

AGENDA ITEM 4

REPORT TO THE TEES VALLEY COMBINED AUTHORITY CABINET

22 FEBRUARY 2018

REPORT OF THE MANAGING DIRECTOR

DURHAM TEES VALLEY AIRPORT

SUMMARY

The note summarises the latest position with Durham Tees Valley Airport (DTVA), including potential options for the Combined Authority.

Although this paper is unclassified, information presented by officers at the meeting will include matters of a commercially confidential nature. The Cabinet meeting will therefore exclude the press and public.

RECOMMENDATION

The Cabinet are recommended to consider this note, as background to a discussion about the future of Durham Tees Valley Airport (DTVA). No specific proposals are made at this stage, with firm proposals likely to be brought forward to future meetings.

Cabinet are therefore recommended to support a full appraisal of potential options for the future, ruling nothing out or in at this stage.

DETAIL

Recent developments

1. In 2003 Peel Airports Limited became the majority shareholder in Durham Tees Valley Airport (75%), with six local authorities as minority shareholders. They committed to and delivered a minimum of £7.5 million of upfront investment and grew passenger numbers significantly (to 900,000 per year in 2007). After 2007 however, passenger numbers have declined significantly (to 190,000 per year in 2011, and 160,000 in 2017). The airport has been loss making since 2003, with Peel covering the losses, and the local authority shareholdings diluted to 11%, with Peel owning 89%.
2. DTVA have developed a Masterplan for the airport which was endorsed by all the Local Authorities and NECC. This Masterplan established a principle of a business focused airport supported by commercial activity and nearby residential

development. This proposed the development of the North and South Sides into an aviation themed business park (Aerocentre). DTVA has also secured planning permission for a housing development of around 350 units on the Northside. DTVA have committed to recycle the returns from this development back into DTVA. Additional steps have been made by the local authorities to reduce DTVA's exposure to historical Local Government Pension Scheme liabilities.

3. A new shareholder agreement is now in place. This includes a commitment by Peel to keep the airport open as a functioning airport up to 2026. This commitment becomes conditional after 2021, dependent on the achievement of financial benchmarks which, on current performance, are not currently met.
4. Among other recent developments:
 - Peel have invested around £250k on the refurbished passenger terminal.
 - Loganair announced new operations from DTVA to Norwich and Aberdeen (in competition with Eastern Airlines), but which have recently been announced will close.
 - KLM have announced its new fleet of aircraft operating the DTVA / Schiphol route.
 - The Great North Air Ambulance have prioritised a new location outside the airport, following talks with DTVA which failed to secure a long-term lease agreement.
 - DTVA management proposed the closure of Teesside Airport station. Without support from the Combined Authority, as a member of Rail North, this cannot proceed. As an alternative, DTVA are removing the bridge to reduce maintenance and access costs whilst retaining one operational platform.

Proposals for Combined Authority Investment

5. The Combined Authority is committed to securing a sustainable future for the airport, enhancing its contribution to economic growth, supporting connectivity to international markets and attracting inward investment. This is reflected in its role within the Strategic Economic Plan, and forthcoming Transport Plan. A continuation of the decline of the airport's role over the last 10 years represent a significant risk to local economic growth, given the importance of business connectivity as a factor in location decisions, and to sustain important links between Tees Valley businesses and their markets.
6. Although the constituent councils are minority shareholders, the Combined Authority itself has no formal role in the airport's governance. To remove conflicts of interest between the governance of the airport and of the Combined Authority, the Councils have recently made new appointments to the Board of DTVA, which ensure separation with appointments to the Combined Authority Cabinet.
7. An Expression of Interest for the North Side development has been submitted to the Combined Authority by DTVA, proposing a £2 million capital allocation and mechanism for the Combined Authority to absorb revenue risk in the development. Further details of this proposal are expected from DTVA next month. DTVA have separately withdrawn an application for £5 million support from the Combined Authority for the South Side development, which they regard as non-commercial at this stage.
8. In February 2017, officers from Local Authorities and the Combined Authority developed the heads of terms of a proposed partnership agreement, in discussion

with Peel Holdings as majority owners of DTVA. The Council Leaders subsequently met with the Chair of Peel Airports on 1st March 2017, and expressed support for this proposal in principle. The proposed agreement involved further funding from the Combined Authority to DTVA, of £0.5 million a year for four years. Funds would be disbursed against projects agreed between the parties. It was clear, following the election, that the Tees Valley Mayor does not support this approach, and the proposition was therefore not brought forward for formal agreement by the Cabinet.

9. More recently, on 2nd February, DTVA put forward a proposal for route development support and investment in retail facilities, requiring an allocation of £500k from the Combined Authority. The proposal has been defined by DTVA as commercially confidential, but has been made available to Cabinet members. In principle, there is a rationale for public sector support for route development. Although ultimately any route would need to be commercially viable, the public sector can help establish new routes by reducing the upfront risks faced by airlines. The government has previously operated such a scheme, although DTVA was unable to benefit from it. Officers are therefore considering the scope for a facility to support route development. Such a facility would need to be compliant with state aid restrictions, and would be available only where there is a specific proposition for a new route which will improve the long-term sustainability of the airport. Investment in retail facilities is less likely to be appropriate for Combined Authority investment.

Future Growth Opportunities

10. The decline of DTVA is not inevitable. It has sufficient public facilities and runway capacity to accommodate a much larger scale of operations. 3.5 million people live within a 60 minute catchment area, and this could expand considerably as the Tees Valley's priority transport plans are delivered. Large scale employment sites in the Tees Valley, North Yorkshire and County Durham look to DTVA as their nearest accessible airport.
11. To inform the 10 year plan that will be a necessary element of any new ownership arrangements, or otherwise under current ownership, the Combined Authority needs to have a clear position on its ambitions for the future growth of the airport. A growth plan should be credible, informed by future prospects for the regional airline market, and reflect opportunities for public and private sector investment in the airport and surrounding infrastructure. It will also have to be informed by future investment and operational requirements.
12. Elements of this growth prospectus could include:
 - A stronger role for the Airport in promoting the delivery of the Strategic Economic Plan, the development of key sectors, the UK's Industrial Strategy, and the attraction of inward investment to the Tees Valley.
 - A strategy for route development, targeted at establishing new regular routes, and promoting a more strategic approach.
 - Paving the way for a new route to London, and delivering on the government's commitment that flights to Durham Tees Valley will be facilitated by a Heathrow 3rd runway.
 - Accelerated delivery of the business sites on the North and South Side of the Airport.
 - A proposal to government to establish an Enterprise Zone at the Airport.
 - Improvements to the Airport site; including better access from the road network, improved signage, and better facilities for passengers.
 - Opportunities for a stronger partnership with the armed forces.

- Investment to enhance the use of the airport for freight, with good local facilities and stronger links into national logistics networks.
- Development (with Darlington and Stockton Councils) of simplified planning arrangements, including the option of a Local Development Order, and consideration of the potential role for Mayoral Development Corporation Powers.
- Enhanced public transport links.
- The opportunities for expanding the airport's catchment area, through investment in Tees Valley's key route network, and improvements to the Tees Valley's East-West road links to the A1(M).
- Support for initiatives to enhance skills levels and contribute to the Tees Valley's skills and employment objectives, by developing high quality apprenticeships and training programmes in the aviation engineering sector and associated careers.
- Enhanced marketing and promotion of the Airport.

Future Ownership of the Airport

13. The Tees Valley Mayor was elected with a commitment to buy back the Airport, in order to secure its long-term future and grow its contribution to the local economy.
14. A significant ownership stake by the Combined Authority could in principle provide substantial benefits. It could ensure a long-term approach, extend the keep-open commitment, and ensure wider economic considerations influence decision-making over routes and growth opportunities. Since public investment is likely to continue to be required, public ownership would help to ensure the effectiveness and returns from that investment. It could strengthen the role of the airport as a partner in the wider economic growth of the Tees Valley. A number of successful regional airports, including Manchester and Newcastle, operate with a significant degree of ownership by the local public sector. Governance arrangements can be put in place to ensure a high degree of operational independence, within a clear public-private partnership approach.
15. Since the May 2017 election, a number of discussions have taken place between the Mayor and Managing Director with Peel to determine a way forward. Peel's position is that they are "not inclined to sell", and their preferred option is for the Combined Authority to invest in DTVA without any increase in public sector control or extension of the keep-open commitment. Discussions continue. Some of these discussions involve a high level of commercial confidentiality, and will therefore be discussed with Cabinet in a closed session without access by the press and public.
16. Any proposal brought forward for consideration by the Cabinet will be subject to significant financial due diligence, to ensure the proposal is affordable and sustainable over the long-term. A full risk assessment will be required, taking into account financial and operational risks, land valuation, and proposals for airport operations and revenues. To inform these considerations, the Managing Director and Finance Director have, under delegated authority, commissioned external legal and commercial advice on appropriate models to deliver the Mayor's commitment. The Combined Authority will need to work with other private sector partners, to ensure the effective operations of the airport, and potentially as a co-owner within a public-private ownership arrangement. Any proposal would also need to be accompanied by a credible long-term growth plan, which provides assurance there is an investable proposition which secures wider economic benefits.
17. Leaders have separately considered the case for the Combined Authority buying the minority shareholdings of DTVA held by the five Tees Valley Councils, with the councils therefore securing influence through their role as Combined Authority

constituent councils rather than minority shareholders. This option may be beneficial to the partner councils, and could be considered when and if a wider position on DTVA is brought forward for agreement.

18. Cabinet is invited to consider the issues raised by this paper, and other matters presented in confidence at the meeting, and provide views on the appropriate strategy for the Combined Authority going forward.

FINANCIAL IMPLICATIONS

19. This report makes no specific financial commitments. Any proposals subsequently brought forward at a later date will outline detailed financial implications.

LEGAL IMPLICATIONS

20. This report makes no specific legal commitments. Any proposals subsequently brought forward at a later date will outline detailed legal implications.

RISK ASSESSMENT

21. This paper gives rise to no new risks for the Combined Authority. Any proposals subsequently brought forward will include a risk assessment.

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