

DAA, the next DDDA?

In the light of recent developments at the Dublin Docklands Development Authority (DDDA), it is time to turn the spotlight on another commercial semi-state body, the Dublin Airport Authority (DAA).¹ The DDDA debacle is just a symptom of a wider rot in our commercial semi-state sector.

We have seen that the DDDA operated under a development-driven agenda that had little regard for good governance and no respect for the concept of “value for money”. As a result, the taxpayer may be stuck with a debt of €400 million arising from the purchase of the Irish Glass Bottle site for which the DDDA cannot now even pay the interest. The DAA could hit the taxpayer for five times that sum.

The Annual Report for 2009 showed a sharp deterioration in group performance over 2008, with a loss of €13 million compared with a profit (after tax) of €47 million in 2008.² The outlook for 2010 and 2011 is even worse. With its grandiose Terminal 2 at Dublin Airport opening for business in November 2010 the DAA is facing huge revenue shortfalls due to collapsing passenger numbers at a time when it will have to operate two underused terminals.³ Together, T1 and T2 could handle double the current passenger throughput of Dublin Airport.⁴ Management will find it very difficult, maybe impossible, to run the airport and repay outstanding loans. As debts accumulate further, the taxpayer may have to bail out the DAA.

In 2006, Brian Cowen then Minister for Finance, increased the DAA’s statutory borrowing limit from the previous level of €0.7 billion to €1.8 billion to allow it to fund its ambitious €2 billion expansion plan.⁵ This was driven by the, “If I have it, I spend it,” Celtic Tiger, bubble-generating paradigm that then pervaded government thinking. In the same year he approved the DDDA borrowing up to a more modest €127 million towards the purchase of the Irish Glass Bottle site.

DAA debts are growing rapidly. The gross debt was €1.25 billion at the end of 2009 compared to €481 million at the end of 2007. When adjusted for cash balances, net debt at the end of 2009 was €616 million compared to a surplus of €35 million at the end of 2008. Net debt could be €1.1 billion by the end of 2010.⁶ DAA debt is guaranteed by the state.⁷ Just one part of the current debt, a €600 million bond, requires the DAA to pay a coupon of nearly 6.6% per annum or nearly €40 million year.⁸

Debt will expand by at least €300 million to some €1.6 billion if the deferred parallel runway or the DAA’s now preferred longer runway is built as the DAA continues to insist.⁹ Total debt may reach the approved €1.8 billion. This total does not include the deficit in the joint DAA/Aer Lingus pension fund, which was €700 million at the end of March 2009.¹⁰ It was estimated in 2006 that the DAA’s share of the then estimated liability of €336 million, was 40%. The March 2009 €700 million deficit is believed to have fallen to about €500 million due the improvement in equity markets. If so, a further €200 million must be added to the DAA’s liability, bringing the total to a possible €2 billion.

In February 2010 Standard and Poor's Rating Services downgraded the DAA's credit rating to BBB+ because of falling passenger numbers, which it expected to decline further in 2010 and weaken the authority's financial position.¹¹ Their report also said there was a moderate likelihood of extraordinary government support being provided. Standard and Poor's are saying it is now more likely the DAA will need a government bailout.

The DAA was warned about the potential non-viability of Terminal 2 by the Portmarnock Community Association and Ryanair, but these opinions were derided and ignored by the authorities, including An Bord Pleanála, whose decisions on Dublin Airport's expansion plans imply, unbelievably, that objective testing of economic, social and environmental sustainability is not relevant to planning, in spite of clear government directions to the contrary.¹²

Questions were asked repeatedly in the Dáil and representations were made to ministers on behalf of the PCA (mostly by Trevor Sargent T.D. and Terence Flanagan T.D.) about the failure of the DAA to undertake the Cost Benefit Analysis (CBA) required by government investment appraisal guidelines, which is the official test of the sustainability of proposed large-scale public investments.¹³

The replies were derisory: Yes, the DAA was subject to the guidelines but, as a commercial semi-state body, it was a matter for the Board to certify to the Minister for Transport that the guidelines had been met. As the Board of the DAA had so certified,¹⁴ the Minister was satisfied that the guidelines had been met. So, in spite of the fact that no Cost Benefit Analysis was ever done, as required by the same guidelines, the Ministers for Transport and Finance persist with the non sequitur that the guidelines have been satisfied because the DAA Board says so. It seems these ministers are afraid to demand proof that the board has conformed, by asking to see the analysis, for example.

Another claim often repeated in these replies is that, because passenger charges eventually pay for these new facilities, there are no public funds used.¹⁵ This is not correct. These investments consume public resources. For example, the proposed new runway will take up 840 acres of public land whose value was ignored in costing the runway. Passenger charges do not include any payment for land used. Even in the present depressed land market this land could be worth €1 billion.¹⁶ These public resources are equivalent to tax revenue foregone and the taxpayer should earn a rental for their use. Furthermore, as the DAA is a state body, taxpayers are ultimately responsible for its debts, as they are for the DDDA's debts. This could mean huge and direct exposure for the taxpayer, of perhaps €2 billion. But this truth is twisted in ministers' replies that claim there is no recourse to public funds.

The Commission for Aviation Regulation (CAR) had consultants carry out a CBA on the main investments planned by the DAA (new parallel runway and T2). It came to a negative conclusion even though the analysts hugely understated the capital costs and counted too many benefits. Furthermore, land to be used up was valued at zero opportunity cost and no externality costs (e.g. noise, noxious emissions, road traffic congestion, etc.) were counted. Under pressure from the DAA and the Minister for Transport, the CAR did not complete the study but spun the negative preliminary conclusions so as to allow it to approve the DAA's investment, even though it was

clear, had the study been completed and corrected as the consultants themselves proposed, the final results would have been much worse. Here again is an example of a critical failure of governance. Had the work been completed it would have shown the poor quality of the proposed investment, but improper pressure led to a failure to complete the analysis and a fudge its preliminary results. This is another clear case of the rot that pervades the governance of our commercial semi-state bodies, which will persist until we have independent evaluation.

The failure of Ministers to insist on a proper application of government appraisal guidelines by all state agencies is a clear example of the “disconnect” or lack of accountability by Government for state agencies that was identified by the OECD in its 2008 report “Towards an Integrated Public Service.” That “disconnect” has been a major contributing factor to our current economic mess, exemplified by the DDDA debacle, now being repeated by the DAA.

This is the same failure of governance that has brought, not just the DDDA, but also much of our public service near to ruin. Note that former DAA chairman Gary McGann was also on the board of Anglo Irish Bank that financed building developments with reckless abandon and demonstrably inadequate assessment; a standard of governance that has led Anglo Irish Bank to declare the biggest annual loss in Irish corporate history, imposing an irrecoverable cost to the taxpayer of at least €25 billion that threatens us with economic ruin.¹⁷ He resigned as DAA chairman in March 2009. Like the DDDA, the DAA under his chairmanship “paid little attention to value-for-money considerations in its work” and the government has refused to insist that the DAA and all state bodies strictly follow government guidelines on value for money.¹⁸

We need to have a radical overhaul of the governance of all our commercial semi-state bodies if we are properly to reform the public service and make it fit for purpose.

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Endnotes.

¹ For a list of commercial semi-state bodies, see: <http://www.gov.ie/en/sites/commercialsemistate/>

² See: Annual Report for 2009: http://www.dublinairportauthority.com/AR_2009_English.pdf

³ The CAR estimates that T2 will cost €45 million per annum to operate. With T2 operational, costs of operating T1 will fall by €14 million per annum, so that, in 2011 for example, with 19.9 million passengers expected by the CAR (3.6 million fewer than in 2008) and a consequent drop of about €55 million in revenues, operating costs will increase by about €30 million. That will increase the operating deficit by €85 million – before the problem of interest payments on €1.25 billion debt (about €80 million per annum) is dealt with. The finances of the DAA are precarious, as Standard and Poor's has decided. See 6.2 at http://www.aviationreg.ie/_fileupload/2009_CP4_Final%20Determination_4DEC.pdf

⁴ Terminal 1 handled 23.469 million passengers in 2008, perhaps with some discomfort although the Area 14 extension opened in May 2007. Terminal 2 is designed for 15 million passengers per annum (mppa). That is a total capacity of 38.5 mppa. In 2009 passenger numbers were down to 20.5 million and are expected by the DAA to be about 19 million in 2010. On recent trends 18 mppa is a more likely outcome. Therefore T1 and T2 could handle double expected 2010 traffic. Operating both terminals will be difficult and probably uneconomic. Any future passenger growth will be modest, and probably too late to rescue Dublin Airport from its folly.

⁵ DAA Annual Report for 2006.

⁶ John Mulligan in Irish Independent Business, 29 April 2010.

⁷ See: <http://www.irishtimes.com/newspaper/finance/2010/0222/1224264936940.html>

⁸ The 10-year bonds will carry a coupon rate of 6.5872 per cent. See: <http://www.irishtimes.com/newspaper/finance/2008/0704/1215110018589.html>

⁹ The parallel runway for which planning permission has been given is expected, with ancillary works, to cost €288 million in 2009 money terms. The DAA has announced that it will seek permission to build a longer and wider runway instead. This will undoubtedly cost more. A €300 million figure is therefore conservative. See: http://www.aviationreg.ie/_fileupload/2009_CP4_Final%20Determination_4DEC.pdf

¹⁰ See: <http://www.irishtimes.com/newspaper/finance/2009/0905/1224253906565.html>

¹¹ See: <http://www.rte.ie/business/2010/0223/daa.html> and http://www.alacrastore.com/research/s-and-p-credit-research-Research_Update_Dublin_Airport_Authority_Downgraded_To_BBB_On_Weakened_Financial_Profile_Outlook_Negative-777037

¹² The Cost Benefit Analysis required for larger public investment projects is the government's own objective test of sustainability. Then Taoiseach Bertie Ahern made the following comment at the "Towards Sustainable Airport Development Conference" on 23 October 2006:

“One issue that has come increasingly to influence our thinking in recent years is now critical to the decision-making processes as regards all forms of infrastructural investments in all sectors of the economy. It's the issue of sustainability. The sustainability test of major development projects aims to ensure that the impact on the wider economic and social environment is taken into account before projects go ahead at all.”

¹³ The Department of Finance defines CBA as follows: “The general principle of cost-benefit analysis (CBA) is to assess whether or not the social and economic benefits associated with a project are greater than its social and economic costs.” That is indistinguishable from the definition of sustainable development.

¹⁴ Albeit it dubious language. Gary McGann actually reported to Minister Martin Cullen in 2004: “The capital appraisal and management processes in the company *reflect* the Guidelines for the Appraisal and Management of Capital Proposals issued by the Department of Finance.” Note the deceptively ambiguous term “reflect” which avoids stating clearly that the guidelines were followed, because clearly they were not.

¹⁵ For example, in a reply to Terence Flanagan, T.D. on 30 April 2009 Brian Lenihan said: “Dublin Airport is a critical piece of national infrastructure and the investment currently being undertaken by the Dublin Airport Authority, *without any recourse to the Exchequer*, is crucial for our future economic wellbeing.” [My italics.]

¹⁶ The contaminated Irish Glass Bottle 24-acre site is now said to be worth about €50 million or €2 million per acre. In the Dáil on 9 December 2009, Terence Flanagan T.D. said: “The Irish Glass Bottle Company site was purchased at the height of the boom for €412 million, which is equivalent to €17.2 million per acre, an obscene sum of money to pay. The value of the site has dropped dramatically and it is worth only €50 million now.” See: <http://www.kildarestreet.com/debates/?id=2009-12-09.165.0>

Land at Dublin Airport has at least as good a potential for development. A value of €1 million per acre is conservative and represents a fall of 60% on earlier value estimate of €2.5 million per acre. Cargobridge land completely surrounded by Dublin Airport land, having been rezoned by the Fingal County Council from agricultural to industrial use in 1993 was sold for €2.5 million per acre in 2000, long before the peak. See evidence to the Mahon Tribunal on 19/9/2006 and Irish Independent of 20/9/2006.

In its Annual Report for 2009 it would appear the DAA wrote down the value of its Gatland joint-venture interest in 20 acres of land beside Dublin Airport (the former Parnell's GAA playing field), by €6.349 million. As it paid €11.25 million for its half of the venture, it seems to have written down the value of the land by 57% from €1.12 million per acre to €480,000 per acre. An Bord Pleanála refused planning permission for its development as airport car-parking. It is likely that land within the airport boundary is worth considerably more, about €1 million per acre. However, even if we apply the DAA's Gatland site probable valuation we find that the 840 acres of runway land is worth €400 million by the DAA's own reckoning. It is worthy of note that the opinion of the Board in refusing permission had regard to: “the emerging and likely future pattern of passenger traffic at the airport in the short to medium term, which is one of significantly slower growth if any, and the consequently reduced need for additional parking facilities.” The Board's opinion reinforces the pessimistic outlook for the commercial performance of the DAA.

Paradoxically, in its Annual Report for 2009 the DAA values all the DAA's Lands and Airfields at €20 million. The total land at Dublin, Cork and Shannon airports is 5,280 acres (2,137 hectares). It is not clear to what acreage the €20 million applies, as it is probably only includes green-field lands, and may be about 2,000 acres. It would appear therefore that airport land is valued at €10,000 an acre, or about agricultural value. Although the valuation applies to land at all three state airports, the CAR uses the comparable figure of €19.6 million taken from the 2005 Annual Report in determining maximum airport charges for Dublin Airport. The effect of this is that air travelers pay almost nothing for the use of Dublin Airport's land, at the taxpayers' expense.

¹⁷ At the oral hearing into the proposed parallel runway, the DAA's then director of capital programs, Mark Foley, admitted that the DAA did not do a Cost Benefit Analysis for the proposed parallel runway. He said: “DAA does not believe an unbounded Cost Benefit Analysis is required, relevant or beneficial for either the north parallel runway or indeed the overall CAPEX programme...” He did not define "unbounded." So, the person responsible for capital programmes did not believe following government guidelines was “beneficial”. Elsewhere the DAA has argued that, because it is implementing government policy for the expansion of Dublin Airport, no analysis is required. With such respect for good governance, obviously tolerated by the DAA's board and its chairman, there should be no surprise at the mess the DAA and the country are in.

18

See Barry O'Halloran's “Senior managers over-rode policies in 'loose culture.’” in The Irish Times, 26 March, 2010 <http://www.irishtimes.com/newspaper/finance/2010/0326/1224267097272.html>