

MINISTERIAL BRIEFING NOTE

Subject	Review of Fullers360 Waiheke Ferry Service Exempt Status – final assessment against the Land Transport Management Act criteria
Date	14 September 2023
Briefing number	BRI-2865

Contact(s) for telephone discussion (if required)				
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Action taken by Office of the Minister

- ☐ Noted
- ☐ Seen by Minister
- ☐ Agreed
- ☐ Feedback provided
- ☐ Forwarded to
- ☐ Needs change [please specify]
- ☐ Withdrawn
- ☐ Overtaken by events

14 September 2023

Hon David Parker – Minister of Transport

REVIEW OF THE EXEMPT STATUS OF THE WAIHEKE PASSENGER FERRY – FINAL ASSESSMENT AGAINST THE LTMA CRITERIA

Purpose

1. This briefing provides Waka Kotahi NZ Transport Agency's final assessment of whether the Fullers360 Waiheke Ferry Service meets the criteria under section 150(2)(b) of the Land Transport Management Act 2003 (LTMA) to remove its exempt status and require it to be contracted to Auckland Transport.

Background

2. On 11 July 2023 we provided you with background information and an update on the Waka Kotahi review of the exempt status of the Fullers360 Waiheke ferry service under section 150 of the LTMA (MIN-4248 refers). The purpose of the review is to determine whether the Waiheke ferry service can, by Order-in-Council, be replaced by a unit or part of a unit to be provided under contract to Auckland Transport (s150(1)(b)).
3. The review was initiated at the request of the previous Minister of Transport who was concerned with how long Fullers360 and Auckland Transport were taking to agree a Quality Partnering Agreement (QPA) for the Waiheke ferry service and that the QPA may not achieve the outcomes the Minister expected to see.
4. Waka Kotahi has been investigating whether the criteria under s150(2)(b) are met such that contracting the Waiheke ferry service under the LTMA is a legally viable option. We engaged a consultant in 2022 to assess whether the criteria had been met and received his report in late November 2022. The consultant concluded that the criteria had appeared to be met.
5. We sought Crown Law advice s 9(2)(h)
[REDACTED]
6. s 9(2)(h)
[REDACTED]
7. To enable us to complete our investigation, we engaged the services of consultants s 9(2)(h)
[REDACTED]

High level conclusion – LTMA criteria have not been met

8. To require an exempt public transport service to be replaced by a unit or part of unit to be provided under contract you must be satisfied that the public transport service:
 - is an integral part of the relevant region's public transport network; **and**
 - needs its fares to be regulated.
9. After careful consideration of the three reports, Crown Law advice and Fullers360's willingness to work with central and local government on delivering concessions to groups that government wishes to assist, we have concluded that:
 - the Waiheke ferry service is an integral part of the Auckland public transport network; **but**
 - there is insufficient evidence to conclude that the service needs its fares to be regulated.

Basis for our assessment

The exempt public transport service is an integral part of the relevant region's public transport network

10. The LTMA does not define or provide guidance on what constitutes an integral public transport service. s 9(2)(h)
11. It is the responsibility of public transport authorities (PTAs)¹ to identify in their regional public transport plans (RPTPs), the services that are integral to the public network(s) that the PTA proposes to provide². Further, PTAs can decline a registration of an exempt service if the PTA has adopted a RPTP and identified the service as integral³.
12. In its 2015 and 2018 RPTPs, Auckland Transport identified the Fullers360 operated Waiheke ferry service as an integral service. In its 2018 RPTP Auckland Transport stated integral exempt services were exempt services that 'provide important public transport connections within the urban area and are integrated with other services in the network'⁴. This description is consistent with the plain meaning of integral.
13. Auckland Transport also stated that if any of the integral exempt services cease to be operated by the relevant operator, Auckland Transport would deregister the service and replace the service with a unit for the purpose of the LTMA⁵.
14. We consider this to be sufficient basis for concluding that the Waiheke ferry service is integral to the Auckland public transport network.

¹ Includes regional councils, Auckland Transport, city councils and unitary councils that provide public transport.

² LTMA, s120(1)(a)(i)

³ LTMA, s134(2)(c)

⁴ <https://at.govt.nz/media/1978732/rptp-2018-2028-final.pdf>, pg 53

⁵ <https://at.govt.nz/media/1978732/rptp-2018-2028-final.pdf>, pg 54

The exempt public transport service needs its fares regulated

15. s 9(2)(h)

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19. Waka Kotahi engaged the services of Sapere and Deloitte consultancies to investigate the s 9(2)(h) We received the final reports from the consultants in early September and have completed our investigation into whether the 'fares need regulating' criterion has been met.

Equity, integration and customer needs

20. In the original report prepared for Waka Kotahi in 2022 the consultant argued that the need to regulate fares should be seen in the context of price regulation more broadly. The consultant argued that the decision to regulate prices is usually first based on the community impact of higher prices, before looking at how prices have been set and to what extent they are justified or could be reduced. Therefore, any assessment of the need to regulate should focus on the community impacts, and not how fares are set, or whether the current prices are reasonable.⁷

21. The consultant investigated three key issues:

- *Relative fare alignment with comparable contracted ferry services* – the consultant argued that Waiheke residents have a reasonable expectation to be treated in a similar way and enjoy the same benefits of other Auckland residents. The consultant concluded that Waiheke residents who do not use the Service daily are required to pay fares significantly higher than what other Aucklanders pay on similar ferry services.

⁶ s 9(2)(h)

⁷ Kidd, B. (2022) *Review of the Exempt Status of Fullers360 Waiheke Ferry Service* p10

- *Level of integration required with the AT HOP system* – fares on the Service are integrated with the AT HOP system and the consultant argued that as this is no longer a barrier it is a contributing reason for removing the exemption.
- *Composition of the customer base* – The Service's customer base is a mix of Waiheke residents, commuters working on Waiheke and visitors. The consultant argued that there was a case for regulating fares for Waiheke residents and commuters to Waiheke as the Service is effectively their only transport option for movement between Waiheke and the rest of the city.

Level of competition in the market

22. Sapere was engaged to complete a high-level assessment of the level of competition Fullers360 faced on the Waiheke ferry route. Sapere's analysis is based on the Commerce Commission approach to assessing competition in a market.
23. Sapere concluded that there is competitive rivalry on the downtown Auckland to Matiatia Waiheke ferry route:
 - There is direct rivalry for short-term visitors between the SeaLink car ferry and Fullers360 passenger services.
 - Aggressive pricing for frequent users on Fullers360 is not matched by SeaLink car ferry and suggests the threat of entry is a factor in this pricing behaviour.
 - There is rivalry for Waiheke as a destination relative to other rival destinations (e.g., other tourism opportunities in the Auckland region).
24. Sapere noted that other operators have entered this market in the past and that some of the previous barriers to entry, including access to berth facilities, have reduced. There are also media reports of at least one other firm (Sea Waiheke) that has developed a proposal for a new ferry service to Waiheke to the point that it will seek resource consent.
25. Residents who travel less regularly appear to benefit the least from the competitive responses of Fullers360 to its other two primary market segments: commuters and short-stay visitors. The one exception to this observation is residents with a SuperGold Card. Residents who have a SuperGold Card travel free all-day except the morning peak Monday to Friday.
26. For the reasons set out in paragraphs 24-25, and the fact that Fullers360 is not making supernormal profits (see below), Sapere advised 'it **cannot** be concluded that the Fullers360 downtown Auckland to Matiatia services operates in a market where there is little or no competition and little prospect of future competition'.

Whether Fullers360's current profit margin for the service is proper or supernormal

27. Deloitte was engaged to investigate whether Fullers360's profits are normal or supernormal and whether Fullers360's pricing methodology for setting fares is an appropriate commercial approach.
28. Because actual revenues from 2019/20 to 2022/23 were abnormally low due to COVID-19, the consultants had to estimate a normalised revenue stream for the 2019/20 to 2022/23 based on 2018/19, which was the last full financial year before COVID-19 hit. The purpose of the exercise

is to determine the level of revenue Fullers360 would have collected during 2019/20 to 2022/23 if COVID-19 had not happened.

29. Deloitte developed a methodology similar to that prescribed by the Commerce Commission for regulated businesses in the energy industry to assess whether Fullers360's profits were normal or supernormal.
30. Using this methodology Deloitte calculated the 'maximum allowable revenue' (MAR) for the Waiheke ferry service for the period 2018/19 to 2027/28. Deloitte then calculated and compared Fullers360's normalised revenue streams against the MAR as set out in Table One. Conceptually, any revenue above the MAR will result in supernormal profits.
31. On the basis that Fullers360's normalised revenues (light green line) were below the MAR (dark green line) Deloitte concluded that the current and previous fares charged by Fullers360 do not generate what could be classified as supernormal profits.

s 9(2)(b)(ii)



32. s 9(2)(g)(i)



Fullers360's approach to setting fares

33. Fullers360's approach to pricing incorporates different methodologies to consider distinct user groups, encompassing both commuters and visitors, who use the same assets. This involves implementing a "Segmented value-based methodology" which assigns differing prices to various user segments based on their travel frequency/purpose.

⁸ A sensitivity analysis was done on the normalised revenue, specifically excluding any factors related to the growth in patronage and price adjustments from the existing fares. Under this scenario, the revenue falls significantly below the MAR.

⁹ The uplift in revenue between FY23 and FY24 reflects the 20% increase to adult peak return fare introduced on 1 July 2023 by Fullers360. A 4% growth rate has been applied from FY25 onwards.

34. For example, Fullers360 one-way and return fares are set with the visitor market in mind. When determining what level to set one-way and return fares, Fullers360 considers s 9(2)(b)(ii)

35. Deloitte concluded that this is a normal commercial approach to fare setting.

Fullers360's willingness to implement concessions for targeted groups

36. Finally, Waka Kotahi considered Fullers360's willingness to work with local and central government to implement concessions for targeted groups like Waiheke residents who infrequently use the ferry services and are on low incomes. Entering into an agreement with Fullers360 to implement a targeted concession(s) is likely to be lower cost, and faster to implement, than entering a contract for the Waiheke ferry service.
37. Fullers360 currently offers the Government's SuperGold card concession and the AT HOP monthly fare for outer harbour ferry services under its Quality Partnering Agreement with Auckland Transport.
38. Fullers360 has also publicly advocated 'for further subsidies with the Government and Auckland Transport, for the specific benefit of the Waiheke Island community to support public transport equivalent fares for Waiheke Island residents and commuters'¹⁰.
39. s 9(2)(g)(i) According to the competition assessment, Fullers360's existing commuter fare products are already aggressively priced for frequent users suggesting that additional financial support from central and local government is required to deliver new lower-priced concessions.

Conclusion on whether the Waiheke ferry service needs its fares regulated

40. The two extra reports commissioned by Waka Kotahi concluded that, while some of the Waiheke ferry fares were high relative to AT HOP ferry fares, they were appropriate from a commercial perspective.
41. While the original report commissioned by Waka Kotahi noted there is a significant difference between Fullers360's one-way and return peak fares and AT HOP fares, it is not a 'like for like' comparison because AT HOP ferry fares are subsidised. According to Auckland Transport's April 2023 Monthly Indicators report, the average subsidy per passenger kilometre travelled was 63 cents.¹¹ When the subsidy is added to the AT HOP fare the gap between the Waiheke fares and AT contracted outer-harbour services is significantly reduced.
42. The Waiheke residents who are currently not well-served by Fullers360's approach to setting fares are irregular users on low incomes who cannot afford the upfront price of many of the commuter products. Fullers360 does offer an off-island return ticket that costs \$33.50 (adult) and

¹⁰ <https://www.scoop.co.nz/stories/PO2307/S00114/fullers360-awaits-final-outcome-of-four-year-government-review-and-waka-kotahis-recommendation-to-minister-of-transport.htm>

¹¹ <https://at.govt.nz/media/1992054/211-auckland-transport-monthly-indicators-report-april-2023-attachment-1.pdf>
p24

\$16 (child) that is significantly cheaper than the standard peak return price of \$59 and \$26 respectively, but travel is restricted to same day travel.

43. On the basis that the threshold to meet the criterion is high and that Fullers360:

- does not operate in a market where there is little or no competition and little prospect of future competition
- is making normal profits and not supernormal profits
- is willing to work with local and central government on implementing targeted concessions

Waka Kotahi does not consider that the second criterion – needs its fares to be regulated – has been met.

44. Based on the consultants' reports and our understanding of Crown Law advice we are confident our conclusions are robust and therefore have not sought further advice from Crown Law as to basis for our conclusion on this criterion.

Conclusion

45. Because both LTMA criteria have not been met as required under section 150, Waka Kotahi does not consider it is legally possible to use the Order-in-council process under section 150 to change the exempt status of the Waiheke ferry service.

46. s 9(2)(h)

47. Given that Waka Kotahi considers that the criteria have not been met there is little merit in investigating these additional issues at this time. Waka Kotahi therefore advises its review is complete.

Next steps

48. Our next step will be to inform stakeholders of our conclusion, that Waka Kotahi will not be making a request, and that its review under section 150 is now complete. We are finalising communication material in preparation of further queries from the media and public and plan to release a media statement on the Waka Kotahi website once we have confirmed with you how you wish to handle publicity on the Waiheke review.

It is recommended that you:

1. **Note** that Waka Kotahi has completed its investigation into whether the Fullers360s Waiheke passenger ferry service meets the criteria set out under s150(2)(b) of the Land Transport Management Act 2003 (LTMA).
2. **Note** that Waka Kotahi has concluded that the first criterion – the Waiheke ferry service is an integral part of the Auckland public transport network – has been

met but that the second criterion – the Waiheke ferry service needs its fares regulating – has not.

3. **Note** that due to the second criterion not being met, Waka Kotahi does not consider that the Waiheke passenger ferry service can lawfully have its status changed by Order-in-Council and Waka Kotahi will not be making a request under s150 of the LTMA.
4. **Note** that Waka Kotahi considers its review of the exempt status of Fullers360 Waiheke passenger ferry service complete.
5. **Discuss** with Waka Kotahi officials who will lead on communication with stakeholders and the public on the outcome of the Waiheke ferry service review.



Chris Bunny

General Group Manager, System Leadership

Hon David Parker, Minister of Transport

Date: 2023

APPENDIX ONE – s 9(2)(h)

s 9(2)(h)

Proactively Released