

Commercial in Confidence

Office of the Minister of Transport
Office of the Minister of Finance
Cabinet Development Committee

Covid 19- Airfreight Response

Proposal

1. This paper proposes that the Crown:
 - 1.1. Agrees to an aviation relief package comprising:
 - 1.1.1. The suspension of funding reviews across all aviation and border agencies for the next 12 months;
 - 1.1.2. Government financial support to airlines to pay passenger-based government charges (\$83m GST exclusive)
 - 1.1.3. [REDACTED] and [REDACTED]
 - 1.1.4. Ensuring that government works with the sector and CAA to ensure there is no regulatory impediments to new/re-starting airlines.
 - 1.2. Financial support for Airways New Zealand that would inter alia provide airlines relief from Airways charges (\$107m GST exclusive).
2. The Minister of Finance has already announced an appropriation of \$600m for an Aviation Relief package. The \$270m worth of initiatives in this paper would be funded from this money. Further initiatives will be developed with the sector as we better understand the impacts and potential mitigations and develop up the medium term package.
3. Separate to this, border and aviation agencies and the Treasury are considering the impacts on border agencies of declining passenger numbers in terms of lost revenue and the ability to keep operating and pay staff over the next few months. Those matters are not addressed in detail in this paper.
4. The Government is also undertaking discussions with Air New Zealand.

Withheld
under section
9(2)(f)(iv) of
the OIA

Background

Impact of COVID 19 on Aviation Sector

5. In light of the border restrictions announced on 14 March, Air New Zealand announced that it will be reducing international air services by 85% and domestic services by 30%.
6. Foreign airlines operating services to New Zealand have not yet informed us of all the changes they will be making to their schedules but we anticipate that some airlines will make similar reductions, while many are likely to cease services to New Zealand

for at least a period of time. Several airlines, including Korean Air, have already done so.

7. On 9 March 2020, the International Air Transport Association (IATA) estimated that airlines could lose US\$113 billion as a result of COVID 19. The potential losses will have increased massively over the past week as travel restrictions have been imposed around the world.

Border and Aviation charges

8. Airlines pay charges for a number of services provided by government agencies. These agencies include the Civil Aviation Authority (CAA), the Aviation Security Service (AVSEC), the Ministry for Primary Industries (MPI), the New Zealand Customs Service (Customs) and Airways Corporation of New Zealand (Airways).
9. These charges are based on passenger numbers or flight volumes. If there are increases in passenger numbers agencies collect more money, and if passenger numbers go down they collect reduced revenue. The COVID-19 related border restrictions in New Zealand and overseas have caused a significant drop in passenger numbers. This has meant that the current system of revenue based on passenger number has seen all border and aviation agencies hit with significant and sudden cost pressures as revenue has materially declined.
10. Border and aviation agencies are working collectively with Treasury to find a way to address the decrease in passenger numbers and revenue, and a Cabinet paper outlining the issues and a way forward will be developed for Cabinet consideration in April.
11. Agencies will try to use reserves first, delay infrastructure, cut costs, re-deploy staff where possible and operate efficiently. However, in some cases reserves will not last long and border and aviation agencies will need equity injections to keep operating.
12. [REDACTED]

Relief from Border and Aviation Charges

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The Aviation Sector has asked for relief from border and aviation charges.

13. IATA, the Board of Airline Representatives in New Zealand (BARNZ), Airlines for Australia and New Zealand and Air New Zealand have written seeking relief from the Government to address the significant pressures of COVID-19 on the sector.
14. In summary the request includes:
 - a) Deferral of future increases to fees and levies until the sector has recovered;
 - b) Either waiving charges for the CAA, AVSEC, Biosecurity/MPI and Customs for a period of 6 months or reducing charges by 20% while still ensuring sufficient funding so border and aviation staff can be retained and ready for recovery without charging airlines;
 - c) Considering reductions to the International Visitor Levy;
 - d) [REDACTED]

Withheld under sections 9(2)(b)(ii) and 9(2)(j) of the OIA

- e) [REDACTED]
[REDACTED] Withheld under section 9(2)(f)(iv) of the OIA
- f) Regulatory support for new/re-starting airlines;
- g) Rebates for airport landing charges;
- h) No implementation of blanket staff travel bans by Government agencies.
15. They have also asked for Government to ensure that as many international connections (particularly cargo) are maintained, and that critical specialised skill-sets needed to run the aviation system are protected during an extended downturn, and measures are in place to support system recovery (i.e. wage subsidies and tax relief).
16. Airports have also been significantly hit with liquidity issues which will result in a significant deferral of planned infrastructure, and are likely to seek support from Government, particularly if the aviation impacts go on for a long period of time.
17. We are recommending the following short-term relief package for the sector:
- a) The suspension of funding reviews across all aviation and border agencies for the next 12 months;
- b) Government financial support to airlines to pay passenger-based government charges for 6 months (discussed in more detail below and valued at \$163m GST excl);
- c) Relief from Airways fees (discussed in more detail below and valued at \$107m GST excl)
- d) [REDACTED] and [REDACTED] Withheld under section 9(2)(f)(iv) of the OIA
- e) Working with the sector and CAA to ensure there is no regulatory impediments to new/re-starting airlines.
18. Providing six of financial support to airlines to pay passenger-based government charges will help airlines manage costs for those services they are able to maintain during the current precipitous decline in demand. This may assist some airlines to remain in New Zealand rather than exiting the market altogether.
19. It will also signal the value New Zealand places on these services and may encourage airlines to increase services more quickly during the recovery. For example around the 4-5 month period some services may come back on line, particularly to and from China and Asia. This support (and the commitment to suspending funding reviews for 12 months) may encourage airlines to choose New Zealand early in their return to markets.
20. We consider that six months relief from charges would also be a good signal that the government understands the impact on the sector, and would show commitment to maintaining services and incentive to return earlier.

Mechanism

21. Waiving, refunding or creating exceptions to these charges would require changes to regulations, as the liability to pay is set out in law and the current powers to waive or refund would not cover COVID-19 circumstances. This could take some time to design develop and could have unintended consequences.
22. At this stage, officials' proposed mechanism is to provide financial support to airlines for the full amount of these passenger-based charges. This would be implemented by the Crown reimbursing the airline when those charges fall due to be paid to the relevant agency, or by the Crown paying the amount of the charge direct to the relevant agency on behalf of the airline. The exact process for each charge would be worked out with the relevant agency and the airlines.
23. Airlines are facing severe cash flow issues and mechanisms which maximise the speed with which these refunds are received will be crucial.

Cost to Crown

24. The cost to the Crown of paying fees based on the number of passengers actually travelling is difficult to estimate in the current demand environment.
25. However, given Air New Zealand and other airlines have signalled a 85 to 90% reduction in services, based on 85% reduction in international passenger numbers and 30% reduction in domestic passenger numbers, the cost to the Crown of paying these fees for six months would be approximately \$83 million made up as follows:

	Charge per passenger (all exclusive of GST)	Forecast total charges (based on 85% reduction in international passenger numbers and 30% reduction in domestic passenger numbers)
Civil Aviation Authority and Aviation Security Service – domestic	CAA: \$1.60	\$16,481,000
	AvSec: \$6.33 (averaged based on current rate and regulated change from 1 July 2020)	\$36,098,000
Civil Aviation Authority and Aviation Security Service – international	CAA: \$1.60	\$1,726,000
	AvSec: \$12.30 (averaged based on current rate and	\$14,927,000

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	regulated change from 1 July 2020)	
Customs and Excise Border Processing Levy	\$6.43 for arrivals \$2.56 departures	\$5,015,400 \$1,920,000
Biosecurity Border Processing Levy	\$8.50 for arrivals	\$6,630,000
		\$82,797,400

26. It is difficult to predict when the recovery of the sector will occur. However, the recovery is likely to be slow given the economic impact as a result of the COVID-19, and may start earlier in relation to different countries. If the package above were successful in incentivising return of some services early, there may be a small increase in services from some airlines around 4-5 months into the charge relief period. We have costed another \$80 million into the package for these services to arrive and not have to pay the charges.

International Visitor Levy

27. The International Visitor Levy (IVL), a levy of \$35 per passenger levy that is invested in sustainable tourism and conservation projects. It is not payable by citizens or permanent residents of New Zealand, Australia and most Pacific Islands.
28. We anticipate that there will be very few passengers liable for the IVL travelling to New Zealand in the short-term.
29. Unlike the other charges discussed in this paper, the IVL is paid directly by passengers rather than being paid by, or collected by, the airlines. Relief from this would therefore need different implementation processes.
30. We recommend that consideration of waiving the IVL be included as part of any future tourism recovery package, but not as part of this package as it would not provide real relief or incentives to airlines at this time.

Precedent Risk

31. While providing this financial support for payment of fees and charges will signal to airlines the government is willing to support them, there is a risk that it sets a precedent, leading to other sectors also seeking relief from charges in the current environment (for example tax relief).
32. We consider this could be mitigated to some extent by highlighting that the measures relate to the border and are being instituted to support a sector directly impacted by government decisions around the border, rather than market forces. The government should also signal that the relief from fees and charges is time-limited.

Airways New Zealand

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and 9(2)(g)(i) of the OIA

33. [REDACTED]

34. We propose to provide Airways with \$107 million of financial support. This funding is to provide resources for Airways to operate through the current downturn, enabling it to support airline customers through suspension of the air traffic services charge. This approach to the company would be consistent with, and further strengthen the Crown's Aviation package.
35. We seek delegated authority from Cabinet for shareholding Ministers (Hon Robertson and Jones) and the Associate Minister of Finance Hon Dr David Clark (acting as Minister of Finance for those appropriations in Vote Finance for which Hon Grant Robertson is the appropriation minister) to jointly agree funding of up to \$107 million to Airways, including making the necessary changes to appropriations. Following Cabinet approval, Treasury officials will prepare a paper for Ministers to consider.

Medium-term work relating to the Sector

36. The Ministry of Transport and The Treasury will provide Ministers with further advice on the impacts of the border restriction on critical freight flows such as pharmaceuticals, time-sensitive machinery, and high-value exports, as well as possible interventions the government could take to support certain freight flows.
37. Some of these measures may provide revenue support to airlines offering the services.
38. As stated above some airports will be significantly impacted by the border restrictions. The Ministry of Transport and the treasury will continue to monitor airports ability to seek capital, and whether any intervention is needed as part of the economic response package or through further aviation support.

Next steps

39. If Cabinet agrees to proceed with the short-term package, we recommend that it be announced after Cabinet Development Committee, as the sector are under considerable pressure and want to understand as soon as possible the detail of any relief. Officials will provide further advice following public announcements about the introduction of the scheme, necessary changes to appropriations, and assorted legal matters.

Financial Implications

40. The cost to the Crown of funding this for a period of six months is estimated to be around \$270 million dollars.
41. This paper seeks agreement to delegate authority to relevant Ministers to agree the final funding to be provided and make the necessary changes to appropriations.
42. I note, as per above, there will also be funding pressures faced by border and aviation agencies as a result of decreasing passenger numbers, and that a paper addressing these issues will go to Cabinet shortly.

Legislative Implications

43. The proposed mechanism set out in paragraph 28 above would not require any changes to the existing regulations.

Regulatory Impact Statement

44. In the time available a regulatory impact statement has not been prepared.

Consultation

45. This paper has been jointly prepared by the Ministry of Transport and the Treasury

Recommendations

46. The Ministers of Transport and Finance recommend that the Committee:
- 1 **Note** that border restrictions in New Zealand and around the world have resulted in airlines reducing or cancelling services altogether
 - 2 **Note** that providing financial support to airlines to pay passenger-based government charges would assist some airlines to maintain services which provide vital international connections to New Zealand and would send important signals to airlines resuming services during the recovery.
 - 3 **Agree** to an aviation industry relief package comprising:
 - 3.1 the suspension of funding reviews across all aviation and border agencies for the next 12 months;
 - 3.2 Government provision of financial support to airlines to pay passenger-based government charges for the next 6 months (with an estimated value of \$163m GST excl);
 - 3.3 waiver of Airways fees to airlines as part of a capital injection into the company (see recommendation 6 below);
 - 3.4 [REDACTED]
 - 3.5 ensuring that we work with the sector and CAA to ensure there is no regulatory impediments to new/re-starting airlines.
 - 4 **Direct** officials to further develop details for implementing the package, referenced in recommendation 3 above, and associated legal matters;
 - 5 **Authorise** the Minister of Finance and Minister of Transport to jointly agree further detail relating to the industry relief package referenced in recommendation 3 above, including any necessary changes to appropriations;
 - 6 **Authorise** Airways' shareholding Ministers (Hon Robertson and Jones) and the Associate Minister of Finance Hon Dr David Clark (acting as Minister of Finance in respect of appropriations in Vote Finance for which Hon Grant

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Robertson is the appropriation minister) to jointly agree funding of up to \$107 million to Airways, including the necessary charges to appropriations;

- 7 **Note** that the Ministry of Transport and the Treasury will provide Ministers with further advice on the impacts of the border restriction on critical freight flows as well as possible interventions the government could take to support certain freight flows.

Authorised for lodgement

Hon Grant Robertson Minister of Finance	Hon Phil Twyford Minister of Transport
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