

# CAA's development of an indicative airport licence: Gatwick Airport's response

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## Introduction

On 23 November, the CAA published a discussion document setting out its initial thoughts on the development of an indicative airport licence. This followed a request by the Secretary of State for Transport to the CAA for advice by January 2012, in order to inform the progress of the draft Civil Aviation bill through Parliament. We understand there will be further opportunities to engage with the CAA on the development of airport licences. At this point we provide our initial views on the indicative draft licence and accompanying discussion document published by the CAA on 23 November.

## Licensing framework

Gatwick has consistently supported the policy proposal to move to a licence-based regulatory framework for airports. This will provide a more flexible and responsive approach to economic regulation than provided for under the Airports Act 1986. However, the potential gains provided for by such a change in approach is highly dependent on the precise details of what is included and excluded from any future licenses. In this context we welcome the opportunity provided by the CAA's discussion document on an indicative airport licence. We will continue to engage with the CAA's process as it develops detailed licence proposals going forwards.

## Part I - Context

### Rationale for a licence

The CAA – in its context discussion – does not mention the most important contextual element of separate ownership. The need for the CAA to design a licensing regime that supports separate ownership and the resulting competition should be uppermost when the CAA considers the need for, and design of, a licence.

The CAA sets out that it can only grant a licence to an airport operator once it has demonstrated that the proposed three part test set out in the draft bill has been met. As the CAA is aware, it is Gatwick's view that the available evidence does not support a finding of the three parts of the test set out in the draft bill can be met.<sup>1</sup> In summary:

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<sup>1</sup> Gatwick Airport made submission to the CAA on 30 November setting out the available evidence. This is available on Gatwick Airport's and the CAA's website [http://www.gatwickairport.com/Documents/business\\_and\\_community/8.8%20Publications/Wed,%20final,%20redacted.pdf](http://www.gatwickairport.com/Documents/business_and_community/8.8%20Publications/Wed,%20final,%20redacted.pdf)

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- Using the CAA's competition guidelines, supported by the CAA's views, we have assembled sufficient evidence clearly to show that Gatwick does not have substantial market power and that the minimum condition for designating the airport and applying a licence is therefore not met.
- The Competition Commission described numerous ways in which competition might manifest itself in its original BAA Airports Market Investigation, and has subsequently concluded that there is greater scope for competition in the near term than it originally anticipated. At that time, the CAA considered that the Competition Commission had underestimated the benefits that might arise from competition and rivalry.
- There are now a range of indications in Gatwick Airport's performance and behaviour of the competitive dynamic forecast by the Competition Commission and the CAA. This competitive dynamic reflects the competitive constraints to which the airport is subject and the resultant need, therefore, for it to seek out new business and retain that which it has. It is important that this competitive dynamic is allowed to develop further.
- In light of this we concluded that Gatwick does not have SMP; the CAA does not need to regulate Gatwick; and that if the CAA gives this clear steer, commercial negotiations between Gatwick and its airlines can start in earnest.

Therefore, in our view, the CAA will not be in a position to grant a licence to Gatwick after the Q5 price control has expired.

While we continue this debate, the terms of the licence would be of interest to Gatwick and we will wish to ensure that any such licence is fit for purpose.

### Other sectors

We note the references to other sectors. A slightly wider review of other sectors – as they move towards competition – is merited here. For example, drawing on the electricity distribution licences would seem to be of limited relevance in developing an airport licensing regime that is intended to protect passengers by promoting competition.

### Approach based on Better Regulation principles

We agree with the CAA's proposal that its approach to licensing should be based on Better Regulation principles, in particular that any regulation should be necessary, proportionate and targeted to the risks that could materialise.

## Part II – Draft indicative licence

We broadly agree with the structure set out by the CAA for its draft indicative licence. This reflects to a large extent the approach and structure in many other regulated sectors where licences are present.

### Terms of the licence

We have no comments on the material presented here. It will be important however to understand the process by which the CAA is intending to issue the initial licence. As we commented at the

stakeholder workshop on 7 December, the Transitional Provisions and the process of the issuing of the initial licence will be of interest to us and we look forward to receiving further detail.

#### Condition 1 – Payment of fees

We have no comments on this as it is a standard condition in licences of this type.

#### Condition 2 – Licence revocation

We agree with the proposals set out by the CAA for the circumstances under which it may revoke a licence. In particular:

- We consider it important that the CAA retains discretion over whether to revoke a licence in the event that any of the circumstances arise;
- We do not consider it would be appropriate for a serious safety breach to be a relevant circumstance for licence revocation as the CAA addresses safety through a separate regulatory licence; and
- We agree that the question of whether insolvency is a relevant circumstance for licence revocation should be considered further during the development of full licences, given that there are factors common with the financial resilience considerations.

Revoking a licence due to the failure in some way of the airport operator is clearly a serious move. We would wish to see the introduction of a concept of “warning” to the airport operator to allow the operator the opportunity to remedy such shortcoming.

#### Condition 3 – Q5 price control condition

We note that the example provided transposes Heathrow’s current price control condition, as requested by the Secretary of State. In doing this we agree that it is appropriate that the licence condition would be identical to the text contained in the current Heathrow price control decision (including the one year extension to the end of March 2014).

We assume this is done merely for illustration and that as the licence is intended not to commence until the first day following the end of Q5, the actual licence will contain only conditions relevant to Q6.

#### Condition 3(a) – Alternative forms of price regulation

We welcome the CAA setting out for illustrative purposes an example of what a licence condition to give effect to an alternative form of price regulation might look like. The CAA, with stakeholders, has spent a lot of time considering alternative forms of regulation which could better deliver in the interests of passengers, more so than traditional forms of regulation. Proper consideration to any such licence condition can only be given once it is clear what the risk of abuse identified by the CAA are that the regulation is seeking to address. This will be informed by the CAA’s airport competition analysis, which it is intending to publish early next year.

#### Conditions 4 and 5 – Public interest conditions

We have no comments on the material presented here. The question we have is how the public interest investigations will be carried out given the intention to remove the Competition Commission from the price control process.

#### Condition 6 – Regulatory Accounts

As the CAA notes, the provision of regulatory accounts is not currently an explicit requirement on the designated airports. We agree that it could be appropriate to include a requirement in a licence for the licensee to provide regulatory accounts to the CAA.

We suggest that the CAA should not – in the licence – specify the accounting standards to be used. This would more usefully be contained in any Regulatory Accounting Guidelines.

#### Condition 7 – Operational resilience

The introduction of operational resilience conditions would be a new regulatory development. Currently there are no such conditions on airports, although Gatwick is continuing discussions with its airlines about whether and how we should include such provisions within the service quality rebate scheme. This would involve including provisions for performance and associated financial penalties if performance was not as required.

We agree with the CAA's preferred approach that operational resilience should be voluntary sector led solutions. If the licence includes detailed operational resilience conditions, we would be cautious if there was the possibility of 'double jeopardy' whereby an airport is penalised through a performance regime as well as potentially being penalised for a breach of a licence condition.

Finally, the drafting appears somewhat broad. Paragraph 7.1 refers to an "efficient and reliable" airport. Paragraph 7.2 requires the licensee to "effectively co-ordinate and co-operate with all relevant parties at the airport". Further detail as to what the CAA might mean would be welcome.

With respect to paragraph 7.5, we do not consider that the CAA should approve a resilience plan. This is properly a matter for the Board of the regulated airport to approve, for onward submission to the CAA.

#### Condition 8 – Financial resilience

We welcome the proposals to allow derogations from the airport operator's financial structure at the time of Royal Assent. However, while we do not have detailed comments on the material presented, we note that this will be an important condition with potential significant implications for Gatwick Airport. As such we reserve our position on the material presented by the CAA and note that the development of this condition will require full discussion during the process to develop licences for regulated airports.

### Part III – High-level timetable for the full licence

We are aware that the arrangements to be put in place to manage the transition from the Airports Act 1986 to the new Civil Aviation Act have yet to be fully developed. These transitional arrangements will be shared with stakeholders in due course. However, it is not clear from the CAA's high-level timetable how and when the current price control will be transitioned from the

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Airports Act 1986 to the new Civil Aviation Act. We are uncertain as to whether the CAA will develop and issue a licence to each of the currently designated airports to give effect to the current price controls under the new legislation and this is not included in the timetable as set out by the CAA. We would appreciate further clarity on this in due course.

### Contact details

We hope that you find this response helpful. If you would like to discuss any issue raised or seek clarification please use the contact details below. We are happy for you to publish this response.

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