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**Busselton Margaret River Regional Airport
Post Project Governance Review
Final Report
City of Busselton**

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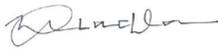
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Executive Summary

The Busselton Margaret River Regional Airport (BMRRA) is currently owned and operated by the City of Busselton (the City), and is undergoing a \$70 million upgrade which has been funded by Federal, State and Local governments. The Airport is strategically positioned as a gateway to the South West region of Western Australia, and the upgrade project has the overarching objective of enabling economic and social growth within the region.

This review, conducted by Aurecon and reporting to the Project Governance Committee, assessed options comprising:

- Continued local government ownership and operation utilising service contracts
- Management contract
- Corporatisation
- Asset lease or divestment.

The review concluded that, at this time, the optimum governance model for BMRRA is for continued management by the City of the airport upgrade and operation because:

- The airport will be more valuable with a few years' demonstrated patronage growth.
- The current Council team has the expertise to manage the delivery of the upgrade and incentive to increase patronage growth.
- Regular passenger transport through the airport is effectively a start-up business, which is better managed within the 'incubator' environment of the Council.
- The airport has greater economic value to the region in terms of increasing tourist numbers than value of passenger landing fees, especially in earlier years of operation.

Airport management should be reviewed when the following conditions are triggered:

- Two years post opening
- Earlier of five years post-opening, annual patronage of 250,000 passengers and/or earnings before interest, taxes, depreciation and amortisation (EBITDA) of \$3.5 million
- Ten years post opening.

The assessment framework that has been developed is intended to be applied in the future assessments to ensure a consistent approach to determining the optimum governance model for BMRRA at these trigger points.



Contents

1	Overview	0
2	Assessment framework	2
2.1	Definition of draft criteria	2
2.2	Consultation with key stakeholders	2
2.3	Revision of criteria based on consultation	5
2.4	Identification of assessment considerations	5
2.5	Development of performance measures	6
3	Governance models	7
3.1	Continued local government ownership and operation	7
3.2	Contracts for service	8
3.3	Management contract / Operating lease	8
3.4	Corporatisation	9
3.5	Asset lease or divestment	10
4	Governance assessment	12
4.1	Assessment	12
4.2	Summary of recommended option	16
5	Future assessment and funding	17
5.1	Trigger Points	17
5.2	Future Funds	17
6	Recommendations	19

Tables

Table 1	Draft criteria	2
Table 2	Final criteria	5
Table 3	Assessment considerations	6
Table 4	Performance measures	6
Table 5	Detailed assessment	13
Table 6	Future governance reviews	17



1 Overview

The Busselton Margaret River Regional Airport (BMRRA) is owned and operated by the City of Busselton (the City). The airport is strategically positioned as a gateway to the South West region of Western Australia, and the impending major infrastructure upgrade to BMRRA has the ultimate objective of advancing economic and social growth within the region.

Funding the development of BMRRA

To enable operation of direct domestic interstate services to Busselton and support regional growth, State Government funding for the proposed \$59.95 million expansion of BMRRA was announced in June 2015. This significant project has been made possible by the financial investment of:

- \$45.9 million from the State Government allocated through the Royalties for Regions program which is administered by the Department of Regional Development
- \$10 million through the Department of Transport's Regional Airport Development Scheme
- \$3.5million from the City of Busselton
- \$300,000 from the South West Development Commission
- \$250,000 from Tourism Western Australia.

A further \$9.78 million of funding was later announced by the Federal Government to support subsequent phases of the development project. Through combined State and Federal Government funding it is anticipated that the City will be able to leverage general aviation and freight opportunities, in addition to expanded Regular Passenger Transport (RPT) opportunities.

The requirement for a governance review

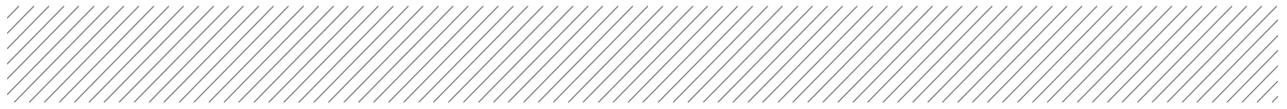
The Financial Assistance Agreement (FAA) between the State and the City which relates specifically to the funding administered by the Department of Regional Development, requires that the City undertake an independent review of the post-project governance arrangements for BMRRA. To ensure that the review is constructive and delivers the greatest ongoing value for the airport, a robust assessment framework will be developed, to evaluate all available governance structures. This framework will be applied now, and revisited as identified milestones and strategic operational metrics for BMRRA are achieved.

Advantages, disadvantages and risks associated with a range of available management and operating options will be considered as part of the review. This will enable the most efficient and economically viable model to be identified, which will support delivery of the development project goals and objectives. We believe that this review presents a great opportunity for the City to leverage insights of key stakeholders and implement a governance structure which maximises the future value of BMRRA.

Governance review scope

The review was conducted through a three-stage process which included:

- Stage 1 – Development of criteria against which future governance models would be assessed
- Stage 2 – Assessment of governance model types against the criteria developed in Stage 1
- Stage 3 – Consideration of proceeds resulting from any change in governance structure.



This Report presents the assessment framework, governance models considered, the assessment outcomes and future considerations, all of which were informed by the outcomes of consultation with key stakeholders.

2 Assessment framework

The assessment framework that was applied to determine the optimum governance model for BMRRA was developed through the following process:

- Definition of draft criteria
- Consultation with key stakeholders
- Revision of draft criteria based on consultation
- Identification of assessment considerations
- Development of performance measures.

These steps are further described in sections 2.1 to 2.5 respectively.

2.1 Definition of draft criteria

Aurecon developed draft criteria for the governance assessment, based on past experience working with other regional airports and a preliminary understanding of BMRRA operations, management and the development project. Table 1 shows the draft criteria.

Table 1 Draft criteria

Criterion
a) Ability to deliver operational efficiency and revenue growth
b) Capacity to increase visitor numbers
c) Ability to grow the airport traffic, and in turn, growth for the region's tourism industry <ul style="list-style-type: none">i) Capacity to attract low cost air serviceii) Improved financial returns to Council, in terms of a lease rental income and possible upfront payment for lease acquisition
d) Capacity to fund capital expenditure for required landside and airside infrastructure and potential land development
e) Political considerations of which community acceptance is the main consideration
f) Regulatory framework, specifically compliance with safety regulation by CASA
g) State Government Public Private Partnership (PPP) guidelines compliance.

2.2 Consultation with key stakeholders

Relevance of the draft criteria was discussed with the identified key stakeholders:

- City of Busselton Council, Chief Executive Officer and senior management
- Department of Transport
- Department of Treasury
- Department of Regional Development
- South West Development Commission.

Consultation included targeted discussions with each stakeholder over a three day period, from Tuesday, 20 September to Thursday, 22 September 2016. Tourism WA was contacted during the consultation period but the key contact person was unavailable to provide review and input. The



discussions focused on confirmation of the objectives, requirements and constraints associated with potential governance options for BMRRA, as well as identification of key features and opportunities that could be leveraged to deliver increased regional benefits.

Core themes and topics relevant to potential governance models, which emerged through the consultation process, included:

- **Current BMRRA governance**

The City of Busselton Community and Commercial Services business unit is responsible for management and operation of the BMRRA. The current structure applies basic commercial principles to separate financial performance, and provide clear accountability and autonomy of personnel from the City who support management and operational functions at the airport. The State Government Business Case and project delivery to date is considered to have been well managed within the current model.
- **The State Aviation Strategy**

The strategy recognises the potential mismatch which often exists between regional aviation infrastructure demands and the funding capacity of local governments. Alternative governance models to local government ownership and operation are considered, and where improvements in the effectiveness and efficiency of an airport can be achieved through private sector investment or management, this model will be encouraged.
- **Regional economic development**

A core objective of the development project is to facilitate regional economic development by enabling air access to the region, which will support tourism and other industries. Any reduction in passenger charges or landing fees, which could enable air travel to become more attractive, would reduce revenue for the airport operator.
- **Financial sustainability**

The ratepayer base of Busselton (~15 000) will have a limited ability to sustain the increased operational and maintenance expenditure of the upgraded BMRRA over an extended period without RPT services. There needs to be an appropriate emphasis on maximising the utility of the airport to support operations, maintenance and development of airport infrastructure.
- **Organisational capability and capacity**

The risks associated with the development project require an appropriate depth of management expertise to respond to the changes necessary to ensure successful outcomes for BMRRA. Commercial returns and levels of productivity will be underpinned by professionals with experience specific to the defined commercial objectives of the airport. Noting that operation and management of the airport is sourced from within the Community and Commercial Services business unit, this allows the City to leverage resourcing and administration efficiencies through broader economies of scale.
- **Local government processes**

It is important to ensure that management is sufficiently nimble to be able to respond to airlines in a manner that facilitates commencement and retention of RPT services. Requirements of the *Local Government Act 1995*, associated regulations and political pressures relating to BMRRA operation and management processes may constrain the current model of local government ownership and operation.
- **Other aviation-related opportunities**

In addition to opportunities associated with passenger and commuter transport, the BMRRA development project offers potential to leverage freight and general aviation opportunities which encompass aviation-related business potential of the land surrounding the airport. Export volumes through BMRRA of 120 tonnes per week were estimated in the RPS Air Freight Viability Study (2016) and a number of producers were identified in the region with interest in exporting to Asian destinations.



- Understanding private sector opportunities

Recent asset transactions within Australia recognise a demand for opportunities that offer a history of demonstrated, stable returns and attractive growth projections. BMRRA, as a developing brownfield asset, will not currently offer the established incentives and value that would be attractive to potential private sector investors. Furthermore, BMRRA offers monopoly air access to the South West region, and it will be important to understand and appreciate the opportunity and associated transaction drivers.

- Regulatory considerations

Corporatisation of BMRRA was identified to offer a number of benefits associated with minimisation of legal liability and financial risk, and increased commercial and corporate expertise through establishment of an independent board of directors (Board). However, section 3.60 of the *Local Government Act 1995* states that “a local government cannot form [...] an incorporated company or any other body corporate.” An amendment bill was recently discharged, which if passed, would have enabled two or more local governments to form a regional subsidiary.

Additional regulatory considerations relating to noise management specific to BMRRA, which is administered by the Environmental Protection Agency (EPA), and general airport safety, which is administered by the Civil Aviation Safety Authority (CASA), were identified.

- FAA restrictions

Clause 5.10 of the FAA specifies a 10 year post project timeframe before sale, transfer, lease or disposal of the BMRRA may occur, unless consent is provided by the Department of Regional Development as the State department responsible for provision of the majority of funding. Noting that the project has the overall objective of facilitating economic and social development in the region, this clause was included to ensure that the State investment is not diverted for a different purpose.

The findings of the Review were presented to the Project Governance Committee on Monday, 28 November 2016. The Project Governance Committee identified the following changes to the final criteria and governance assessment:

- Access to capital

The ability of an airport owner or investor to access capital is critical to future development of the airport. The final criteria defined in Table 2 specifically highlight the importance of access to capital, particularly in relation financial sustainability of the future governance model. Through the assessment defined in Table 5 the comparative strengths and weaknesses of the respective governance options have been identified.

- Financial return on airport investment

The list of final criteria defined in Table 2 was revised to ensure the financial return on investment by Local, State and Federal governments was appropriately prioritised.

The ability of the private sector to grow the airport revenues post-project, does not directly relate to the financial return on airport investment that would be realised by the City should an asset divestment process be pursued post-project. The risk profile associated with unrealised passenger and revenue projections would significantly reduce the asset value despite comparative advantages that are typically recognised by a private sector investor in relation to revenue growth – at least until there is a clear record of growth in passenger numbers.

- Airport operations

The City and the South West regional economies will benefit from effective operation of the BMRRA assets. The private sector is often able to leverage broader operations and specialist expertise to deliver optimised and enhanced outcomes. Airport operations are typically improved through operational efficiencies. This has been identified as part of the final criteria defined in Table 2.

- Financial performance

The private sector often places a considerable emphasis on financial performance, in contrast to government which is required to consider a broad range of objectives prioritised by the communities that it represents. The governance assessment defined in Table 5 highlights the commercial nimbleness associated with private sector decision making which typically enables more rapid responses to market conditions and improved financial outcomes.

These features have been appropriately considered as part of the governance review.

2.3 Revision of criteria based on consultation

Updates to the draft criteria were informed by the outcomes of consultation, which are summarised in section 2.2. The final draft criteria which were applied during the Stage 2 governance assessment are defined in Table 2. The performance of identified governance models, at a particular point in time, can be assessed based on the ability of each model to meet the respective criterion.

Table 2 Final criteria

Criterion
a) Increase in Airport usage to facilitate regional economic development <ul style="list-style-type: none"> i) Commuters ii) Visitors (RPT, ideally low cost air services) iii) Freight iv) General aviation.
b) Airport operations, including operational efficiencies
c) Financial return on public investment
d) Financial sustainability of the Airport including asset management and access to capital to support asset requirements
e) Organisational capability and capacity
f) Community acceptance
g) Compliance with the <i>Local Government Act 1995</i> and State government funding provisions, e.g. FAA
h) Compliance with regulatory frameworks, e.g. noise management regulation (EPA) and safety regulation (CASA).

Combined with the assessment considerations and performance measures described in sections 2.4 and 2.5 respectively, the final criteria form the assessment framework.

2.4 Identification of assessment considerations

Insights provided by key stakeholders and background information provided by the City were further synthesised to identify a number of assessment considerations specific to each criterion, which informed the governance review. These assessment considerations are provided in Table 3.

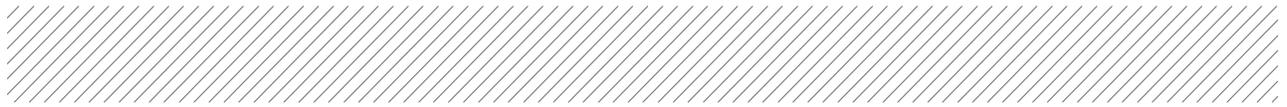


Table 3 Assessment considerations

Criterion	Assessment considerations
a) i) ii) iii) iv)	<ul style="list-style-type: none">Traffic forecastsRealised traffic results
b)	<ul style="list-style-type: none">Financial projectionsFinancial performanceOperational performance
c)	<ul style="list-style-type: none">Realisation of passenger and revenue projectionsIncrease in asset value
d)	<ul style="list-style-type: none">Asset managementOperating expenditure including corporate overheadsRevenues
e)	<ul style="list-style-type: none">Corporate expertisePersonnel capabilityResourcing requirements
f)	<ul style="list-style-type: none">Political landscapeCommunity benefits
g)	<ul style="list-style-type: none">Relevant policies and regulationsAmendments to the <i>Local Government Act 1995</i>Cost of compliance
h)	<ul style="list-style-type: none">Noise management restrictionsRelevant policies and regulationCost of compliance

Combined with the final criteria and performance measures described in sections 2.3 and 2.5 respectively, the assessment considerations form the assessment framework.

2.5 Development of performance measures

The performance measures defined in Table 4 were also developed based on the outcomes of stakeholder consultation, and when collectively applied with the final criteria and assessment considerations form the overarching assessment framework that was applied in section 4.

Table 4 Performance measures

Rating	Definition
5.	Greatest potential to deliver the criterion
4.	Good potential to deliver the criterion
3.	Moderate potential to deliver the criterion
2.	Limited potential to deliver the criterion
1.	No potential to deliver the criterion

These measures were applied during the Stage 2 assessment, and qualifying text has been provided to emphasise the advantages, disadvantages and risks associated with each governance option.



3 Governance models

The following governance models were identified for further consideration during Stage 2:

- Continued local government ownership and operation
- Contracts for service
- Management contract
- Corporatisation
- Asset lease or divestment.

These options are defined in sections 3.1 to 3.5 respectively, with assessment of the identified governance options presented in section 4.

3.1 Continued local government ownership and operation

Like the vast majority of regional airports and aerodromes throughout Australia and ten of Western Australia's 12 larger regional airports, BMRRA is owned and operated by local government. BMRRA The current model of local government ownership and operation integrates BMRRA functions as part of the City's Commercial Services business unit. This model enables the City to leverage economies of scale and reduce airport management costs through partial allocation of City resources, whilst separated reporting for BMRRA maintains transparency of airport performance through explicit recognition of costs.

At present, BMRRA generates a positive, but not significant, annual net operating profit. Therefore State funding of the development project has been critical to enabling this major infrastructure upgrade. By leveraging synergies and efficiencies within the Commercial Services business unit, the City has been able to apply the necessary business expertise to develop the BMRRA opportunity and improve the use of available assets. The City has been successful in attracting professionals with relevant aviation experience to support the commercial objectives of the airport, the development project and broader City operations.

Furthermore, to increase post-project airport usage and realise the demand projections that underpin the business case for investment in the upgrade of BMRRA, the City is currently working with specialist aviation advisors to develop and execute a strategic approach to airline engagement. It is noted that airline engagement would typically commence within a 9-12 month period prior to airport infrastructure becoming available, and the City has been proactive in its approach to securing (interstate) RPT services.

This comparably low-cost structure is considered to be an effective incubator to support development of post-project airport operations and actively drive achievement of the proposed passenger projections. However, there are a number of limitations associated with the current local government ownership and operating model, which include:

- Extensive requirements for operational oversight and monitoring
- Restrictive capital funding processes defined in section 6.21 of the *Local Government Act 1995*, which prevent the use of local government assets as security for debt
- Political influences impacting day-to-day operation and strategic management of the airport
- Prescriptive decision making processes constraining commercial agility
- Reduced capacity for Commercial Services business unit personnel to support other City initiatives.



A number of these limitations are a direct result of *Local Government Act 1995* provisions.

3.2 Contracts for service

Through contracts for service an external provider is engaged to deliver specified tasks or services for an agreed period of time. This model is in place to an extent at BMRRA, with ground handling, security screening and AVGAS refuelling services currently outsourced.

Contracts for service are most effective where:

- The service can be clearly defined
- The level of demand is reasonably certain
- Performance can be easily monitored
- Attracting capital investment is not an objective.

The application of this model allows the City to outsource ancillary services, where service providers are incentivised to achieve improved efficiencies and higher sales.

A governance option of continued local government ownership and operation utilising service contracts was identified for assessment in section 4.

3.3 Management contract / Operating lease

A management contract / operating lease expands on the services currently contracted at BMRRA to encompass management and operation of the airport. Typically, the private partner delivering the contract provides working capital under this model, but no financing for investment.

Examples of management contracts include a number of airports managed by Aerodrome Management Services Pty Ltd (AMS)¹, including:

- Barrow Island, where AMS provides a variety of services on the airport including management, ARO, ground handling, emergency management support, check-in and screening. The workforce currently numbers 38 people, making it the largest of the AMS regional bases.
- Weipa Airport, which has been managed by AMS since 1 June 2012 with a staff of 16 local personnel covering airport reporting, security screening and aviation refuelling. Weipa Airport mainly services QLink Dash 8 fleet, Skytrans and GA aircraft movements with the Royal Flying Doctor Service and Customs being very regular visitors.

- Miles Aerodrome, which is situated approximately 45 k's from the town of Chinchilla on the Leichhardt Highway. A major expansion of the aerodrome began in 2013 to meet the needs of the coal seam gas industry, culminating in the construction of a new terminal which was completed in February of 2016, the result of a \$30 million investment by Origin. The aerodrome caters for circa 2500 pax per month and accepts various aircraft types, including Fokker 28 – 70, Bae 146-200, de Havilland Q200/300/400, SAAB 340TW, ATR72-500/60 series A/C, Embraer 135 & BJ600 series A/C, airline operators include QantasLink, Virgin Regional, REX, Corporate Air and Skytrans, with ground handling provided by Arrow Airport Services & Aviation Ground Handling.

Chinchilla Aerodrome has benefitted from a considerable \$5 million dollar investment. CASA certification was obtained in August 2015 and the aerodrome caters for FIFO, general aviation and agricultural operations. Passenger movements are currently recorded at circa 1800 per month.

AMS commenced management of the aerodromes on the 1st of October, on behalf of the Western Downs Regional Council.

¹ <http://www.amsaustralia.com/service/management-support-services/>, accessed 4 December 2016



AMS is based in Perth².

The key advantage of the operating lease model is that operational gains, which typically result from private sector management, can be made without transferring ownership of BMRRA to the private sector. Other strengths of this model include:

- Designated professional management with specific and relevant experience
- Efficiencies associated with operating on conventional commercial terms, otherwise limited by provisions in the *Local Government Act 1995*
- Limiting financial and legal risks to the City associated with airport operation
- Separation of political influences from airport operations
- Broad political oversight through contract provisions, which ensure operating strategy is incentivised to support regional priorities
- Establishment of a consistent and reliable annuity stream
- Availability of City resources to focus on other local initiatives.

Whilst the ultimate obligation for service provision would remain with the City, this model transfers daily management control and authority for the airport to the private partner. Key weaknesses of this model therefore include:

- Risk of the contractor failing to meet obligations, leading to community dissatisfaction
- A requirement for ongoing monitoring of performance to ensure contractual conditions are met
- Financial risks associated with asset capital requirements that would need to be met by the City.

A governance option of management contract was identified for assessment in section 4.

3.4 Corporatisation

A corporatisation process aims to increase commercial focus, efficiency and transparency of a local government business whilst minimising financial risk and avoiding conflicts of interest through the establishment of a separate legal entity, a Council controlled organisation (CCO), governed by an independent Board.

Adoption of a corporatised model would enable the City to retain ownership and continue to provide strategic direction for BMRRA by setting key financial and non-financial performance targets for the Board to deliver. However, the *Local Government Act 1995* contains a number of provisions that currently limit the City from adopting this model and operating on normal commercial terms, specifically section 3.60.

A bill to amend to the *Local Government Act 1995* and enable two or more local governments to form a regional subsidiary was introduced in June 2014. This bill did not gain parliamentary support and was discharged in October 2016 under Standing Order 144A.

If changes to the *Local Government Act 1995* were implemented in future, corporatisation of BMRRA would offer a number of additional benefits, including:

- A greater emphasis on commercial performance including an increased ability to diversify revenues and improve cost controls
- Increased transparency of performance through standalone reporting with more explicit recognition of costs

² <http://www.amsaustralia.com/about-us/>

- An ability to limit political influences on day-to-day operational decisions, whilst retaining political oversight of BMRRA strategy through the implementation of performance targets and metrics
- An enhanced ability to employ professional directors and managers with experience specific to the commercial objectives of the airport
- Releasing City resources, who would otherwise be allocated to airport activities, for other initiatives of value to the community
- Separation of the City and its ratepayers from legal liability and financial risks relating to airport investment and operating activities
- An ability to engage with the private sector on conventional commercial terms
- Establishment of an ongoing annuity stream through dividend payments from the corporate entity.

Whilst there are a number of benefits associated with corporatisation, capital funding processes and reporting requirements imposed by the *Local Government Act 1995* would continue to limit the commercial agility of the Board and airport management. The following additional limitations would also need to be considered:

- Loss of City control of fees and charges, resulting in possible price increases that might deliver positive commercial outcomes as the expense of regional economic development
- Failing of the Board and airport management to achieve targets set by the City, resulting in community dissatisfaction
- Additional management and administration costs incurred through increased reporting processes and remuneration requirements, with marginal financial upside from a City dividend perspective.

Notwithstanding these limitations, a governance option of corporatisation was identified for assessment in section 4. It is important to note that while this option was considered further, it cannot legally be pursued under the *Local Government Act 1995*.

3.5 Asset lease or divestment

The State Aviation Strategy identifies a preference for private sector investment in, and management of, regional airports to improve effectiveness and efficiency by addressing limitations associated with:

- Restrictive capital funding processes that rely on general funds, rates and grant income for security
- Non robust management arrangements and insufficient depth of governance
- Lack of flexibility to act commercially in areas of charging and industrial relations
- A local government's capacity to support the aviation requirements of major users and state economic growth, beyond the needs of local community.

Potential privatisation options for BMRRA include:

- A long term asset lease, encompassing the site
- Permanent divestment of the airport land and assets including existing operations.

An asset lease is typically provided in exchange for an upfront or annuity payment, of an amount less than that associated with a divestment process. In line with the lease of federal airports and more recently the Port Hedland airport, it is anticipated that a lease period of approximately 50 years would be considered with a 50 year option. Under this model the City would establish performance criteria for the operator such as improvement of the assets and growth of the business that would be monitored and audited on an ongoing basis during the lease.



By way of example, the lease of Port Hedland International Airport to the consortium of AMP Capital and ICG in 2015 included an upfront payment of \$165 million to the Town of Port Hedland and a further investment of \$40 million to redevelop the airport.

Similar to an asset lease, an asset divestment process typically incorporates divestment of the land as an upfront or annuity payment. Under this model the City would transfer all commercial interest in the airport and maintain no further involvement in ongoing operations beyond that of a key stakeholder. Community acceptance of this model is often low as, unlike an asset lease, there is no retention of ownership. Broome International Airport has undergone transition from government to private operations through an asset divestment process. Freehold title of the Broome International Airport site was transferred to Airport Engineering Services in the early 1990s through a divestment process facilitated by the Federal Government. The airport continues to be privately owned and operated.

Through a privatisation process, the City would be able access large institutional infrastructure investors with experience and expertise relevant to airport management and financing. These companies often have an ability to:

- Access cost effective debt and equity funding and financing sources
- Leverage scale and efficiency to increase productivity and optimise commercial returns
- Deliver safer airport operations through an enhanced network approach to regulatory compliance across a portfolio of airport operations
- Source greater depth and diversity of management expertise through broader airport operations and existing industry partnerships
- Respond to local or regional priorities through established local teams
- Ensure best practice governance oversight and commercial decision making through robust corporate governance structures.

Potential issues and limitations associated with privatisation of BMRRA include:

- Complexities associated with the privatisation process and documentation, which requires support from specialist transaction advisors such as financial, legal and probity
- A risk that the airport investor fails to appropriately manage operations resulting in poor regional development and community outcomes
- A requirement for ongoing administration, if an asset lease is pursued, to ensure that the airport operator is meeting the defined performance metrics
- Increases in charging for services and facilities, if provisions to manage this are not specified as part of the contractual documentation

In addition to the identified issues, privatisation of BMRRA in the short term is expected to represent lesser value for the City than other governance models, as significant uncertainty is associated with unrecognised passenger and revenue projections. Institutional investors typically prefer to focus on OECD brownfield assets with a history of demonstrated and consistent revenues.

Without established and reliable returns, privatisation of BMRRA would require that investors take a calculated risk. It is anticipated that the considerable risk profile associated with achievement of the passenger demand projections would ultimately result in a risk-adjusted price that does not accurately reflect the potential value of the asset.

Despite concerns relating to privatisation of BMRRA in the short term, a governance option of asset lease or divestment was identified for assessment in section 4.



4 Governance assessment

4.1 Assessment

The assessment framework defined in section 2 was applied to evaluate the following governance options, which are based on the models presented in section 3:

- Option 1: Continued local government ownership and operation utilising service contracts
- Option 2: Management contract
- Option 3: Corporatisation
- Option 4: Asset lease or divestment

The identified options were assessed using the criteria defined in Table 2 and performance measures defined in Table 4. The assessment considered the respective strengths and weaknesses of the governance models as defined in section 3, to establish a performance measure for each criterion relevant to each option. Table 5 shows the results of the assessment.

Based on core themes and topics that emerged during the consultation process and review of each governance model, the following key considerations and critical success factors relevant to each model and its comparative performance were explored throughout the assessment:

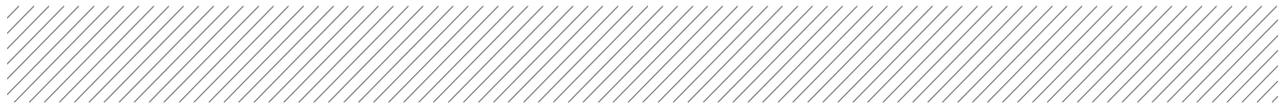
- Retention of ownership
- Maximised financial return to the City
- Transparency of operational performance
- Prioritisation of community outcomes
- Political influence and oversight
- Operational oversight and monitoring
- Financial sustainability
- Strategic oversight
- Access to debt and equity to support capital requirements
- Commercial agility and focus
- Availability of City resources to support community initiatives
- Regional development and expanded community benefits
- Relevant expertise and experience
- Operational, legal and financial risks
- Relevant *Local Government Act 1995* provisions
- FAA restrictions specific to sale, transfer, lease or disposal of BMRRA within 10 years
- Risks associated with regulatory compliance specific to CASA regulation and noise management.

Table 5 Detailed assessment

Criterion	Option 1 Local government own/manage	Option 2 Management contract	Option 3 Corporatisation	Option 4 Asset lease or divestment
a) Increase in Airport usage to facilitate regional economic development: i) Commuters ii) Visitors iii) Freight iv) General aviation.	5 Expertise sourced to support realisation of demand projections through the attraction of RPT and other aviation services. Funding of an engagement strategy has been allocated.	4 Expensive, as operator would typically be incentivised financially to increase airport usage. Comparable access to required expertise and experience, potentially limited as unlikely to have been involved in development of the engagement strategy	5 Access to resources and expertise with extensive experience in areas of airline negotiating and development of aviation opportunities. Potential that Board oversight will further support achievement of increase.	5 Access to resources and expertise with extensive experience in areas of airline negotiating and development of aviation opportunities. Comparable advantage in ability to leverage broader portfolio of operations.
b) Airport operations, including operational efficiencies	4 Post-project operational efficiencies available through integration of airport management as part of broader City operations. Post-project passenger growth uncertainties limit ability to fully optimise operations.	3 Comparably less post-project operational efficiencies anticipated as establishment of designated management team limits flexibility of resourcing, introducing a higher cost structure whilst operations continue to grow.	3 Comparably less post-project operational efficiencies anticipated as establishment of Board and designated management team introduces a higher cost structure initially. This will likely be offset by improved commercial efficiencies as operations grow.	5 Airport investors are highly experienced in airport operation and development of non-aviation revenues. An investor would likely find commercial and operational efficiencies through broader portfolio of operations, with corporate support typically centralised.
c) Financial return on public investment	5 Consistent with increased airport usage driving revenue growth.	4 Consistent with increased airport usage driving revenue growth, noting operator fees.	3 Dividend to City likely structured to align with increased airport usage driving revenue growth.	2 Risk profile associated with demand projections will reduce the asset value realised through a leasing – at least until solid record established.

Criterion	Option 1 Local government own/manage	Option 2 Management contract	Option 3 Corporatisation	Option 4 Asset lease or divestment
d) Financial sustainability of the Airport including asset management and access to capital to support asset requirements	3 Federal and State funding does not require interest or repayment of investment. City can elect to forego dividend, during initial post-project growth phase as reliable revenues are developed. Local Government Act limitations associated with capital funding process provides potential exposure to financial risks in the medium term, as demand for maintenance and sustaining capital activities increase. Any funding shortfalls would need to be met by City, until such time that sustainable revenues are realised.	2 Designated resources with airport specific experience will prioritise financially sustainability of operations. Limitations associated with Local Government capital funding process. Upfront management costs would likely be realised as airport usage continues to develop.	3 Designated resources with airport specific experience will prioritise financially sustainability of operations. Limitations during initial post-project growth phase, upfront corporatisation and management costs as airport usage develops. City is quarantined from financial risk associated with capital requirements of the airport assets. Noting, the lending requirements and capital funding processes, if corporatisation was available under the Local Government Act remain unclear.	5 Designated resources with airport specific experience will prioritise financially sustainability of operations. Airport investors are highly experienced in developing all available commercial revenues. Better access to funding to support capital requirements of assets. Noting interest or dividend payments will reduce free cash flow due to debt financing.
e) Organisational capability and capacity	4 Demonstrated ability to attract relevant expertise. Limitations associated with ongoing integration of airport operations as part of a broader business unit.	5 Improved transparency comparable ability to attract and leverage highly experience professionals with relevant expertise.	5 Improved comparable ability to attract and leverage highly experience professionals with relevant expertise.	5 Improved comparable ability to attract and leverage highly experience professionals with relevant expertise.

Criterion	Option 1 Local government own/manage	Option 2 Management contract	Option 3 Corporatisation	Option 4 Asset lease or divestment
f) Community acceptance	5 City continues to own and operate airport in the interest of the community, with direct oversight provided by elected officials.	3 City continues to own the airport, private partner operates the airport. City limited in ability to influence operations outside requirements and provisions within the management contract.	4 City continues to own the airport, providing strategic operational oversight. City is able to structure Board performance targets that prioritise community interests.	2 Community acceptance of asset privatisation is typically low. Asset lease would be received more favourable than divestment as City ultimately retains ownership.
g) Compliance with the <i>Local Government Act 1995</i> and State government funding provisions	5 Compliant with <i>Local Government Act 1995</i> and FAA.	5 Compliant with <i>Local Government Act 1995</i> and FAA.	1 Not compliant with <i>Local Government Act 1995</i> . Amendment to section 3.60 would be required for option to be legal. Consent of funding State departments required by FAA, to enable transfer of asset to CCO.	5 Compliant with <i>Local Government Act 1995</i> noting disposal provisions are defined in sections 3.58 and 3.59. Consent of funding State departments required by FAA, to enable transfer of asset to investor.
h) Compliance with regulatory frameworks, e.g. noise management regulation (EPA) and safety regulation (CASA)	4 Fully compliant, although compliance risks rest with the City.	4 Fully compliant, although compliance risks rest with the City.	5 Legal and financial risks associated with non-compliance transferred to CCO. Reduced revenues may impact City dividend.	5 Operating, legal and financial risks associated with non-compliance transferred to investor. Recognised expertise in managing compliance.
Overall rating	35	29	29	34



4.2 Summary of recommended option

Option 1, namely continued local government ownership and operation utilising service contracts, has been identified as the most suitable and appropriate post-project governance model for management of BMRRRA at this time.

This option is Business As Usual for the City. The City has an airport project team managed within Community and Commercial Services. This team is currently managing the upgrade project and preparing to engage with airlines closer to opening of the new runway. The team appears to be progressing well under the guidance of the Project Governance Committee, which should continue with appropriate oversight of risks such as key personnel or project slippage. Section 1 suggests some specific monitoring points.

5 Future assessment and funding

5.1 Trigger Points

Table 6 identifies trigger points in the future operation of BMRRA, where further review of the governance structure is recommended.

Table 6 Future governance reviews

Trigger point	Recommended activities
<p>Two years post-opening</p> <p><i>Considered an appropriate period to report on post-project performance of the governance model implemented. Noting minimal capital requirements are anticipated within the initial two year post-project period, limiting any financial risks to the City.</i></p>	<ul style="list-style-type: none"> Review performance, with specific reference to achievement of the demand projections Based on performance and identified limitations of the model, consider whether a review of the governance model is required.
<p>Earlier of five years post-opening, realising annual patronage of 250,000 passengers and realising EBITDA of \$3.5 million</p> <p><i>Five years is recognised as a minimum period to demonstrate reliable revenues and returns that ultimately attract institutional infrastructure investors, noting that the FAA specifies a 10 year post-project timeframe before sale, transfer, lease or disposal.</i></p> <p><i>Patronage and earnings before interest, taxes, depreciation and amortisation (EBITDA) thresholds identified are considered to be the minimum levels attractive to institutional infrastructure investors.</i></p>	<ul style="list-style-type: none"> Assess asset performance, local government legislative requirements, market conditions and appetite for brownfield airport assets. Engage with State departments that provided funding to understand whether consent would be provided for sale, transfer, lease or disposal (if applicable) Review of the governance structure, applying outcomes of preceding activities.
<p>Ten years post-opening (if applicable)</p> <p><i>Recognised as a suitable period to demonstrate reliable revenues and returns that ultimately attract institutional infrastructure investors. Trigger point and associated activities may not be applicable if sale, transfer, lease or disposal was pursued previously and a contract would limit the ability to pursue an alternate governance structure.</i></p>	<ul style="list-style-type: none"> Review of the governance structure, considering asset performance, market conditions and appetite for brownfield airport assets.

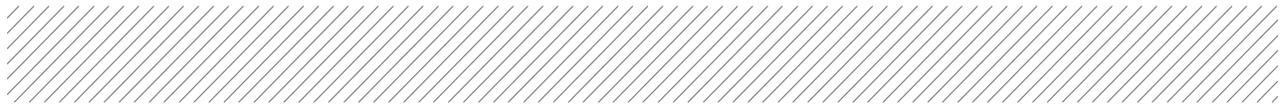
5.2 Future Funds

The following approach is recommended for management of proceeds that would result from a change in governance arrangements, specific to an asset lease or divestment:

- Replace the post-project airport income that would typically accrue to the City
- Invest the remaining funds in development projects that improve the Busselton and Margaret River region and benefit the community.

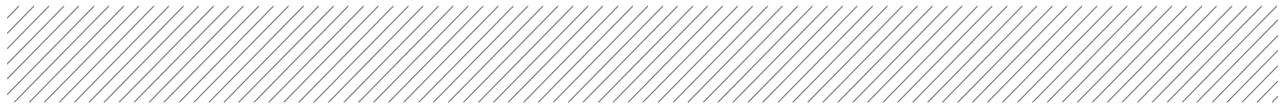
This could be achieved through the establishment of a stabilisation fund through which the proceeds from a change in governance arrangements are invested. If an asset lease was pursued as opposed to an asset divestment, the stabilisation fund could be depleted over the duration of the lease period to ensure consistent reinvestment in the community on a periodic basis. An example of this reinvestment profile might include:

- Establishment of an investment portfolio that delivers a recurrent annual return to replace the established post-project income streams from the airport and associated assets, noting that as the City continued to drive efficiencies across its other businesses this could be structured to deplete.



- A small allocation of proceeds provided as community grants to support a range of local initiatives. It is recommended that funding be administered at the discretion of the City.
- A more substantial allocation of proceeds being assigned to a strategic reserve for investment development projects, with an emphasis on those that cultivate regional economic buoyancy. It is recommended that administration and governance of this reserve be structured such that the final investment decision would be driven by the community.

If an asset divestment was pursued, the additional value associated with absolute ownership of the airport assets would ideally provide the required additional funds to support ongoing returns and community investment, whilst balancing rather than depleting the fund.



6 Recommendations

This governance review recommends that continued local government ownership and operation utilising service contracts is most likely to improve the economic and social value of the airport to the City. Additional recommendations relevant to this post-project governance review include:

- Continued successful and effective management of the development project by the City
- Engagement with target airlines to commence no later than 9-12 months prior to upgraded airport infrastructure becoming available
- A review of the governance model post opening of the upgraded BMRRA to ensure best-practice ongoing governance of the airport, suggested at two years, earlier of five years and 250,000 passengers or EBITDA of \$3.5 million, and ten years
- Development of a reliable baseline demonstrating airport revenues and returns
- Ongoing monitoring of legislative amendments that would enable establishment of a Council controlled organisation.



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