

Appendix 1 – Engagement Letter

29 July 2002

Mr A Peterson
Partner
Minter Ellison Rudd Watts
P O Box 3798
AUCKLAND

Mr P Taylor
Partner
Bell Gully
PO Box 4199
AUCKLAND 1030

Dear Sirs

Air New Zealand Limited / Qantas Airways Limited Proposed Strategic Alliance

1. Further to Minter Ellison Rudd Watts' letter of 23 July 2002, and our meeting on 26 July 2002, we write to confirm our understanding of the work which you require us to perform on the proposed strategic alliance between Air New Zealand Limited ("Air New Zealand") and Qantas Airways Limited ("Qantas"). The work will be carried out on behalf of Air New Zealand and Qantas and we understand that you are contracting on behalf of those companies.
2. We shall peer review the methodology, modelling and results of the economic analysis prepared by Network Economics Consulting Group Pty Limited ("NECG"). Specifically, we shall:
 - (a) Review all material input assumptions and establish the extent to which they are substantiated. Where possible we will cross check to alternative verification sources.
 - (b) Confirm that the methodology applied is reasonable in the circumstances.
 - (c) Consider the reasonableness of model outputs in light of the input assumptions, including the results of sensitivity analyses.
 - (d) Test the accuracy of the operation of the principal models used as far as that is possible.

- (e) Prepare a report setting out our analysis and conclusions for possible use by Air New Zealand and Qantas in connection with the approval process with the Commerce Commission (“NZCC”) and Australian Competition and Consumer Commission (“ACCC”).
 - (f) Present, if required, the analysis and conclusion to the NZCC and ACCC.
3. You will understand that it is not possible to verify the operation of a spreadsheet model so as to guarantee it contains no errors and we will give no such guarantee.

Staff, Timetable and Fees

4. I shall take responsibility for the assignment; the review partner who will provide input into material economic issues will be Suzanne Snively. We will use other staff as required, initially Simon Mann, Ben Campbell and Chris Gould. We may also seek input from one of our Australian partners with experience in submissions to the ACCC, but will discuss this with you in advance to determine whether this is appropriate.
5. We shall charge our normal rates for work of this nature, New Zealand partner time will be charged at \$550 per hour, plus GST, junior staff are charged at lesser rates depending on their experience.
6. Given the detailed and interrelated nature of much of the modelling, we think it best to use a reasonably small assignment team (named above) so as to minimise the prospect of issues ‘falling between the cracks’, but recognise that you seek some feedback in your briefing meetings on 8 and 9 August. We shall therefore make every effort to identify key issues and complete as much of the review as possible by that time, although we do not expect to complete our formal report by then. There may also remain outstanding issues at that stage depending on the timeliness and adequacy of information which Air New Zealand and Qantas are able to provide.

Terms and Conditions

7. The attached terms and conditions set out our respective obligations and duties. The terms and conditions provide that, amongst other things; our liability is excluded in certain circumstances and in other circumstances limit our aggregate liability whether in contract, tort or otherwise to a maximum amount of five times the amount paid by Air New Zealand and Qantas in respect of the Services.
8. This letter and the terms and conditions attached comprise the entire agreement (“the Contract”) for the provision of the Services to the exclusion of any other express or implied term, whether expressed orally or in writing, including any conditions warranties and representations. The Contract shall supersede all previous letters of engagement, undertakings, agreements and correspondence regarding this assignment. The terms and conditions should, therefore, be read in full.

Governing Law and Jurisdiction

9. The Contract shall be governed by and interpreted in accordance with the laws of New Zealand. The New Zealand courts shall have exclusive jurisdiction in relation to any claim, dispute or difference concerning the Contract and any matter arising from it.

Reliance on Information

10. Air New Zealand, Qantas and NEG (“the Information Providers”) will need to provide such information and assistance to us as we may reasonably require from time to time to enable us to provide the services (as described above).
11. We will expect that the Information Providers shall use all reasonable care, skill and attention to ensure that all information we may reasonably require to complete the assignment is provided on a timely basis to us and is accurate and complete and we will not check back to source their source documents unless we consider that the information appears questionable. We also expect that they will notify us if they subsequently learn that the information provided is incorrect or inaccurate or otherwise should not be relied upon.
12. Our reports will be based on the information provided. While the engagement may involve an analysis of financial information, the engagement does not include an audit or formal verification of source information provided by Air New Zealand or Qantas. Accordingly we assume no responsibility and make no representations with respect to the accuracy or completeness of any information provided by and on behalf of the Information Providers.
13. In accordance with our normal practice we may seek confirmation of the factual content of our report direct with the Information Providers prior to its completion. We may also require a letter from the Company confirming representations made by you to us.



Acknowledgment and Acceptance

14. If the scope and terms of the engagement are acceptable, please acknowledge your acceptance on behalf of Air New Zealand and Qantas by signing the confirmation attached, returning the enclosed copy of this letter to us at the above address.
15. If you have any questions or amendments please ring me.

Yours faithfully
PricewaterhouseCoopers

ERIC LUCAS

Enclosure



Confirmation of Terms of Engagement

Having read the letter of engagement from PricewaterhouseCoopers dated 29 July 2002 and the Terms and Conditions attached thereto, on behalf of Air New Zealand and Qantas we acknowledge acceptance of and agree to engage PricewaterhouseCoopers upon the terms of the same.

.....
Signed: A Peterson	P Taylor
Partner	Partner
On behalf of Minter Ellison Rudd Watts	Bell Gully

.....
Date:	Date

Attachment to engagement letter dated 29 July 2002

Terms of Engagement

This document together with the attached letter (“Engagement Letter”), form the Contract between Air New Zealand Limited, Qantas Airways Limited, and PricewaterhouseCoopers.

1. Services

We will provide the Services described in our Engagement Letter dated 29 July 2002 (“the Services”).

Timescale

We will use our best endeavours to carry out our obligations in accordance with the timescale set out in our Engagement Letter. However, unless both parties specifically agree otherwise in writing, the dates contained in our Engagement Letter are indicative dates intended for planning and estimating purposes only and are not contractually binding.

Changes to Services

Any of us may request changes to the Services as set out in the Engagement Letter or changes to any other aspect of the Terms of Engagement. Changes must be requested in writing with sufficient detail to enable the other party to assess the impact of the requested change on the cost, timing or any other aspect of the Services. Both of us agree to work together to consider and, if appropriate, agree any changes. Until a change is agreed in writing, the latest agreed terms will apply.

2. Reports and Advice

We will report to you in accordance with the terms set out in the Engagement Letter. You may make copies of the report available to those people referred in our Engagement Letter but, unless required by law, you must not provide the report or copies of it to any other third party without first obtaining our written consent. Such consent will only be granted on the terms we deem appropriate which will include that we accept no duty or responsibility to any other party who may seek to rely on our report. In some cases appropriate releases from third parties may be required.

You acknowledge that no reliance shall be placed on draft reports, conclusions or advice, whether oral or written, issued by us as they may be subject to further work, revision and other factors which may mean that such drafts are substantially different from any final report or advice issued.

3. Information

You agree to provide in a timely fashion all information and documents reasonably required to enable us to provide the Services. Unless otherwise stated in the Engagement Letter, we will not independently verify the accuracy of such information and documents and we will not be liable for any loss or damage arising from any inaccuracy or other defect in any information or documents supplied by you.

4. Fees and Payment

How fees will be calculated

Our fees are calculated in accordance with the terms of our Engagement Letter. Alterations to the scope of work or delays beyond the control of PricewaterhouseCoopers may require a re-negotiation of fees.

Performance

Our performance is dependent on you carrying out your responsibilities as set out in these Terms of Engagement and the Engagement Letter. Should this not occur, it may lead to an increase in our fees depending upon the extent to which we have to perform more work ourselves or reschedule our commitments to deliver the agreed Services.

Expenses

You agree to pay our reasonable travel and accommodation costs incurred in connection with our services. We also charge a service fee of 3% to cover our costs in respect of photocopying, postage, tolls, taxes, filing fees, stationery, couriers and mileage. Any special expense arrangements will be agreed.

Payment of invoices

Our invoices will be issued either on a fortnightly basis reflecting the status of the assignment or following completion of the assignment. All invoices will be due for payment within 14 days of issue. PricewaterhouseCoopers retains the right to charge a commercial rate of interest on accounts which are overdue by more than one month.

5. Term and Termination

Duration of Contract

The Contract will apply from the commencement date stated in the Engagement Letter, if any, or where no commencement date is specified from the date of signature by both parties. The Contract will continue until all the Services and deliverables have been provided unless it is terminated earlier in accordance with the terms set out below.

Termination

The Contract may be terminated by either party by written notice if either party fails to remedy a material breach of these Terms of Engagement.

6. Confidentiality

To afford the maximum protection to your confidential interest, all employees of PricewaterhouseCoopers are employed under a service contract which contains a clause strictly forbidding the unauthorised disclosure of information. All personnel involved will sign your standard Confidentiality Agreement before starting work. We will provide original signed copies of the Confidentiality Agreement for all such personnel.

7. Third Party Disclaimer

Notwithstanding any other provisions contained herein, PricewaterhouseCoopers expressly disclaims any responsibility for liability to third parties in connection with this engagement. Any reports we issue are solely for the use of Air New Zealand Limited and Qantas Airways Limited and for the purpose for which they are intended. No third party is entitled to place any reliance on the reports, or any other work products we produce.

Any report we issue will be accompanied by a written disclaimer, stating that the statements and opinions expressed in our report have been made in good faith, and on the basis that all information relied upon is true and accurate in all material respects, and not misleading by reason of omission or otherwise.

8. Liability

1. We shall use reasonable skill and care in the provision of the services set out in our Engagement Letter and these Terms of Engagement. We shall accept liability to pay damages for losses arising as a direct result of breach of contract or negligence on our part in respect of services provided in connection with, or arising out of, the engagement set out in this letter (or any variation or addition thereto); but, to the extent permitted by law, any liability of PricewaterhouseCoopers, its partners and staff (whether in contract, negligence or otherwise) shall in no circumstances exceed five times the fees paid in aggregate in respect of all such services.
2. To the maximum extent permitted by law, PricewaterhouseCoopers, its partners or employees, shall in no circumstances be liable for any loss, damage, cost or expense arising in any way from or connected with fraudulent acts or omissions, misrepresentation or wilful default on the part of Air New Zealand Limited and Qantas Airways Limited and its advisers, directors, employees or agents.
3. To the maximum extent permitted by law, all claims, whether in contract, negligence or otherwise, must be formally commenced within two years after the party bringing the claim becomes aware (or ought reasonably to have become aware), of the fact which gave rise to the action and in any event no later than three years after any alleged breach of contract, negligence or other cause of action arises. This expressly overrides any statutory provision which would otherwise apply.
4. You agree that if you make any claim against us, and that loss is contributed to by your own actions, then liability for your loss will be apportioned as is appropriate having regard to the respective responsibility for the loss, and the amount you may recover from us under any cause of action will be reduced by the extent of your contribution to that loss.

9. General

Entire Agreement

The Contract comprising the Engagement Letter and Terms of Engagement and the letter from Minter Ellison Rudd Watts dated 23 July 2002 forms the entire agreement between us relating to the Services. It replaces and supersedes any previous proposals, correspondence, understandings or other communications whether written or oral.

Representations

You acknowledge that PricewaterhouseCoopers has made no warranties or representations in relation to this assignment other than those set out in these Terms of Engagement and the Engagement Letter.

Legal and Regulatory Requirements

You confirm and undertake that you have all necessary powers and have obtained all necessary authorisations, consents and approvals to enter validly and lawfully into the Contract.

Appendix 2 – Restrictions on Use and Principal Sources of Information

1. This report has been written solely to assist Air New Zealand and Qantas in their submissions to the NZCC & ACCC.
 - (a) This report should not be used for any other purpose and should not be reproduced or supplied to any other party without our prior written permission. We accept no responsibility to the Alliance Parties for any reliance that might be placed on this report should it be used for any purpose other than set out above, and in any event accept no liability to parties other than the Alliance Parties in respect of its contents.
 - (b) We reserve the right, but will be under no obligation, to revise or amend our report and the conclusions contained therein if any additional information, which was in existence on the date of our review but was not brought to our attention in preparing our report, subsequently comes to light.
 - (c) The procedures we have performed do not constitute an audit examination conducted in accordance with Auditing Standards promulgated by the Institute of Chartered Accountants of New Zealand (“ICANZ”) or a review in accordance with RS-1, Statement of Review Engagement Standards issued by ICANZ. We do not express an audit opinion or any assurance on the achievability of assumptions which we have examined.

Principal Sources of Information

2. Discussions with management of both Alliance airlines, their respective advisors and NECG.
3. Management accounts for Air New Zealand and Qantas by route group by aircraft for the years ending 30 June 2001 and 2002.
4. The NECG Report on the Competitive Effects and Public Benefits from the Proposed Alliance between Qantas and Air New Zealand, dated 8 December 2002.
5. Economic models provided by NECG.
6. International Visitor Arrivals to New Zealand 2002-2008, August 2002, Tourism Research Council of New Zealand.

7. International Length of Stay and Expenditure Forecasts 2002-2008, August 2002, Tourism Research Council of New Zealand.
8. The Elasticity Database of the Bureau of Transport and Regional Economics (Australia), <http://dynamic.dotars.gov.au>
9. Heathrow, Gatwick and Stanstead Airports' Price Caps, 2003:2008, CAA recommendations to the Competition Commission, February 2002.
10. A Survey of Recent Estimates of Price Elasticities of Demand for Transport, Oum, Waters and Yong, January 1990.
11. Australian Tourism Overview, Tourism Futures International, November 2002.
12. Other publicly available information.



Appendix 3 – Detailed Unit Cost Analysis

Air New Zealand Costs – 2001 vs 2002

[CONFIDENTIAL TABLE]

Qantas Costs – 2001 vs 2002

[CONFIDENTIAL TABLE]

Appendix 4 – Net Benefits – 2001 Unit Costs

Benefits - 2001 Unit Costs (NZD)						
	Cost Savings	Scheduling	Direct Flights	Tourism	Engineering	Freight
Year 1	\$7	\$22	\$0	\$100	\$39	\$2
Year 2	\$139	\$9	\$14	\$221	\$37	\$0
Year 3	\$270	\$4	\$16	\$217	\$35	\$5
Year 4	\$254	\$4	\$15	\$203	\$33	\$5
Year 5	\$257	\$3	\$15	\$189	\$31	\$5
Total	\$926	\$41	\$60	\$931	\$174	\$15

Detriments (NZD)	
Dead Weight Loss	Net Transfer
\$78	-\$14
\$28	\$1
\$49	-\$19
\$48	-\$27
\$47	-\$26
\$250	-\$84

Net Benefit (NZD)
\$117
\$402
\$527
\$502
\$487
\$2,036

Variance vs 2002 Unit Costs						
	Cost Savings	Scheduling	Direct Flights	Tourism	Engineering	Freight
Year 1	10.1%	0.0%	0.0%	0.0%	0.0%	0.0%
Year 2	-10.2%	0.0%	0.0%	0.0%	0.0%	0.0%
Year 3	-6.5%	0.0%	0.0%	0.0%	0.0%	0.0%
Year 4	-6.5%	0.0%	0.0%	0.0%	0.0%	0.0%
Year 5	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
Total	-5.3%	0.0%	0.0%	0.0%	0.0%	0.0%

Detriments	
Dead Weight Loss	Net Transfer
0.0%	0.0%
0.0%	0.0%
0.0%	0.0%
0.0%	0.0%
0.0%	0.0%
0.0%	0.0%

Net Benefit
11.5%
-1.1%
-1.5%
-1.5%
2.0%
0.1%

Appendix 5 – DPL Tornado Diagram

Net Benefits Sensitivity Analysis

Impact of Independent +/-10% Change in Variable

