

# The International Passenger Clearance Funding Bill

Regulatory Impact Statement

ISBN 978-0-478-37049-2 (online)

August 2010



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# Agency Adequacy Statement

This Regulatory Impact Statement has been prepared by the Ministry of Agriculture and Forestry (Biosecurity) in conjunction with the Ministry of Labour (Immigration), the Ministry of Transport, the Aviation Security Service (Avsec) and the New Zealand Customs Service (Customs). It provides an analysis of the policy decisions required to finalise the *International Passenger Clearance Funding Bill*.

The *International Passenger Clearance Funding Bill* is the legislative means of giving effect to Government's decision to impose cost recovery on international airports in very specific and limited situations. The proposals covered by this RIS alter and add to the already agreed policy for this Bill.

There are some constraints, caveats or uncertainties concerning the analysis in the RIS. Significant time and effort has already been invested in the development of the policy for funding of international passenger clearance services. The primary policy was formed in 2004/05 following extensive industry consultation. Under this arrangement:

- **customs** and **biosecurity** services are considered to deliver a public benefit and services at established international airports are Crown funded;
- **Aviation Security Services (Avsec)** are considered to deliver a private benefit (i.e. to those travelling on the aircraft) and are funded by a per passenger fee charged on airlines;
- it is envisaged that costs will be borne approximately 50/50 between government and airlines; and

In conjunction with this arrangement, the previous Government decided that biosecurity, aviation security and customs services at new international airports and low volume international airports would be funded by cost recovery from airports.

This RIS assessment accepts this policy arrangement as the status quo and focuses on assessing only the final policy for applying cost recovery at new and restart international airports.

The engagement with industry has continued since 2004/05 as the policy for cost recovering from new and restart airports has been fine tuned. There has not been a formal consultation round to specifically support these final policy decisions because:

- the basis for cost recovery has been the subject of various consultations in the past and the shift to have cost recovery apply for a fixed term is a marginal adjustment that will lead to a simpler and more certain funding arrangement – but the fixed term basis has not been specifically consulted on;
- the need for an arrangement to cover restart was covered in the 2009 consultation led by Customs and making this provision is beneficial for industry; and
- the inclusion of Immigration services in the Bill has not been canvassed to date, but if/when Immigration does use the framework of the Bill to apply cost recovery, it would need to consult with affected parties as a part of the regulation making process – there is no immediate direct economic impact from the coverage of immigration in this policy.

Some of the policy options identified in this paper may impose additional costs on business compared with the status quo. The inclusion of Immigration has the potential to do this – but the costs would be relatively small and the likelihood of Immigration using this facility in the foreseeable future is low. The shift to a fixed time cost recovery period may add or reduce costs depending on what volume threshold may have been regulated and the numbers of

passengers that depart from the particular airport concerned. There is also an associated competition impact where a new airport would have exceeded the volume threshold within its first year of operation as the policy of a fixed two year cost recovery period would be adding additional cost and thereby reduce competitive ability.

The policy initiatives for this amendment should have no other effects (common law, property rights or innovation compared with the status quo policy position) such that the government would likely require strong analysis and justification.

Further, I have considered the analysis in the attached Regulatory Impact Statement in light of the commitments in the Government Statement on Regulation and I am satisfied that the policy for the time basis for applying cost recovery and the simple approach to a stand-down period for restarting airports is consistent with better regulation, less regulation. The inclusion of Immigration may be questioned in regard to regulatory need, but is a pragmatic inclusion regarding the International Passenger Clearance Funding Bill's design scope.

Chris Baddeley, Policy Manager, MAF Biosecurity New Zealand

[Signature] \_\_\_\_\_

[Date] \_\_\_\_\_

# Status Quo and Problem Definition

## CURRENT SITUATION

The current policy setting for funding of passenger clearance services across Customs, MAF and Avsec was determined under an arrangement made between the previous government and the aviation sector in 2004/05. Under this arrangement:

- **customs** and **biosecurity** services are considered to deliver a public benefit and services at established international airports are Crown funded;
- **Aviation Security Services (Avsec)** are considered to deliver a private benefit (i.e. to those travelling on the aircraft) and are funded by a per passenger fee charged on airlines;
- it is envisaged that costs will be borne approximately 50/50 between government and airlines; and
- **immigration** was excluded from the 2004/05 funding policy, and is currently funded approx 25 percent fees, 75 percent Crown.

The following tables set out the actual current and forecast funding situation.

### Government Agency Passenger Clearance Revenue Projections (\$ millions)

| Source of revenue                     | 2009/10 | 2010/11 | 2011/12 | 2012/13 | 2013/14 | % increase over 5 years |
|---------------------------------------|---------|---------|---------|---------|---------|-------------------------|
| Crown<br>(MAF, Customs, Immigration)  | 71.27   | 77.38   | 78.31   | 78.35   | 78.51   | 10.2%                   |
| Cost recovery<br>(Avsec, Immigration) | 44.44   | 50.85   | 54.73   | 56.85   | 59.36   | 33.6%                   |
| % Crown Funded                        | 61.6%   | 60.3%   | 58.9%   | 58.0%   | 56.9%   |                         |

Source: the respective Government agencies

### MAF, Customs and Immigration Passenger Clearance Net Funding Position (\$ millions)

| Surplus/(Deficit) (\$ million) | 2009/10 | 2010/11 | 2011/12 | 2012/13 | 2013/14 |
|--------------------------------|---------|---------|---------|---------|---------|
| MAF                            | 0       | (0.887) | (1.570) | (2.578) | (3.564) |
| Customs                        | (0.347) | (0.904) | (1.409) | (1.879) | (2.360) |
| Immigration                    | 0       | (0.172) | (0.455) | (0.628) | (0.692) |
| Total Deficit                  | (0.347) | (1.963) | (3.434) | (5.085) | (6.616) |

Source: Border agencies

### International Commercial Air Passenger Number Projections (millions)

|                               | 2009/10 | 2010/11 | 2011/12 | 2012/13 | 2013/14 | % increase over 5 years |
|-------------------------------|---------|---------|---------|---------|---------|-------------------------|
| Total Arrivals and Departures | 8.264   | 8.304   | 8.774   | 9.086   | 9.394   | 13.7%                   |

Source: Ministry of Tourism

## FUNDING OF PASSENGER CLEARANCE SERVICES AT NEW AND RESTART AIRPORTS

The previous Government decided that biosecurity, aviation security and customs services at new international airports and low volume international airports would be funded by cost recovery from airports. Cost recovery would apply for a minimum of one year and until the airport reached a threshold of 9,000 departing international passengers. This was to ensure that the Crown was not exposed to an unlimited and unpredictable liability for providing passenger services at locations where international flights might commence.

To this end, the *International Passenger Clearance Funding Bill* is in draft form, but the Bill has not been finalised for introduction to Parliament. Three outstanding issues are yet to be agreed by Cabinet and require a regulatory impact analysis, namely:

- Cost Recovery: Passenger Volume versus Time;
- Restarting Airports: stand down period; and
- Treatment of immigration secondary processing costs.

### Cost Recovery: Passenger Volume versus Time

The original policy setting allowed for international passenger clearance costs to be recovered at new international airports for a minimum period of one year, and thereafter until the airport reached a threshold of 9,000 departing international passengers. This approach was considered appropriate as it would enable start-up costs to be recovered, and passenger volume was considered to reflect an airport's long term viability for international services. The ability to cost recover from low-volume international airports was seen as offering protection to the Crown from unpredictable and unmanageable demands for rapid deployment of resources at new and restarting airports (CAB Min (05) 13/3A refers)

In June 2009, the Minister for Biosecurity initiated a reconsideration of the 9,000 passenger threshold as it was thought that cost recovery should be based on the actual costs incurred over a commencement period rather than being based on fluctuating and arbitrary passenger volumes. That is, if the objective is to limit exposure of the Crown to an unpredictable liability for providing passenger services at new or restart airports, cost recovery should be based on the costs of commencing passenger clearance services over a fixed period of either one, two or three years.

### Restarting Airports: stand down period

In 2008 Cabinet also considered how passenger clearance services should be funded in cases where international services have completely ceased at a location and then recommence (a restarting airport). The Cabinet directed Customs to consult with the aviation sector on this issue, and report back to the border-Ministers. As a result of this process, Ministers agreed that restarting airports be funded on the same basis as new international airports [Cabinet Business Committee Minute (CBC Min (08) 29/7) refers].

### Inclusion of Immigration New Zealand

Primary processing for immigration is done by Customs at the border and is funded as part of Customs' costs. Immigration New Zealand is responsible for secondary processing which includes interviewing passengers referred by Customs then granting a permit or otherwise. The 2004/05 policy setting for funding of passenger clearance services excluded immigration secondary processing costs on the basis that these were already partially funded through fees (collected from people applying for visas and permits). A subsequent Government decision [October 2006] set the level of the fee/crown funding mix for immigration at 25 percent fee,



75 percent Crown funding. As a consequence of finalising policy for the Bill, the Department of Labour have taken the opportunity to seek consideration of providing for cost recovery for immigration services at new and restart airports.

## INTERNATIONAL PASSENGER CLEARANCE FUNDING BILL

This Bill has been included on the Legislation Programme for several years now. Parliamentary Counsel has prepared three versions of the Bill to date (the first draft was received by departments in May 2009). Work on the Bill's drafting has been on hold awaiting final policy decisions.

The Bill is enabling in that it only provides a framework for empowering regulations to provide for cost recovery. Implementation of cost recovery can only occur when specific cost recovery charges are prescribed in regulations for a particular international airport. The costs that can be recovered are limited by the legislation and there is a consultation requirement for the making of any regulations. At the time any cost recovery regulations are being made, Cabinet papers and a Regulatory Impact Statement would be required and these would be subject to the usual scrutiny of Ministers and departments. The legislation also provides for the ability to exempt, waive and refund charges in whole or part.

## COSTS AND BENEFITS OF THE STATUS QUO

The status quo would involve stopping work on the *International Passenger Clearance Funding Bill* as there is not a comprehensive policy mandate to complete it.

As a consequence there would be no legal means to implement Government's decision to apply cost recovery at new and restart international airports from airport companies for MAF, Avsec or immigration. Whether Customs has a means to cost recover will be assessed by the Judicial Review of its charges at Hamilton airport, scheduled for October 2010.

The likely status quo is that MAF, Customs and Immigration will remain Crown funded and face unmanageable demands for the rapid deployment of resources at new and restarting airports should these occur. Avsec will remain funded from its charges on airlines.

### Costs

It is likely that regional airports will continue to have little regard for the impacts on the border agencies in their decisions to service international flights. Commercial negotiations around such decisions have tended to keep border agencies at arms length and there is a risk that an airport's costing does not capture the costs associated with the border clearance services.

Service demands are likely to increase and this puts pressure on existing services. New regional international services compound cost/resource pressures. As such government agencies will continue to face unpredictable and unlimited liability for the provision of their services.

### Benefits

The benefits of the status quo relate to the costs of border services for customs and biosecurity remaining Crown funded and therefore not impacting on direct costs to airports and international air travellers. It can be argued that if biosecurity and customs costs are cost recovered, the price of travel would rise and there could be some reduction in the number of

tourists travelling to New Zealand, and a loss of tourism revenue. The benefit of the status quo could be said to be a prevention of any reduction in tourists.

The assessment of such a benefit is very assumption dependent and is not quantified.

What we do know is that recent international literature<sup>1</sup> indicates that trans-Pacific international air travel has an inelastic response to price changes. For both short haul and long haul trans-Pacific travel, a 1% increase in price would result in an average 0.4% reduction in the number of travellers. Studies also show that business travellers are less sensitive to price changes than tourists. Studies indicate that the change in the numbers travelling to/from New Zealand because of a small price change would be small, and they also suggest that this is not a permanent impact but is a short lived market response only.

## PROBLEM DEFINITION

The start up and restart of regional international airports creates fiscal and human resource risks for the Crown which generally meets the costs of Biosecurity and Customs passenger clearance services, particularly when there is a number of entry and exists within a year.

**Fiscal risk.** The point of implementing cost recovery for biosecurity, aviation security and customs passenger clearance services at new and restart international airports is to ensure that the Crown is not exposed to an unlimited and unpredictable funding liability.

**Funding gap.** Crown funding does not match the resource need when a new passenger clearance service is required for a regional airport. Neither MAF nor Avsec has a statutory basis to cost recover passenger clearance services from airports, and Customs operates from a cost recovery basis that is currently undergoing judicial review. In the absence of cost recovery for new and restart airports for an initial period, government agencies will be unable to adequately plan for the implementation of new services, which will place pressure on the delivery of those services and existing services.

**Entry and exit of services at regional international airports.** New and restart airports are difficult for border agencies to manage from a funding perspective. Customs, MAF and Avsec have been required to enter, then exit, then restart international passenger clearance services as a result of aviation sector business decisions. Human resource, equipment and logistics costs have been borne by the Crown rather than the aviation sector.

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<sup>1</sup> Air Travel Demand Elasticities: Concepts, Issues and Measurement, October 2008 – Department of Finance Canada

Air Travel Demand – IATA Economics Briefing

Working paper 4: Expected economic implications of cost recovery of passenger clearance services (a summary of economic studies), May 2004 – Funding of Passenger Clearance Services At New Zealand's International Airports in Today's Security Environment: A Government Discussion Document for Key Stakeholders

# Objectives

**Risk management.** To improve the ability of government agencies to manage fiscal and human resource risks around the start up and restart of regional international airports.

**Policy completion.** The broader funding policy for passenger clearance services has been in place since 2005. The detail for new and restart international airports needs finalising so the cost recovery legislation can be completed. Once this is done, the funding policy as originally intended will be implemented.

**Sustainability.** The business decision to start up an international airport should be robust and include all costs, this will reduce the likelihood of the Crown being committed to provide resources to international passenger clearance services that are not viable in the longer term.

**Efficiency.** The funding policy should encourage business and operational efficiency for both the airport and government.

**Equity.** There should be a fairer dealing of the speculative aspect of a start up international airport based on the airport bearing some of the overall passenger clearance service costs.

**Better regulation, less regulation.** Policy preference is for simple and clear solutions where possible.

**Stakeholder management.** Stakeholders have been engaged several times on the matter of funding international passenger clearance services. There is general acceptance of the funding approach for new and restarts, and stakeholders are aware that legislation to implement this is being progressed. An objective is to complete the policy detail of the *International Passenger Clearance Funding Bill* in a timely manner so as not to incur further costs and delays associated with repeating stakeholder consultation.

# Regulatory Impact Analysis

## COST RECOVERY: PASSENGER VOLUME VERSUS TIME

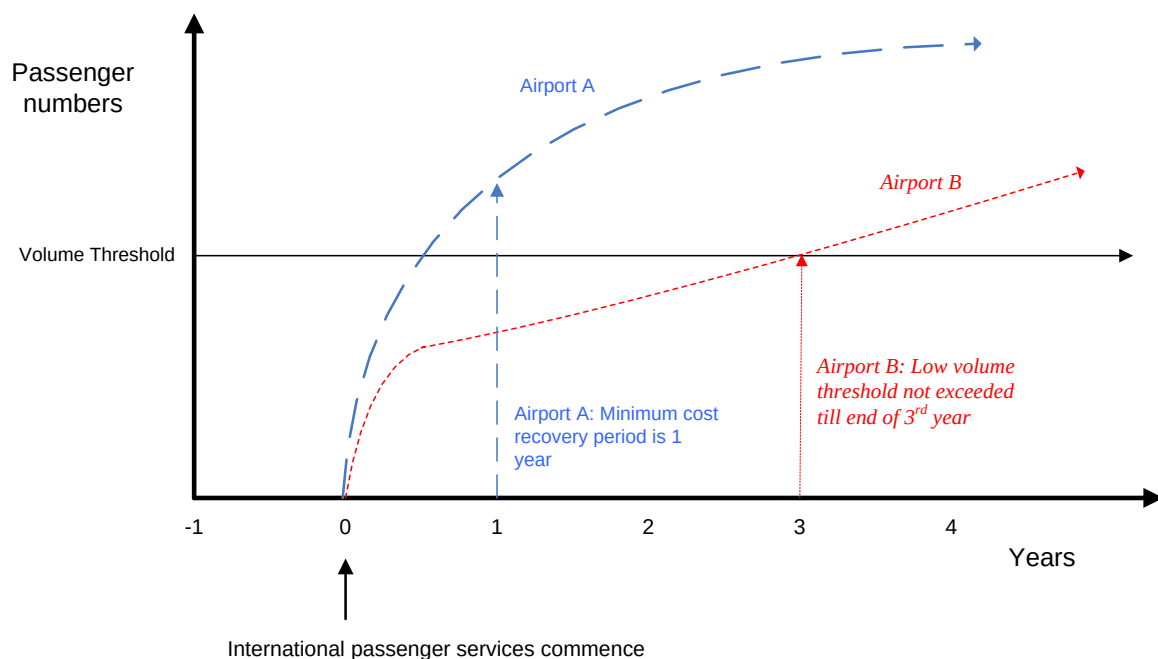
The low-volume concept was promoted by the previous Government. This was on the rationale that:

- there is a higher per-passenger cost of delivery services at airports with a lower volume of passengers;
- it was desirable to place a reasonable limit on the Crown's exposure to costs it has no influence over; and
- to send a price signal to these less unit-efficient airports.

Passenger volume was seen as a measure for indicating the likely ongoing viability of an international airport. The notion was that a low-volume threshold (e.g. 9,000 international passengers departing per annum) would be set and any airport processing less than that number would have biosecurity, customs and aviation security services cost recovered from the airport company.

So the initial cost recovery policy for new international airports was a minimum of one year, plus further time, if needed, to progress through the volume threshold, if ever achieved. The following diagram shows the intended effect. Also if an established international airport went below the threshold for 2 years it would then be subject to cost recovery (this is not shown on the diagram).

Cost Recovery: Time and Volume



- **Airport A:** this example shows that the volume of passengers exceeds the volume threshold after approximately six months at this international airport. In this scenario cost recovery from airport companies for border services would apply for the 1 year minimum and then move to Crown funding (cost recovery from airlines for Avsec).

- **Airport B:** this shows that the volume of passengers does not exceed the volume threshold until approximately the end of the third year at this international airport. In this scenario cost recovery from airport companies for border services would apply for three years and then move to Crown funding (cost recovery from airlines for Avsec).

As agencies debated the volume threshold to be set in law, it became clear that any volume would be inherently arbitrary and provide no certainty either to the Crown or an airport company over when the airport would move to or from the Crown funding (airline funding for aviation security) track. This would be compounded for airports with passenger numbers that vacillate around the prescribed volume threshold.

The pattern of quick entry and exit of international services at regional airports is the principal issue, not volume. This matter was most recently demonstrated at Hamilton Airport. Following the cessation of international services by Air NZ, MAF and Customs proceeded to make staff redundant after consulting the airport – only to have to find new staff to service the airport when services resumed with Pacific Blue only a few months later. The restart followed confidential negotiations between the airline and airport company.

The alternative option considered is a shift from the one year/volume threshold approach to a fixed time period basis.<sup>2</sup>

A sufficient time period is needed for government agencies to recover start-up costs that would bridge the shortfall/lag in Crown appropriation, and also enable some spreading of the fixed costs involved. This may indicate a time period of say two, three or more years. However, if the cost recovery period was too long it would distort the underpinning cost recovery/Crown funding balance. This may indicate a shorter time period of say one or two years. What time period to set is essentially one of judgement.

Weighing up these factors, it is considered appropriate for the legislation to set a maximum cost recovery period that could not be exceeded, but allow for regulations to set a lesser period. It is proposed that the legislated maximum be three years and that regulations set the actual cost recovery period to two years.

Two years is seen as a reasonable balance allowing for the spread of risk between the Crown and airport companies and a spreading of fixed costs, while not being too long so as to distort the basic funding policy.

## Costs

The status quo for the assessment of the impact of this two year fixed time cost recovery period is the Cabinet agreed policy of a one year/volume threshold option.

For those airports that might move through the volume threshold inside two years, there will be additional cost recovery. This cannot be quantified as the volume threshold is a theoretical concept and was never implemented, furthermore the cost impacts would be highly location specific.

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<sup>2</sup> A partial cost recover option (costs per passenger that exceeded the costs of operating at the principal gateway airports) was considered earlier, but not continued with because the expense, complexity and legal risk of partial cost recovery outweighed the relatively small amount of revenue to be recovered.

## Benefits

For those airports that might **not** move through the volume threshold inside two years, there will be the benefit of not incurring an extended period of cost recovery.

The arbitrary nature of the volume threshold, and the concept itself, would lead to budget uncertainty for the airport company and funding uncertainty for government. So a benefit for the fixed time proposal is greater financial certainty for both the airport company and the government.

Additional benefits arise from:

- The compliance costs of administering the cost recovery regime would be reduced as the fixed time approach is simpler and does not rely on the keeping of statistical records. This gives a benefit to both airport companies and government.
- The potential for argument is removed. Arguments could occur around the calculation of the passenger numbers in regard to passing through the threshold and around the longer term trend of passenger numbers.
- The potential compliance costs associated with switching to and from the cost recovery regime at an airport where the passenger numbers move around the threshold is removed.

## RESTARTING AIRPORTS: STAND-DOWN PERIOD

Regional airports usually have only one international airline operator, and because of commercial sensitivities airlines give short notice of service cessation to the airport companies. When an airport company learns that an airline is to cease services, it may endeavour to attract another airline; but there is no guarantee of getting another operator in a timely period, indeed the likelihood would be very low. Despite this generalisation, referring back to the Hamilton example, does demonstrate that an alternative airline can sometimes be found. The shift from Air NZ to Pacific Blue took approximately 14 weeks.

### Option 1: Status Quo

The status quo for this matter is for the *International Passenger Clearance Funding Bill* to strictly treat a restart airport as a new airport and not make any allowance for when only a short stand-down occurs before a replacement airline commences.

The Customs led consultation in 2009 showed that it was the view of many stakeholders that arrangements should be in place for restarting services so that they should not always revert to cost recovery from airport companies. Industry wanted a provision in place to allow airport companies to be able to find a replacement airline within a reasonable timeframe during which border agency services would remain in place. For reasons of pragmatism and fairness it would seem appropriate to provide for a stand-down period during which an established international airport can cease international operations and have them restart without triggering cost recovery from the airport company.

It would be desirable for all parties concerned if there was some arrangement that would encourage government passenger clearance services to be held in place for some period to allow for an alternative airline to restart without major resource changes or funding impacts.

The status quo is not recommended.

## Option 2: Open negotiation

Officials initially considered allowing an open period for negotiation, but it was realised that this could lead to Customs, Biosecurity and Avsec all coming to different arrangements – a very undesirable position for both airports and the Government. So this option was discounted as unfeasible.

## Option 3: three month mandatory stand-down allowing for Ministers to extend a further three months (enabling a six month maximum)

This approach would see the International Passenger Clearance Funding Bill include a provision that set out a mandated stand-down period of three months, allowing for this to be extended once for a further three month period on the request of an airport company. The exact detail of this option was not determined, but an airport company would be able to seek an extension of time based on meeting set criteria. The criteria would require airports to be able to demonstrate that they were in progressive negotiations with an international airline and that they required further time to conclude a deal. Also the detail of how Government's decision would be made was not determined, but it was likely that the law would have placed that decision on the Minister responsible for administering the Act. That Minister would have to meet requirements regarding consultation with the other Ministers/agencies that were affected.

This approach was preferred by some departments on the basis that Ministerial discretion would provide an incentive for airport companies to keep border agencies informed with respect to negotiations.

Working against this option:

- a) this process would create a relatively complex administering provision;
- b) the process itself would open Minister(s) decision to judicial review; and
- c) the process would very likely always default to a six month stand-down period, yet add compliance costs.

This option is not recommended.

## Option 4: a fixed six month stand-down period

This approach would see the International Passenger Clearance Funding Bill include a provision that set out a mandated stand-down period fixed at six months.

This approach is acceptable to all government agencies but is not the preferred arrangement. It provides for simplicity and certainty, however in terms of legislative design this option provides for no future proofing. This option is not recommended because option 5 is seen as marginally better.

## Option 5: Six month maximum stand-down, allowing for regulations to prescribe a lesser period

This is a simple variation on option 4, and in the short term will effectively deliver exactly the same policy outcome: a stand-down period of six months. However, allowing for a lesser period to be prescribed in regulations does add an element of future proofing of this provision should future events around restart airports justify a stand-down period of lesser than six months.

The setting of a lesser period would be subject to stakeholder consultation and the usual scrutiny required for making regulations.

## Option 6: Setting a three month stand-down time period either in the primary legislation or via regulations made at this time

Employment agreements generally specify a redundancy payment of three months salary and it would generally not make financial sense to retain staff for longer than this period if they had limited work activity. Under this option government border agencies would be more likely to retain staff and be better prepared to resume passenger clearance services if an international service was resumed within this time period. Agencies may also face lower redundancy/recruitment costs.

Working against this option:

- a) three months is seen as too short a time for an airport company to negotiate a restart service;
- b) even if negotiations can occur, the mandated time period could place inappropriate pressure on the airport company to reach a deal and therefore distort the bargaining position in favour of the international airline over the New Zealand airport company; and
- c) the length of the stand-down period is not by itself a determinant of whether agencies would retain or release resources. At the time of an international service ceasing, the agencies would need to make a business decision based on their expectations of when services are likely to resume, and this decision is not bound in any manner by the mandated stand-down period.

This option is not recommended.

## Costs

The status quo for the assessment of the impact of a stand-down period is not having a stand down period at all. That is, a restart airport would be treated in the same manner as a new airport and be subject to cost recovery charges.

Industry sought an arrangement that would encourage Government services to be kept in place. No stand-down arrangement can ensure this although the shorter the stand-down period the greater the likelihood that resources would be retained. In all cases, border services management would need to assess the likelihood and timing of a replacement airline, and then weigh up if it would be best in that particular situation/location to retain/redeploy staff, or lay-off staff and recruit/train at the time another international services did commence. It would take similar decisions with equipment and leases.

A potential cost of providing a longer stand-down period is that the agencies may be more inclined to lay-off staff, and should a replacement international airline be found within the stand-down period, then hiring and training costs would be incurred.

A shorter stand-down period may place unnecessary and counter-productive pressure on the airport company – hence weakening the commercial bargaining position of the New Zealand airport with the international airline. Policy should not create a push to enter into ‘flaky’ arrangements that are not in support of long term business sustainability.

## Benefits

The provision of a stand-down period – irrespective of its length – would provide the benefit sought by industry to reduce the impact on the airports’ ability to be competitive and grow. In addition a stand-down period should give an incentive to the airport company to share information with Customs, MAF and Avsec.



The effect of a stand-down period would not govern or limit the business decisions that would need to be taken by MAF, Customs and Avsec with regard to the retention or release of resources. However, if the decisions are based on better information there is more chance that government agencies make the right call. The provision of stand-down period would give some incentive to perhaps retain staff, equipment and leases for a longer period than would otherwise be the case. The benefit, although probably very marginal, is that the costs of unnecessarily laying off staff and recruiting/hiring and training would be avoided (NB: if the decision to retain staff proves wrong, this benefit would become a cost).

The stand-down period alters the restart funding base, keeping customs and biosecurity passenger clearance services Crown funded. The benefit is that this places incentives on the airport company to find a replacement international airline so as not to incur two years of cost recovery for passenger clearance services.

The size of the cost recovery bill to pay government international passenger clearance agencies may not be material significant in the airport's business decision to seek out a replacement international airline, but neither are the costs insignificant. The Customs/MAF costs for an airport the size of Hamilton would be in the order of \$1.5 million over the 2 year statutory cost recovery period [if triggered]. So, on the margin, this would put an incentive on the airport to push an airline to start within the stand-down period.

## CONSULTATION

Stakeholder consultation shows that industry considers that an airport restarting services should not be treated as a new international airport required to undergo a cost recovery funding period. Industry believed this requirement may impact on the airports' ability to be competitive and that these costs are counterproductive to long term aviation growth. Industry wanted a provision in place to allow airport companies to be able to find a replacement airline within a reasonable timeframe during which equipment and infrastructure would remain in place.

## CONCLUSION AND RECOMMENDATION

All agencies accept that to provide for a stand-down period is the preferred policy. Discussions have focused on the length of the stand-down period and the economic impacts of that time period and in particular the degree that any stand-down period affects the business decisions of the agencies to retain or lay-off staff or not.

The stand-down period needs to be long enough to allow commercial air service negotiations to occur. All agencies accept that the stand-down period need not extend beyond six months.

Option 5: six month maximum stand-down, allowing for regulations to prescribe a lesser period is the recommended policy because it establishes a stand-down period acceptable to the government border agencies and allows for future variation if required and justified.

## INCLUSION OF IMMIGRATION NEW ZEALAND

The following text has been prepared by the Department of Labour.

The Department of Labour is responsible for granting permission for non-New Zealanders to enter the country, under the Immigration Act 1987 (to be replaced by the Immigration Act

2009 later in 2010). Primary clearance is undertaken by the New Zealand Customs Service under delegated authority, acting on instruction from the Department of Labour provided via an electronic interface between the two agencies' systems. The Department provides the "secondary" line, when incoming passengers cannot be immediately granted entry permission.

The Department can provide secondary support remotely. However, as the number of airports grows this increases potential funding pressures. These pressures will be augmented as passenger numbers increase as forecast, and would be particularly increased if risk profiles altered. The increased use of wide bodied jets means that even relatively small airports are likely to be able to welcome passengers from further afield into the future.

The tipping point would occur at the point that it became most cost effective from a risk management perspective to station staff physically at airports that were not currently staffed. Lack of resources could mean such a decision was not taken.

That could lead in turn to:

- immigration risk being less well managed (especially if people smugglers identified those routes as easy to get people into New Zealand);
- refugee status claimants being less humanely dealt with (because of for example having to spend days in custody awaiting the arrival of an immigration officer); or
- other travellers awaiting interviews – which could lead to them being granted a permit to enter New Zealand - having to wait considerable lengths of time to be dealt with, resulting in poor facilitation and potentially high levels of dissatisfaction.

Funding for Immigration has not been considered in work to date because of a 2006 Cabinet decision that Immigration border clearance costs be covered by visa fees (25 percent) and direct Crown funding (75 percent). Between Australian citizens and visa-free visitor arrivals (New Zealand offers visa-free entry to the citizens of 55 countries), only around 12 percent of border crossings relate to fee payers. However, those fee payers are relatively high risk from an immigration perspective, which is why they contribute 25 percent of the funding.

That means resourcing is fixed unless new Crown funding is approved, regardless of changes to volumes. In the foreseeable future it is likely that Crown funding will be fixed or will decline.

## STATUS QUO

Currently, passengers arriving at new and restart airports are predominantly New Zealanders – who are not subject to the Immigration Act 1987 – and Australians, who are very low risk in immigration terms.

### Staffing

The Department of Labour has "onshore border" staff posted 24/7 at Auckland airport. Onshore border staff are posted 7am-5pm seven days a week at Christchurch (and provide rostered on call support) and one staff member is posted at Wellington airport. Onshore border staff interview passengers referred by Customs then either grant a permit, formally refuse entry (which may involve housing the passenger until a flight is available) or do not grant a permit but enable the passenger to enter New Zealand (most refugee status claimants).

Other airports are lower risk (largely because they have Trans Tasman traffic only) and are supported through telephone by Auckland, with officers travelling to them for rare issues which cannot be handled over the telephone, such as refugee status claims.

Auckland airport also houses the “offshore border” staff, who support the Advance Passenger Processing system (which checks each incoming passenger against Immigration systems at check in, and instructs the airline whether the passenger can be boarded to travel to New Zealand).

## Funding

The 2009/10 budget for Department of Labour border clearance is:

|               |             |
|---------------|-------------|
| Crown funding | \$3,563,000 |
|---------------|-------------|

|              |             |
|--------------|-------------|
| Fees funding | \$1,187,000 |
|--------------|-------------|

|              |             |
|--------------|-------------|
| Total Budget | \$4,750,000 |
|--------------|-------------|

As noted above, the high proportion of Crown funding reflects the large number of people crossing the border who are subject to the Immigration Act 1987 (non-New Zealand citizens) who do not pay immigration fees in relation to their crossing.

## OPTIONS ANALYSIS

Three major options have been identified.

### Option one: status quo.

This would mean a fixed or reducing budget for passenger border clearance into at least the medium term. All new or restart airports would be supported by telephone as necessary, with physical attendance kept to a minimum. This option is most viable if the number of airports does not increase and passenger risk profiles do not degrade over time.

### Option two: levying passengers to cover the costs of border clearance, including secondary processing.

This would mean that increases in volumes would be fully or partially self funding (depending on the method of calculation, which could vary by airport or be averaged nationwide). It would reduce future calls on Crown funding. It would however mean introducing a new tax, which would not be favoured by the tourism industry.

### Option three: enabling the Department of Labour to bill new and restart airports for certain costs associated with establishing a physical presence at an airport if required.

This functionality might never be used. It would however provide a fall back position should risk profiles alter to such an extent that a physical presence was imperative. It is consistent with the approach agreed for funding start up costs for the Ministry of Agriculture and Forestry and the New Zealand Customs Service.

Other agencies have been consulted and observe that the inclusion of immigration would be inconsistent with the Government statement on regulation through which Government is committed to ensuring that regulation is only used when it is required, reasonable and robust. Immigration New Zealand would be unlikely to use cost recovery in the immediate future, thus agencies are not convinced that the inclusion of immigration in the Bill is required or necessary at this time. Further, Treasury observe that providing for immigration cost recovery also appears to be at odds with the more general decision by Cabinet not to extend cost recovery.

The Department of Labour is aware of previous consultation undertaken by the Ministry of Agriculture and Forestry and Customs regarding the earlier version of the Bill (where agreement to the approach was broadly reached), and of more recent public comments by Hamilton airport, which has now come out against billing by Customs for primary clearance services.

## IMPLEMENTATION

The Department of Labour would only consider establishing a physical presence at a new or restart airport if telephone support was not sufficient and an immigration officer was required to attend that airport on a regular and frequent basis. Such a move would still require reprioritisation within existing budgets and there would be in depth consultation with the airport concerned, and with other interested parties.

## Consultation

The following summary of consultation draws on the historic RISs and Cabinet papers.

### 2004

The policy development for the funding of passenger clearance services was overseen by a *Ministerial Committee on funding of border security* under the chairmanship of Hon Dr Michael Cullen, Minister of Finance. The Ministerial Committee developed a set of proposals on how passenger clearance services at international airports could be funded and implemented.

The proposals formed the basis of the stakeholder consultation document *Funding of Passenger Clearance Services – at New Zealand’s International Airports in Today’s Security Environment* published in May 2004. The RIS assessed the effect of an overall financial cost of border services split between Crown and industry of 50/50. The expected increase in border charges of \$4.16 would result in a 0.3 to 0.8 percent reduction in total tourist and permanent arrivals plus temporary departures.

The 2004 consultation involved two presentations by the Minister of Finance and the initial round of consultation activity (having informed the key set of proposals) was followed by a second round. In both rounds formal written submissions were sought. At that time industry stakeholders were broadly supportive of the proposals although submissions did address some detail by way of “fine tuning”. The consensus among industry stakeholders was that there was no ideal option, yet the agreed position reflected the best solution in terms of the principles that stakeholders were most concerned about. The 2004 RIS went on to report that Wellington Airport and Pacific Blue did not accept that customs and biosecurity should be cost recovered from new international airports.

### 2005

In 2005, Government specifically considered the allocation of aviation security charges across airports. This saw further consultation undertaken with stakeholders and attracted twelve submissions from industry and local government organisations.

## 2006

A consultation document was circulated by the Ministry of Transport to obtain industry views on the issue of low volume airports. Forty-three different groups received a copy of the consultation document including all of the international airports then operating, the larger regional airports, the Board of Airline Representatives NZ, various trade and tourism groups, unions and aviation interest groups. Of note Auckland airport firmly suggested that the 9000 departing passenger volume threshold was too low and would not discourage non-viable airports beginning international services. This consultation confirmed that industry agreed that at all low volume international airports all passenger clearance charges should be collected from the airports rather than the airlines.

It also canvassed matters such as ownership of equipment and sought suggestions on transitional measures for when a low volume airport becomes a high volume airport. This led to the recommendation that a lag time was appropriate on a case by case basis as a transition mechanism.

This consultation was the foundation for a Cabinet paper in August 2007 [CAB Min (07) 29/3A] and following this, drafting instructions for the *International Passenger Clearance Funding Bill* commenced.

## 2008

In 2008, officials reported to the Cabinet Business Committee their findings of a review of the passenger clearance funding regime – the main elements being in place since October 2005. This review was set in place at the time Government took the funding policy decisions in 2004/05 and had the objective of determining whether the funding regime was working as intended. To inform officials, broad consultation with industry based on a published consultation document was the platform for this review. Response to the consultation showed that industry was largely satisfied with the arrangements for international passenger clearance service charges.

Of note, the cost recovery of new and low-volume airports was formally outside of this review as this aspect of the original funding decisions had yet to be implemented. Nevertheless, this report canvassed the need for a specific cost recovery policy for restart international airports and further targeted stakeholder consultation was initiated from this point. This paper considered ‘restart’ to apply where a replacement international airline resumed within a 2-year period of cessation of the original airline and contemplated costs at restart airports would be recovered from airport companies for the first year of the restart service.

The Government agencies consulted were Customs, MAF, Transport (Avsec) and Treasury.

## 2009

On 17 March 2009, Customs issued a consultation document to stakeholders for determining policy for restart international airports vis-à-vis new international airports. Around 70 percent of stakeholders submitted on this issue.

There was consensus among stakeholders that a gap did exist in the current policy and acknowledged that the fiscal consequences resulting from the ceasing of an international service should not fall entirely on the Crown. However, there was some divergence in the

views (of regional airports versus metropolitan airports) as to what the preferred detail of the funding solution should be.

It was the view of many stakeholders that an airport restarting services should not always be treated as a new international airport required to undergo a self funding period. Industry believed this requirement may impact on the airports' ability to be competitive and that these costs are counterproductive to long term aviation growth. Industry wanted a provision in place to allow airport companies to be able to find a replacement airline within a reasonable timeframe during which equipment and infrastructure would remain in place.

Also, a common theme from the submissions was around the need for clarity on what customs and biosecurity costs were involved in a restart situation. Industry accepted that staff costs would need to be covered but raised questions about the extent industry would need to contribute to infrastructure and passenger clearance costs. In an actual situation the border agencies will work with the airport company to plan for a restart.

Of importance, the decision for the cost recovery policy for restart international airports was delegated to the Ministers of Customs, Biosecurity, Transport and Finance. They were given delegated authority to make a final decision and instruct Parliamentary Counsel Office [CBC Min (08) 29/7 refers]. Thus, the stakeholder consultation undertaken in 2009 was only privy to Customs, MAF, Ministry of Transport and The Treasury.

## SUMMARY OF HISTORY

Formal and extensive consultation with stakeholders was undertaken during the development of the cost recovery policy in 2004/05. There have been subsequent discussions with many stakeholders and they are aware that the Government intends legislating to enable cost recovery at new and restarting airports.

As a generalisation, stakeholders are more likely to agree to the higher level approach to the funding solution but hold a variety of views on the detail.

## 2010

There has not been a formal consultation round to specifically support these final policy decisions because:

- the basis for cost recovery has been the subject of various consultations in the past and the shift to have cost recovery apply for a fixed term is a marginal adjustment that will lead to a simpler and more certain funding arrangement – but the fixed term basis has not been specifically consulted on;
- the need for an arrangement to cover restart was covered in the 2009 consultation led by Customs and making this provision is beneficial for industry; and
- the inclusion of Immigration services in the Bill has not been canvassed to date, but if/when Immigration does use the framework of the Bill to apply cost recovery, it would need to consult with affected parties as a part of the regulation making process – there is no immediate direct economic impact from the coverage of immigration in this policy.

In the context of trying to finalise whether the cost recovery for new/restart international airports should be based on volume or time, the question was raised as to the merits of widening such a review to cover all airports. This was the core issue discussed at Cabinet on 19 January 2010 as an oral item. Minister's considered that sufficient industry awareness of

the funding policy existed and that it was not necessary to re-open a formal consultation process for the few relatively minor matters that remained outstanding.

## Implementation

The *International Passenger Clearance Funding Bill* will be the legal instrument to give effect to cost recovery from new and restart international airports for government passenger clearance services.

This Bill is enabling and by itself does not give effect to any cost recovery charges. To implement cost recovery, regulations will be required and the introduction of regulations will require consultation with affected parties by Immigration (if included) Customs, MAF and Avsec.

In regard to the basis of cost recovery being a fixed time of two years and not 1 year/volume based, the legislation will establish a three year default funding period, allowing for regulations to set the lesser two year period. Thus, regulations will be required to give effect to a two year fixed time period and to expedite this arrangement the regulations will be prepared and consulted on in conjunction with the process for passing the Bill. The fixed time approach should reduce compliance costs compared with the status quo.

In regard to the stand-down period the legislation will set a maximum period of 6 months. If it is decided to implement a lesser period regulations will be required.

In all of these areas no specific transitional arrangements are required.

Any future regulations will require consultation with affected parties and will be subject to the usual scrutiny checks and balances. These standard processes are in place to mitigate intervention risks.

## Monitoring, Evaluation and Review

No specific monitoring is planned for the fixed two year cost recovery period or for the stand-down period. These are fixed statutory parameters that will apply when triggered. In the actual new or restart situation agencies will continue to apply appropriate financial/accounting methods and reporting.

Once in place there is no plan for regular or periodic review. Cost recovery is likely to be implemented rarely over the foreseeable future. It is likely that whenever a new international airport starts or a possible restart situation is being handled there will be much policy, business and legal attention given to the *International Passenger Clearance Funding Bill* at those times.