the issue of jurisdiction. Hence, I have reluctantly not supported the Mayoral Forum submission. However, I hope that the principled approach that I have endeavoured to take is useful in your deliberations. I am copying this letter to the same copy addressees as the Mayoral Forum submission.

Yours sincerely



Jenny Brash  
**MAYOR**

**Copy to:** Hon Pete Hodgson  
Hon Annette King  
Hon Trevor Mallard  
Hon Phil Goff  
Hon Lianne Dalziel  
Hon Dr Michael Cullen