

Airport Consultative Committee – Gatwick Airport (ACC)

ACC Response to CAA document:

Economic regulation at Gatwick from April 2014

Final proposals

4 November 2013

Table of Contents

	<u>Page</u>
1. Summary	3
2. Introduction	6
3. Traffic	7
4. Capital Expenditure & The Regulatory Asset Base	10
5. Operating Costs	14
6. WACC	21
7. Service	25
8. Commitments	26

I. Summary

I.1 This submission sets out the Gatwick Airline Consultative Committee's (ACC) response to the Civil Aviation Authority's (CAA) Final Proposals for the economic regulation of Gatwick airport. The current submission is the most recent of a list of earlier ACC papers and should be read in conjunction with the ACC's previous submissions.

I.2 Since the publication of the Final Proposals, the CAA only allowed a four-week consultation for responses. Clearly, the ACC believes that this consultation period is too short for it to reasonably address every aspect of the CAA's 300-page consultation document. Therefore the ACC has focussed on the main errors of the CAA's proposal. Because of this short deadline, as commented above, this submission should be read as additional to the points raised and evidence provided in earlier submissions.

I.3 The strength of the ACC's submission is its consensus view across the Gatwick airline membership notwithstanding that there are four separate business models undertaken by Gatwick airlines. These business differences aside there is tight commonality in response to GAL's ideas and the CAA's subsequent proposals. Ninety percent of all Gatwick's passengers are carried by the ten largest of the 72 airlines, prising the core ACC membership leaving the residual 10% of passengers carried by the remaining 60 or so businesses.

I.4 The CAA is proposing a regulatory settlement that relies on the CAA endorsing a voluntary proposal that the airport has made. This proposal is known as The Commitments and includes the main aspects of regulation such as price, service and investment. The CAA has made it clear that it is not able to force Gatwick to amend these proposed commitments. This puts the airlines in the unusual position of not being asked to respond to a consultation of the CAA's proposed price cap, but instead on the CAA's approach to GAL's proposed price cap. This risks elements of the commitments being imposed unilaterally without proper consultation of their content or price.

I.5 Not surprisingly, the ACC does not support this approach and within this submission makes these concerns clear. Weaknesses fall into several categories that include:

The CAA's stated 'fair price' is too high, and furthermore is not a reasonable basis for a comparison with Gatwick's proposed commitment price. Our main concerns include.

- The CAA's estimates of the GAL's passenger traffic are too low. It ignores GAL's very late announcement of an additional 21 slots for summer 2014. Similarly, it also ignores the clear evidence that passenger numbers in the base year are already significantly higher than the CAA expected, which will therefore lead to higher passenger numbers throughout the period.
- Pier 6 Southern Extension is included in the Final Proposals. There is clear evidence, accepted by GAL, that pier service targets will be met at the airport, during Q6. The CAA has justified including the proposed extension on the basis that it will avoid £44m in costs for which the ACC has seen no evidence and on which it has not been consulted. The CAA has also not explained how this counter's its original view that this project is simply not value-for-money.
- The inclusion within the fair price calculation of the sizable pension commutation payment is another reversal of the CAA's earlier thinking. The CAA originally noted that this payment has already been priced into the BAA sale price with GIP. Passengers are effectively being asked to fund a windfall payment for GIP. We are concerned that neither the CAA nor the ACC were consulted on this payment before it was made, and yet passengers are now being asked to fund it. We are not clear on what basis the CAA could include this payment, particularly as it has not been consulted on in line with Annex G.
- The Construction Output Price Index (COPI) has been applied inconsistently. Whereas in Q5 there was a levy of 2% added to COPI to accommodate the rise in costs to reflect the Olympic factor increasing construction costs, now with industry commentators indicating future COPI will be negative the CAA has simply ignored such an adjustment irrationally rewarding GAL again.
- On operating costs the CAA have arbitrarily ignored their own consultancy reports that point to significant savings that could be achieved.
- The CAA has increased the WACC, simply by adopting using arbitrary short-term data points for the cost of debt, setting out a cost of debt greater than GAL's current cost.
- The CAA has reduced its estimate of GAL's potential commercial and other revenues on the basis of an unsubstantiated reduction in ancillary charges

and a reduction in retail unit revenue, despite expert evidence to the contrary and the strengthening economy.

1.6 The commitments as proposed by GAL are flawed and irrationally supported by the CAA. They do not reduce regulatory costs, target efficiencies or promote competition. Instead the CAA has allowed itself to be boxed-in stepping back from its statutory obligations to the consumer by accepting a un-commercial one sided contract written by the airport owner. They do not protect the consumer from GAL's ability to exploit its pricing power and are no more proportionate in their application than the hitherto system of a RAB based approach. Finally, they do not inspire confidence stakeholders such as airlines.

1.7 The CAA's comparison between the 7-year commitment proposal and a 5-year RAB based price control is flawed. The capital spend in commitments is approximately £100m a year compared to the RAB yearly spend of £160m, further, the ACC has already sent the CAA a number of detailed concerns with the key terms of the commitments which have yet to be addressed. Including the unanswered problem of how the CAA will shield the consumer from excessive pricing in preparatory cost of any second runway (R2) at Gatwick. The commitments currently inadequately manage this issue. GAL have ostensibly avoided premium pricing for additional services in the commitments so adding additional undisclosed costs to the passengers that ordinarily would be bundled in to and transparent within a RAB based settlement.

1.8 In sum, the Final Proposals are faulted in two ways; the fair price for the RAB option is incorrect and overly inflated through an inconsistent and irrational methodology and the commitments carry significant risks for consumers. Consequently, the ACC rejects these aspects of the CAA's Final Proposals and considers that the CAA would be irrationally failing in its statutory duty to regulate airports as efficiently and as effectively as possible.

Jason Holt
Chair
Gatwick Airline Consultative Committee

2. Introduction

- 2.1 This is the response of the Gatwick Airport Consultative Committee (ACC) to the CAA's final proposals for economic regulation of Gatwick Airport from April 2014.
- 2.2 In preparing its response, the ACC has sought consensus positions that reflect the views of all the member airlines on each of the issues. This has been possible in the vast majority of areas, reflecting the fact that passengers on all airlines want an efficient airport experience.
- 2.3 ACC membership is open to all airlines operating at Gatwick and we take time to communicate with airlines that do not attend meetings, both on formal positions, and if we consider that they may have different interests, on particular issues. The AOC chair attends key meetings and updates AOC members. We have also been mindful of the need to allow flexibility for the needs of future passengers, most of whom are expected to be customers of existing airlines.
- 2.4 Much of the Q6 work has been led by a working group comprising representatives from easyJet, British Airways, TUI and Virgin. These four working group airlines alone account for two thirds of passengers¹ as well as the full cross section of airline business models. The ACC is confident that the view expressed here properly and accurately reflect the views of the airline community at Gatwick airport and will allow all the airline operating models to promote their own passengers' best interests.
- 2.5 We note the CAA has asked for views on three key issues:
1. the CAA's view of a fair price;
 2. the appropriate form of price regulation for GAL from April 2014 and the CAA's evaluation of the various options;
 3. the appropriate licence conditions that would be associated with GAL's proposed commitments

This response addresses these three areas in turn.

¹ 65% in 2012. Source: Fig 2.42 of CAA's Gatwick Market power assessment, May 2013.

PART A – THE CAA’S VIEW OF A FAIR PRICE

This section sets out the ACC’s views on the CAA’s fair price in their final proposal. The approach taken by the ACC in this section is to highlight the clear errors of fact made by the CAA regarding the fair price and include those alongside the errors in judgement the ACC believe the CAA have made.

There are clear errors in the CAA’s final proposals:

- The underestimation of Traffic – The CAA has not taken account of the unforeseen increase in passengers this year and additional slots that have been created by GAL. This will increase both the traffic forecast and projected commercial revenues.
- Unjustified changes made to the WACC since the initial proposals. Particularly in relation to the cost of debt.
- The inclusion of Pier 6 South:
 - The 95% Pier Service target can be met by 2018 (calculated by GAL)
 - It is unlikely that delay costs of £44m would be incurred by GAL. We have not been consulted on this.
- The inclusion of the £104m pension commutation payment:
 - The liability was known at the time of purchase
 - The payment was not consulted on by GAL, at the time, as required by the CAA.

This section sets out the ACC’s views on the CAA’s fair price set out in their final proposal. The approach taken by the ACC in this section is to highlight the clear errors of fact made by the CAA regarding the fair price and include those alongside the errors in judgement the ACC believe the CAA have made.

3. Traffic

3.1 A reasonable assumption on traffic growth is crucial to the estimation of a fair settlement and therefore price. The ACC welcomes the constructive discussions with both the CAA and GAL to date on traffic forecasting. The high combined level of understanding of the drivers of the forecast and assumptions taken has been a positive development in the Q6 process.

3.2 The ACC welcomes the analysis the CAA has presented on the traffic forecasts for Q6 and the extent to which some of the analysis presented by the ACC was taken on board in reaching its assessment of expected traffic levels at Gatwick over the next five years.

3.3 However, the ACC believe the balance of risk is wrong in the final proposals as the forecasts understate the likely passenger growth at the airport and therefore

inflate the fair price proposal. We therefore believe that this does not meet the CAA's duty to the passenger as GAL's shareholders will be over-rewarded at their expense.

3.4 We believe there are 2 areas which point to a significant increase from the proposals put forward by the CAA:

- Significant outperformance of estimates in the base year. GAL's traffic growth has continued to outperform previous assumptions. The base year has a significant impact on the overall forecast so this needs to be taken into account;
- The announcement by GAL of an additional 21 slots including 8 peak slots from summer 2014. The ACC does not believe this type of slot growth was accounted for in the CAA's forecast in the final proposals[1]. We have provided evidence below on the increase in traffic this could provide;

3.5 These impacts combined with the more favourable economic outlook, and recent announcements on long-haul growth from the airport (from BA and Norwegian) mean we believe GAL has the opportunity to significantly outperform the traffic estimates in the final proposals.

3.6 This response provides a cautious estimate of these impacts, on the CAA's forecast, which are discussed in more detail below.

Assessment

Growth in the base year

3.7 The base year of the forecast (2013/14) has a significant impact on the overall level of traffic over the quinquennium. Since the ACC provided its last assessment, traffic at Gatwick[2] has shown much stronger growth than forecast. Moreover, it is also significantly outperforming the growth assumed in the CAA's final proposals.

The ACC is surprised that the CAA has not taken this growth into account in its final proposals. It appears to be consistent with the bottom up methodology they have used for the first three years of the forecast. A comparison of the assumption from the CAA and GAL's current performance is shown in the table below:

CAA (April 2013)	GAL (April 2013)	ACC (June 2013)	GAL Latest Data (Sept 2013)
34.7 m	34.4 m	34.8 m	35.1 m (Moving annual average)

The ACC believes that in order to reach a fair settlement this growth needs to be captured in the base of the CAA's assessment.

Additional slots at Gatwick

- 3.8 After the CAA issued its final proposals GAL issued 21 incremental slots for S14. These slots are part of GAL's drive to increase runway utilisation through the ACDM55 project and represent 8 departing slots in the peak morning period and 1 in the evening peak, plus 12 arriving slots.
- 3.9 This announcement is likely to have a significant effect. The ACC have therefore provided a cautious estimate of the likely impact of this effect on total expected traffic over Q6.
- 3.10 The composition and timing of these slots lends itself to short haul flying and a typical line of flying would incorporate three aircraft rotations for each departing early morning slot, therefore 8 based short haul aircraft is equivalent to 48 sectors.
- 3.11 The ACC does not know who will be granted these slots at this time and therefore has taken an approach that half of these slots would be flown year round and the other half would be limited to a six month season only.
- 3.12 For consistency we have applied the same passenger load per flight as used in the easyJet Flybe slot sale and this has provided an incremental passenger figure of 1.9m passengers per annum.
- 3.13 It is worth noting that this announcement came very late in the slot process and too late for the CAA to alter its final proposals. Earlier notice of this significant move would have enabled airlines to plan better and allow for this effect to have been taken account of in determining the 'fair price' in the CAA's final proposals.
- 3.14 This new information therefore needs to be taken into account before the CAA

can finalise its fair price.

3.15 These impacts combine with a more favourable economic outlook, and recent announcements on long-haul growth from the airport (from BA and Norwegian), for which we have made a marginal adjustment to the forecast of 100,000 passengers per year. We have also included an updated estimate provided by easyJet for its use of Flybe slots.

3.16 We therefore believe GAL has the opportunity to significantly outperform the traffic estimates in the final proposals. The ACC's revised traffic forecast is therefore set out below:

	CAA forecast (Millions)		ACC revised forecast (Millions)	
	totals	% change	totals	% change
2012/13	34.2		34.2	
2013/14	34.7	1.5	35.2	
2014/15	35.8	3.0	38.2	9.4
2015/16	36.6	2.2	39.0	2.1
2016/17	37.2	1.8	39.6	1.5
2017/18	37.9	1.8	40.3	1.8
2018/19	38.5	1.7	41.0	1.5

The ACC has a traffic forecast of 198.2m over Q6 compared to the CAA's assessment of 186m.

4. Capital Expenditure and The Regulatory Asset Base

4.1 The ACC has worked hard with GAL and the CAA to try to ensure an appropriate, efficient and value for money capital plan which reflects the needs of our passengers is delivered in the next regulatory period. We welcome the areas where alignment has been reached, however, there are still a number of areas of disagreement.

4.2 The ACC has not repeated its arguments regarding the suitability of individual capital projects to be included within the next regulatory period. However we believe the CAA has come to a number of incorrect conclusions within its final proposals and these are explained in detail below.

Pier 6 South extension

- 4.3 Pier 6 South is a project that has had very close scrutiny during the Q6 consultation process from both the ACC and the CAA. Many working group meetings and large amounts of analysis have been pulled together with an aim that the final decision on such an important project is made taking into account all information.
- 4.4 The CAA's decision does not reflect the evidence provided on the airline/airport consultation on the proposed extension. The CAA has included the proposed extension within the capital plan, despite:
- Clear evidence that 95% pier service will be achieved throughout Q6.
 - No consultation over a claimed £44m delay cost that has been cited by the CAA as a key reason for its support of the project
 - GAL providing incorrect information to the CAA on the project over the summer.
 - The CAA concluding earlier that the project does not provide value for money.
- 4.5 The remainder of this section runs through, in more detail, all the key points that the ACC believe the CAA have not taken into account during their decision making on this project.

Achievement of Pier Service targets.

- 4.6 Since the publication of the initial proposals the ACC has proved beyond doubt that 95% PSL is achievable for all of Q6 through the use of efficient stand planning and using towing levels similar to those undertaken in Summer 2013. This is without the need to build infrastructure that the CAA acknowledges has an unacceptable benefit to cost ratio. The CAA in its final proposals also acknowledges that 95% PSL in the North terminal is achievable in Q6 and says that "Consequently the CAA considers that Pier 6 South is required to meet airport operational requirements in Q7".

Delay Costs

- 4.7 GAL stated in its letter of the 12th August that stopping or delaying Pier 6 will incur £30m of additional spend in Q6 and a further £14m in Q7 for stand rehabilitation works. The ACC has not been provided with any evidence to support this assertion.
- 4.8 It is clear that this delay cost was material to the CAA's decision to support the proposed extension. However, the CAA has not published any assessment of the validity of the claimed delay cost. Further, it has not explained why this cost should be accepted when contrary to Annex G the cost has not been consulted on.

GAL's misleading information

- 4.9 In its 12 August letter to the CAA GAL included a 2018 Pier Service level that was lower than the one provided to the ACC, in the many consultation meetings.
- 4.10 GAL only corrected its evidence after much discussion between the ACC, CAA and GAL, confirming that the pier service estimate set out by the ACC the valid figure.
- 4.11 The ACC is concerned that the CAA's pier 6 proposal may be based on the misleading information provided by GAL in August. The CAA needs to review the impact of this change, before reaching a decision.
- 4.12 The ACC believes the evidence does not support the case for including pier 6 south extension within the fair price assessment.
- 4.13 Under a RAB based approach this should be included as a development project, and therefore excluded from core capex. This would then allow it to be included if traffic development requires, following consultation with airlines

The pension commutation payment

- 4.14 The ACC does not support the inclusion of the pension commutation payment within the Gatwick fairprice RAB estimate. The CAA has made an error by including it in its final proposals.
- 4.15 The CAA originally said that 'the payment made to BAA was paid as part of the sale of the airport and should have been reflected in a lower sale price than had the payment not been made. It would not therefore be appropriate to include the commutation payment within the Q6 settlement.' The ACC agreed with the original position of the CAA but is disappointed in the change that has occurred in the final proposal. It is clear that the purchasers, (Global Infrastructure Partners) knew of the liability prior to purchasing the airport and presumably would have taken this into account in its purchase price.
- 4.16 The CAA has changed its view on whether the pension commutation payment was included in the purchase price, based on advice from the Government Actuaries Department (GAD). The ACC could not see the reason for the change and wanted to seek further guidance from GAD on this. GAD proceeded to direct the ACC to paragraph 7.14 of the CAA commissioned paper on the review

of pension costs for Gatwick Airport. The ACC can see no justification in paragraph 7.14 for the change in view and therefore the CAA has no reason to change its original position.

- 4.17 Further to this, there has been no consultation of airlines or the CAA regarding the payment. Therefore, as with other large impacts to the RAB, the ACC has not had the opportunity to have input into key decisions such as; whether the payment was value for money for passengers and airlines. Considering GAL will be earning a high rate of return as well as inflation on this payment, the ACC believe these points are vitally important.

Incorrect use of Construction Output Price Inflation (COPI)

- 4.18 The ACC believe it is inconsistent and incorrect for the CAA to ignore the effects of real COPI when calculating the cost of the capital plan in the forthcoming regulatory period. In fact the ACC is surprised to see that COPI is largely ignored within the final proposals issue by the CAA, particularly as it featured prevalently in the Q5 decision.
- 4.19 Within the Q5 settlement the CAA allowed a COPI of RPI+2% per annum for each year of the quinquennium; this despite objections from the airlines and also advice from the Competition Commission (CC) that COPI should be no greater than RPI+.75%². Due to the global economic downturn this overly inflated construction price did not materialise and therefore Gatwick's shareholders were over rewarded for the capital plan during the last regulatory period.
- 4.20 Davis Langdon, the CAA's own consultants, have provided advice that COPI, net of inflation, will be negative until at least the end of the next regulatory period (Figure 4.5). This is in line with expectations as the construction industry is still significantly affected by the government austerity measures which are suppressing construction pricing in the UK. However, the CAA has decided to ignore the advice of its expert consultants and take its own position that COPI should be ignored for Q6 as it believes there is some uncertainty in future levels. The ACC accepts that there is always a level of uncertainty in forecasting but in the longer term peaks and troughs balance and the CAA should adopt its expert advice as this provides balance and also consistency in the approach taken over a longer period of time. The CAA's

² Or to exclude COPI on the basis of long term consistency with RPI.

approach is also inconsistent with its own Regulatory Policy Statement³ that forecast COPI would be taken into account at each review.

Capital Plan in Q7

4.21 It appears incorrect that the CAA would allow GAL a capital plan of £151.4m & £201.6 for the first two years of Q7 given that the CAA also supports GAL's commitment to only spending an average of £100m per annum within the commitments framework.

4.22 The capital plan values put forward for the first two years of Q7 are completely arbitrary and have not undergone any scrutiny by the ACC, or as far as we are aware, by the CAA or their consultants. Asset stewardship in Q6 averages £64m per annum, yet for the additional two years this figure is allowed to rise to £90m per annum. All of this information leads to a position where the ACC is unable to reconcile the values proposed by the CAA for use in the capital plan or within the "fair price" calculation. It would appear more practical to reduce the capital plan in the 7 year RAB calculation to £700m.

5. Operating Costs

Operational Expenses

Summary

5.1 The ACC believe the CAA have made errors in judgement across the opex line item:

- It seems the only change the CAA have made since the initial proposals is to take out an over-inflationary salary increase that was never going to be delivered anyway. Taking out the increase of RPI +0.75%, in itself, will deliver the majority of the core efficiency levels recommended by Helios in its report to the CAA
- This means that other areas of efficiency savings recommended in the Helios report, other than salary costs, have not been taken into account;
 - Consultants costs
 - Management ratio
 - General expenses

³ Paragraph E81 Annex E – CAA Q5 decision.

- The ACC is also concerned that instead of forecasting allowed opex based on an efficient cost the CAA has chosen a point estimate of around 25% of the possible total savings identified by its consultants. The CAA states 'the need to ensure that GAL has a realistic chance of outperformance as a regulatory incentive'. This does not justify providing significant room for outperformance on opex as well as other areas of the settlement. E.G. Traffic forecast and WACC This would indicate that the CAA has put more weight on the interests of GAL's shareholders than on the interest of passengers
- The CAA has failed to take into account many of the arguments / pieces of data that the ACC provided in the response to GAL's Q6 Business Plan in areas such as Security costs, including benchmarking, and the inclusion of process efficiencies at AMD's (Archway metal detectors) to reduce headcount.
- The ACC considers that it is not appropriate to use GAL's projection of costs in 2013/14 as the start point for applying efficiency. Regulatory precedent (for both airports and other sectors) is generally to use the most recent full year for which actual data is available as the base year, which in this case is 2012/13. Otherwise, the outperformance that GAL enjoyed during Q5 will not be shared with users. This would be inconsistent with the fundamental principle of RPI-X regulation.
- We also consider that the pensions allowance is inefficient and should be reduced.

Operating cost efficiency

- 5.2 Operating costs have a significant impact on Gatwick's price cap, and thus the fares paid by passengers. Consequently, it is critical that these costs are properly assessed as part of the regulatory process and that they are as efficient as possible, it is not in the passenger interest to subsidise inefficiency. The CAA has a statutory obligation to ensure that regulated airports operate efficiently and effectively.
- 5.3 The CAA initially proposed to offer GAL a challenge of finding 1.1% efficiency per year, which did not include any efficiency on central service costs but allowed a salary increase of RPI +0.75% for staff
- 5.4 The ACC therefore sought to provide further evidence as to how, greater efficiencies could be delivered across Q6, in a sustainable way. The CAA has continued to ignore this evidence and only a marginal change to a 1.2% efficiency per year is now proposed. Our passengers would therefore continue to subsidise a high-cost operation through Q6.

- 5.5 The remainder of this section highlights key issues the ACC has with the CAA response and gives great details on the error in judgment seen through the Helios report.

Helios report review / potential for further central service cost efficiencies:

- 5.6 The ACC was eagerly awaiting the findings of this report considering the Gatwick business plan did not contain any efficiency in this area and contained an annual RPI+0.75% increase in staff pay throughout Q6 (which does not reflect trends seen in the aviation industry, would never have been realised and would be excessive if it as given the pay benchmarking studies which showed GAL salaries are a long way over comparators). This led to an expectation that there will be quite a significant efficiency level found in this section that is over and above the proposed salary increase.
- 5.7 The Helios report finds that Gatwick could reduce central service costs in several areas including finance, insurance, legal and communications and proposed that savings could be made through reducing wages, outsourcing, restructuring and reducing the seniority of departments.

Comments on the CAA's initial interpretation of the Helios study and its implications for the final proposals:

- 5.8 Considering the lack of information received in this area during the Q6 consultation process the ACC viewed this report from Helios as an important link between the Q6 business plan and finding appropriate levels of efficiency that will bring GAL into line with other businesses in our industry. The CAA has a statutory obligation to ensure that regulated airports operate efficiently and effectively which means that the failure of the CAA to set GAL a target to meet this requirement would, in our view, constitute a failure to meet the statutory obligations. In saying this, the ACC was disappointed to read that the CAA seems to hold many areas of uncertainty surrounding this piece of work.
- 5.9 The CAA noted many areas where it originally had concerns with the report, including:
- The late delivery of the report and lower level of stakeholder engagement relative to other CAA studies;
 - The limited analysis of the drivers of central service cost provided by the report;

- The wide range of benchmarks, which sometimes provide conflicting assessments of relative efficiency;
- Additional benchmarking evidence provided by Gatwick in response to the initial proposals;
- Uncertainty over the achievability of the stretch efficiency savings suggested by the benchmarking evidence; and
- The risk of double counting the wage cost efficiencies proposed by the CAA based on the IDS staff cost benchmarking evidence.

5.10 The ACC believes it is important that the findings of the Helios report are taken in to account:

- While the CAA outlined some concerns with the Helios report, it then accepted it in full (we understand it paid for the work). Consequently the ACC does not understand why the report’s recommendations were not adopted.

The CAA’s conservative approach to savings

5.11 The ACC does not understand why the CAA has, again, chosen a point estimate at the low end of the possible total savings developed in the work produced by Helios. At a minimum the ACC believes this should move to the mid-point to reflect the concern that GAL needs to work towards greater levels of efficiency (see table below showing efficiency levels from Helios report and the use of a mid-point efficiency level). The ACC believes this would be more consistent with the CAA’s duties to promote efficiency. The ACC would like to remind the CAA of the point that in previous studies one of the factors that the CAA appears to have considered when selecting a low point in the efficiency range is that there will be traffic growth during the period. The ACC’s view is that it is important to separate the concepts of traffic growth and efficiency savings and to show these separately in any analysis.

The table below shows the Helios recommendations on the savings that GAL could make on central services. The mid-point has been calculated by the ACC.

Stretch	3.3	3.9	4.2	4.8	5.4	21.6
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5.12 The ACC considers that the way the CAA has analysed the results of the consultancy studies is somewhat unusual in that one normally might expect consultants and benchmarking evidence to provide evidence on how inefficient the company is today or compared to the base year rather than how much it can reduce

its own plan by the end of the period (because the plan is likely to be padded anyway).

- 5.13 The ACC would like to emphasise that its proposed efficiency target of 2.8% per year on GAL's original business plan, although challenging, is a more realistic level of savings required considering the large amount of inefficiency embedded in the GAL Business Plan. The ACC highlighted this inefficiency in its earlier evidence to the CAA.

Pension Treatment

- 5.14 The ACC considers that the CAA should make the following changes to its pensions allowances:

- The employer contribution rate for the Defined Benefit (DB) scheme should be around 14.4% (rather than 20% as proposed) in line with benchmark rates. This is also broadly consistent with the reduced benefits seen across the economy, and an assumption that pay will be frozen in real terms, consistent with the CAA assumption about what is achievable in Q5 to reduce pay towards market levels;
- The employer contribution rate for the Defined Contribution (DC) should be set at around 6.6% reflecting benchmark rates, adjusted if necessary to allow for salary sacrifice arrangements.
- The CAA should set out its pensions policy for the future, building on the Q5 RPS, and stating clearly that no deficit payments will be made in future, unless the scheme benefits are consistent with other schemes in key respects and pay reflects market rates.

- 5.15 In the Q5 review, the CAA and CC recognised that regulated airports should not get a cost pass through on pensions, because that would reward inefficiency and make it unlikely that management would address pension risks as other companies have done, leading to significant inefficiencies.

- 5.16 The CC were explicit that users should not bear the additional pension costs caused by the relative generosity of the pension scheme or by the change in investment strategy caused by the acquisition by ADI.⁴ They calculated the deficit assuming a) that the scheme was in balance and b) that benefits were the average of private sector schemes at the time. On that basis, employer cash pension costs of 16-20%

⁴ CAA final proposals Nov 07 6.12

were assessed. The CAA allowed 25% only in order to give the airport time to adjust to a new approach for Q6.

- 5.17 The new approach was set out in the Regulatory Policy Statement in Annex E:
- E.79 Decisions about pensions have long-term consequences for both company and users. The CAA, therefore, considers that it would be helpful if its final proposals document includes a statement of intended future policy setting out how it would expect to deal with pensions at the next review.
 - E.80 The CAA's current thinking is that there is advantage in moving progressively away from the separate assessment of salary and pension costs towards a regulatory approach in which labour costs are evaluated holistically, and discretion afforded to the regulated companies – in this case Heathrow and Gatwick airports – to decide how best to remunerate staff.
- 5.18 There is no recognition of this either by the CAA or by GAD, who appeared to be unaware of this policy and made suggestions that the CAA should adopt a clear policy for future reviews (paras 6.8-6.10). This led GAD to put too much emphasis on previous precedents and to assume that the CAA had intended to allow for no reduction in benefits (para 5.10) during Q5, whereas in fact the reason given by the CAA for allowing 25% rather than the 20% recommended by the CC, was to give the airport time to adapt to its new pensions policy.

Opex allowance for future pension service costs

- 5.19 The CAA proposals should be consistent with the RPS unless there is an explicit change of policy and we have not seen this. This means that a reasonable allowance for remuneration should be set holistically rather than treating pension costs independently.
- 5.20 The assumptions about pay are a significant factor in determining fair contribution rates. In the Q6 review, as in the Q5 review, the CAA has found that pay is well above market rate, so this time the opex allowance has been based on (at least) a real terms pay freeze.
- 5.21 The GAD report assessed the future contributions that would be needed assuming two modest benefit changes:
1. A build up rate of 60ths, rather than 54ths; and
 2. Retirement at age 65 rather than at 60.

- 5.22 GAD also considered that a case could be made for further benefit reductions (para 5.11-12), based on more recent benefit changes made by other schemes, resulting in contribution rates falling to around 12%. However, the CAA appears not to have considered this seriously when making their final proposals. We think there is a strong case for taking account of more recent benefit reductions in other schemes when determining the changes that it is reasonable for the CAA to assume for Q6.
- 5.23 GAD based all other assumptions on assumptions used in GAL's own 2010 valuation report, including the rate of future pay increases. We do not have a copy of this report, and the key figures have been redacted from the GAD report, but GAL's annual report at the time states this as being RPI+0.5%⁵. Therefore we conclude that GAD's suggested contribution rate of 20% is inconsistent with the CAA's opex allowance for pay. While GAD may have been justified in judging that the rate of pay increase was "not significantly out of line with general practice", clearly they did not take account of the fact that pay was already well above market rate and therefore that increases above RPI could not be justified. If an RPI+0% pay increase were to be assumed, a lower employer contribution than 20% would be justified.
- 5.24 According to the ONS annual Occupational Pension Schemes Annual Report 2011⁶ (the latest available), the average employer contribution rate to closed private sector DB schemes of GAL's size was 14.4% in 2011 (excluding any deficit reduction payments) with members contributing a further 5.4%, a total of 19.8%. The CAA has misinterpreted this data in para 5.54-5.55 by comparing this total contribution rate (rounded to 20%) with an employer contribution rate of 25% with employer contributions by GAL.
- 5.25 We conclude that 14.4% would be a reasonable employer contribution rate, taking account of the GAD advice, and making allowances for more recent benefit reductions and no increases in pensionable pay above RPI.
- 5.26 In the same ONS report, the average employer contribution to open DC schemes was 6.5%, with a further 2.8% from members. There is no reason why GAL could not bring its own DC scheme into line with market averages. We do not accept that salary sacrifice arrangements make comparisons difficult, especially as many employers now offer this.

⁵ Note 26, Report for year ended 31/3/2011

⁶ http://www.ons.gov.uk/ons/dcp171766_276117.pdf

5.27 A weighted average, based on average schemes, would therefore be:

DC scheme: 7% x 605 members

DB scheme: 14% x 1628 members

Average c 12% of pensionable pay, reducing as older employees on the DB scheme leave the company and are replaced by new joiners on the DC scheme.

The current deficit

5.28 However, as a matter of principle, GAL's shareholders should bear the risk of deficit payments, given that:

- any deficit is likely to reflect, at least in part, GAL's inefficiency (pay rates and pension benefits);
- the Q5 RPS stated clearly that pensions should not be considered a cost pass through, but would be part of a reasonable allowance for remuneration; and
- risks should in principle rest with those best able to manage them, so that GAL has a proper incentive to address these long term risks efficiently and fairly.

6. WACC

6.1 The ACC believes that the CAA's estimate of WACC of 5.95% (compared with an effective rate of 6.3% in Q5) is inaccurate in three key respects and fails to reflect the WACC of a notionally efficient airport:

- The cost of debt is excessive and the ACC understands the CAA has made errors in its calculations;
- The reduction of gearing to 55% and increasing beta is not based on evidence;
- The CAA is wrong to take a point at the top of the range, implying illogically that all uncertainty is in one direction. The decision on the range also fails to account for the CAA change of policy on reinvestment of returns.

The cost of debt

6.2 The CAA's proposal to increase the cost of debt is based on complex evidence. The ACC does not have the resources to scrutinize this assessment, but is aware of the work done by CEPA and British Airways, which concludes that there are errors in the CAA's approach. The ACC therefore believes that the CAA's proposal to increase the cost of debt to 3.2% is unjustified. The cost of debt is a key component of WACC which must be based on clear evidence.

- 6.3 Further, the ACC considers that there is no justification for the CAA simply to “aim up” to deal with any uncertainties. This is inefficient and not in the interests of passengers because it locks in a high cost of debt and therefore higher prices.

Gearing and beta

- 6.4 The ACC does not consider there is a rational basis for reducing the gearing assumption to 55% for a notionally efficient company of GAL’s size, while also increasing the beta. This is below GAL’s current gearing and its stated intention to its own investors. The CAA/PWC analysis also found that GAL has issued bonds in Q5 at rates lower than HAL on average (2.9% vs 3.3% for HAL). Finally we do not consider that the CAA or PWC have taken account of the evidence provided that traffic risks in Q5 are not representative of future risks, because of the one off effects of the abolition of the Bermuda II agreement.

Point estimate within the range

- 6.5 The ACC does not support the CAA’s proposal to select a point 75% along the range for LGW. Selecting a point high in a range compounds uncertainties and possible errors within each constituent range and also illogically assumes that many of the numbers could be wrong in the same direction at the same time, without considering whether some of these would be likely to balance.
- 6.6 It is also inconsistent with approaches taken by other regulators and ignores the CAA’s stated intention to make no reduction for the reinvestment of returns by GAL, but to take this into account when selecting the point in the range. The CAA asserts that the cost of underestimating WACC is very much greater than the costs to passengers of over estimating WACC and implies that the best estimate might be above the midpoints of constituent range, but no detail is given to explain this further. The CAA also states that the decision is “ultimately a matter of judgement”.
- 6.7 We disagree strongly and also consider that the CAA has not justified its proposal, which appears arbitrary.
- 6.8 The approach is also inconsistent with the specific circumstances of the Q5 review where the future growth in the size of the RAB was larger (33% growth over Q5 compared to 3% for Q6): investment was clearly more important and strategic and the consequences of getting it wrong are now clearly much less significant. In Q5, the CAA had already made what was then a relatively large change in WACC.

- 6.9 We understand that the CAA has not made correct adjustments for the different rates of inflation used by PWC and the CAA. Once this correction is made, the CAA's point estimate is right at the top of the PWC range, well above even the 75th percentile.
- 6.10 The ACC concludes that the CAA's estimate of WACC is based on serious errors and misjudgements which all operate in the interests of GAL's shareholders and against the interests of passengers.

Commercial and Other Revenues

- 6.11 The ACC considers that the CAA has not properly considered the expert evidence put forward by Javelin about the scope for improvement by an efficient airport operator and has put too much weight instead on criticisms by GAL based on their current stated intentions for developing the retail business. Indeed it seems that the CAA has not examined the ACC's evidence at all but just had their own consultants look at it.
- 6.12 In particular, neither SDG nor the CAA appear to have put any weight on Javelin's evidence and experience in the following areas:
- the likely impact of tobacco display restrictions in 2015 based on experience elsewhere and the ability to offset reductions by reallocating space to growing areas such as cosmetics;
 - the potential for more flexible catering arrangements to cater for peak loads rather than dedicating fixed space, which could be more productively used for retail;
 - the ability for GAL to exploit e-commerce revenues.
- 6.12 Rather than examining the updated business cases for retail projects, SDG has simply cited this rather generally as a factor, among other "stretch" factors that would allow upside potential, presumably to show that the forecasts are readily achievable. In addition, the CAA has cited the strengthening economy as a reason to take account of opex risks, without making a corresponding adjustment for retail revenues.
- 6.13 The ACC considers that the CAA has taken an overly conservative view of the commercial potential in Q6 and has not taken due account of clear evidence from

Javelin, from business cases and from the strengthening economy that would all point to significantly higher retail revenues per passenger. Combined with the effect from increased traffic we would expect to see a significant increase in retail revenue in the CAA's final proposals.

Other Charges

- 6.14 The CAA has made significant reductions in the forecast revenue from other revenues. The ACC does not consider that there is a proper basis for this. . We have seen nothing in the CAA consultation paper or in GAL's charges consultation material to suggest that the efficiencies will lead to the income reductions suggested. We conclude that these may have been exaggerated. In the limited time available for this consultation we have been unable to understand the basis of the CAA's reductions but request that the CAA makes these clear.
- 6.15 The specified charges which encompass: check-in, baggage, utilities, staff car parks, staff IDs and PRM total together over £60m by end of Q6. The numbers provided by GAL show an increase in real terms over Q6. The three main activities: check-in and baggage, PRM and utilities which account for 80% all show material real increases during Q6. Check in and baggage increased, by 76% from £13.6m to £23.9m, since the beginning of Q5 through to the end of Q6. This is an example of poor management costs. In the ACC's view, the CAA must enforce upon GAL effective management of the cost base and not allow GAL to pass on poor cost management onto the passengers
- 6.16 GAL have told the ACC that they will consult with airlines at least 3 months prior to raising prices. The ACC would like this to be within the licence to ensure full consultation is met.
- 6.16 We expect the CAA to continue with the measures that were used in Q5 and to include these in a licence; to protect users from any exploitative increases in such charges, we welcome the following measures:
- The ACC ask that the CAA ensures that all data, with the supporting material on underlying costs and volumes provided by GAL to airlines should provide a transparent benchmark which airlines can use to measure any subsequent changes in actual charges during Q6, and against which GAL would need to explain any such variances arising from changes in input costs and/or assumed volumes.

- A confirmation within the licence that airlines will continue to benefit from the transparency conditions imposed following the 1990 public interest finding by the then Monopolies and Mergers Commission.
- 6.17 The ACC note that there may be some opportunities to reduce the costs, and therefore the revenues, but it noted that this was unlikely to have any net impact on Q6 prices as both the costs and revenues would reduce by the same amount. We would like to see a pass through of any reduction in prices.
- 6.18 One reduction that GAL have begun to consult on is the cost of PRM charges. However the reduction only comes with a 14 day notification, which not all airlines have the technology to do, the rest of the PRM costs rise considerably from 65% - 31.3%.
- 6.19 The commitments do not encompass all the charges paid at the airport, thus exposing passengers to significant risk from residual charges.

7. Service

- 7.1 The ACC and GAL has made good progress on the outstanding elements of the service quality regime and therefore below we only discuss those elements where agreement has not been reached or the ACC feels it is necessary to provide clarification to the CAA;
- 7.2 Allocations – The allocation of rebates across the service quality metrics is agreed and has been shared with the CAA in our joint letter dated 17th August 2013
- 7.3 The airfield availability metric has been agreed with GAL and the details of which are covered in our joint letter dated 9th Oct 2013. Therefore this needs to be reflected in the licence or commitments.
- 7.4 Outbound baggage: The core metrics have been agreed including the allocation of rebates. Further work is required to understand the core service level and also the number of acceptable chute fulls. The ACC and GAL agreed to undertake analysis of data captured in September and October before agreeing these points. It is anticipated that agreement will be reached before the end of November. Therefore this should be reflected in the licence or the commitments.
- 7.5 Within Section C of GAL's proposed commitments there are a number of areas where the ACC feels they need to adapt its proposals

- GAL has proposed that Core Service Rebates will not be paid to Airlines who fail to achieve Airline Standards and that future rebates will not be paid if there are outstanding rebates from such airlines to GAL. The ACC believe that this is unnecessarily punitive and should be removed from the commitments.
- PRM service and pre-notification figures should not be published as airlines should not be judged on pre notification when passengers are allowed under legislation to request assistance without the need to pre-notify airlines. The AOC has negotiated a service level agreement with GAL as the provider of the services and it would be appropriate to publish GAL/OCS performance against that SLA including the number of failures to reach agreed engagement standards.

PART B – THE APPROPRIATE FORM OF PRICE REGULATION FOR GAL FROM APRIL 2014 AND THE CAA’S EVALUATION OF THE VARIOUS OPTIONS

8. Commitments

Summary

- 8.1 The ACC has supported the CAA’s intention to reduce regulatory costs, target regulation more effectively and promote competition, but we have concluded that the approach set out in the final Q6 proposals, based on GAL’s current Commitments⁷, will not realise the benefits claimed.
- 8.2 We also consider that the CAA has wrongly concluded that the Commitments price is comparable to the ‘fair’ or RAB price based price and has relied on this when proposing Commitments over alternative approaches. This approach is neither commercially or legally appropriate and is in any case based on an inflated RAB price.
- 8.3 A major disadvantage of the proposed approach is that the CAA appears to be unable to change any of the terms of the Commitments before adopting them and unwilling to make adoption conditional on GAL making any changes. This was

⁷ We understand that the Heads of Terms version issued in September is the current version and that an earlier (August) version has been incorporated in the Conditions of Use agreement.

explained in a recent letter from Andrew Haines to the chief executives of easyJet, British Airways, Thomson Airways and Virgin Atlantic:

“...Ultimately, it is, of course, in the nature of the Commitments that the CAA has to decide whether or not to accept them as a basis for the control or to reject them and revert to a different type of regulation...”

- 8.4 We see no advantage to the regulator in fettering itself in this way. This approach also undermines the current consultation process, if the CAA cannot make changes to key terms, including the price.

Regulatory approach

- 8.6 The form of regulation should be consistent with the CAA’s statutory duties and should provide an effective constraint on GAL’s market power.

- 8.7 ACC airlines have been happy to consider whether a Commitments based approach could work in a more efficient and targeted way than a traditional RAB based approach. We have also considered whether Commitments might be likely to result in greater competition between airports, which is an objective we support in principle.

- 8.8 The ACC believes that the CAA’s proposed evaluation criteria provide a helpful and pragmatic evaluation framework, summarizing as they do the CAA’s formal duties.

- 8.9 At this stage, the ACC considers that GAL’s proposed Commitments do not satisfy the CAA’s criteria. The major concerns are that the Commitments:

- *do not properly protect users from GAL’s ability to exploit its pricing power.* The Commitments price is higher than an equivalent efficient RAB based price. Under Commitments, GAL would also be able to increase prices by passing through R2 costs, or by levying premium charges for existing services, or by demanding additional payments to deliver necessary projects, or by gaming security costs. There is therefore considerably less price certainty;
- *are unlikely to promote airport competition* because Gatwick has market power and many airlines do not have realistic alternative airports for their operations (and those that do cannot discipline airport behaviour overall). In any case, pricing flexibility, product differentiation and growth incentives are all possible under a RAB based approach, should the airport wish to offer greater flexibility, and the

benefits of a longer settlement to facilitate bilateral contracts would also be available under a 7 year RAB based approach.

- *May not result in efficient and effective investment*, because without a RAB or any triggers, there would be little incentive for GAL to invest in areas where there was benefit to users, but no incremental benefit to the airport.
- *Are no more proportionate than a RAB based approach* given that the CAA work necessary to establish a “fair” Commitment price is the same as the work necessary to establish a RAB price. There would also need to be a continued effort from the CAA to monitor and enforce the licence and an increased burden placed on airlines who would have the primary responsibility to try and ensure that GAL honoured its Commitments, which are more complex than a RAB price control.
- *Suffer from practical implementation problems*. The ACC is especially concerned that the CAA’s preferred approach removes the ability of the regulator to adjust individual terms in the settlement, but must rely instead on GAL’s willingness to make changes. The CAA is therefore faced with a simple ‘take it or leave it’ choice over all key elements of the settlement. Alternative approaches would give the CAA significantly more flexibility to deal with unfair, unreasonable or badly worded terms.
- *Have failed to inspire stakeholders with confidence*. There is little or no support for the current version of Commitments among airline stakeholders. This was made clear in the ACC interim response of 22 October, and in an earlier letter to the CAA from the chief executives of the four largest airlines at Gatwick. Equally, GAL does not support the CAA’s proposed licence framework for the Commitments, which both the CAA and ACC consider to be essential. A radical new approach such as Commitments should be able to command broad stakeholder support and recognition that there are significant overall benefits. This is not the case.

8.10 Therefore, while the ACC supports the CAA’s intention to reduce regulatory costs, target regulation more effectively and promote competition, we conclude that the proposed approach, based on GAL’s current Commitments (and on bilateral contracts that have not yet materialized), will not achieve this. We also consider that the CAA has wrongly concluded that the Commitments price is comparable to the “fair” or RAB based price and relied on this when proposing Commitments over alternative approaches.

Key differences between the Commitments price and a RAB based “fair” price.

8.11 The CAA’s assessment of the merits of accepting GAL’s Commitments rather than imposing a RAB-based control is set out in Section 10 of the Final Proposals. Part of the CAA’s assessment involves a comparison between the price commitment offered by GAL under the Commitments and what it calls the ‘fair price’ calculated under a RAB-based approach. As the Commitments are for seven years but RAB-based controls are typically for five years, the CAA comparison is with ‘fair prices’ for 5 year and 7 year periods. The CAA concludes as follows:

“...the commitments blended price is below the CAA’s five year RAB-based price but marginally above the seven year fair price...”⁸

8.12 The CAA also says that it considers that it should put more weight on the five year fair prices because the seven year price has to be considered less certain given that it was developed from the five year price rather than from a separate bottom-up analysis and because there may be greater traffic risk over 7 years.

8.13 We have serious issues with comparisons that the CAA has made:

- *Time period:* the CAA places greater weight on the 5 year RAB price and compares this with a 7 year Commitments price. This is clearly unequal. The CAA notes some uncertainty with costs of a 7 year RAB period, but the capex in the additional years is based on GAL’s own assessments. There is uncertainty with any forecast and other regulators have adopted longer control periods than 5 years. In any case, any additional risks faced by GAL could easily be offset by the potential for greater upside – notably the opportunity to retain outperformance benefits for longer.
- *Capex:* The most significant difference is that the Commitments only commit to a minimum spend of £100m on capex per year compared to around £160m per year used to calculate the RAB-based framework. The CAA acknowledges this lower capex commitment as a drawback of the Commitments⁹ but it does not adjust the prices it uses in its comparison to reflect it. The CAA seems to suggest that it could, after the start of the price control, look to introduce additional licence conditions to address its concerns over the ‘flexibility’ in the capex plan¹⁰but it does not follow that it could actually require GAL to invest more without re-opening the whole price control process. It is clear that GAL’s price is based on only a minimum

⁸ Paragraph 10.89

⁹ Paragraph 10.98

¹⁰ Paragraph 10.109

commitment of £100m per year and it would undoubtedly want more money if it had to invest more. The CAA should at least have adjusted its RAB-based 'fair price' comparator so that it was calculated on the basis of the same capex commitment. Over a 5 year period, the difference between the Commitments capex and the RAB based capex of £791m would be 2 percentage points on the value of "X" in the formula RPI+/-X.

- Use of the 'blended' price: The comparison the CAA makes is between the RAB-based price and the 'average' or 'blended' price commitment under the Commitments. As such it includes any lower prices offered to airlines under bilateral agreements. The price commitment for published prices is 1% per year higher. We do not consider this to be an appropriate comparison as the lower prices under bilateral agreements will not be automatically available to airlines and will only be made available in return for conditions different from those assumed in the RAB-based approach. Thus, for example, the price may be lower in return for accepting lower service standards.

The Commitments price is effectively uncapped because of the R2 provisions, compared with a RAB based approach that would require a licence change, with the decision taken by the CAA and the ability to appeal any unreasonable increase.

- Premium or other new charges: Under a RAB based approach, all such charges are included unless freely negotiated under a bilateral contract. Under Commitments, GAL can impose additional charges at will.
- Security costs: Under Commitments, GAL would have a much greater ability to increase prices – even when there was no real justification - and would not reduce them

8.14 There is a material difference between the financial arrangements under the Commitments and those under a RAB-based approach. The Commitments limit price increases by reference to a slightly broader basket of prices (i.e. including Selected Ancillary Service Charges). If these were stripped out, it might imply higher increases in the relevant airport charges.

8.15 When compared more appropriately, we believe it is clear that the Commitments price is higher than the RAB-based price. Further, we have shown in Section A (our comments on the 'fair price') that the RAB-based price is itself more generous than it should have been because of errors in the calculation of certain elements.

Claimed wider benefits of Commitments

- 8.16 The CAA identifies three "*issues pointing towards accepting a commitments price above the fair price*", acknowledging that the commitments price is above the 7 year RAB-based price). In the ACC's view, any such benefits are weak and are insufficient to overcome what we consider to be a significant price difference under the two approaches.
- 8.17 "the greater period of certainty to airlines and consequently the greater risks to GAL"
- 8.18 As discussed above, there is less price certainty under Commitments because GAL is able to demand various additional payments. We see no basis for concluding that the longer period works in favour of airlines (and therefore passengers) or that the risks only accrue to GAL. It was GAL that proposed the 7 year period. Either side could benefit and the longer period does not itself justify a higher price.
- 8.19 "the commitments would lock in the forecast reductions in prices in the subsequent control period, which often have a tendency of not transpiring, with new cost pressures emerging so the actual price ends up higher";
- 8.20 This is entirely speculative and in any case, no price reductions are proposed. Prices would increase above inflation for longer. Again, this could benefit the airport rather than airlines and cannot justify a higher price.
- 8.21 "the risk that GAL could walk away from the commitments if the CAA sets the price, removing the other benefits from the commitments in terms of flexibility and greater tailoring to individual airline needs".
- 8.22 It is not obvious that these benefits really exist as they appear to rely on assumptions that the RAB-based control must retain the structure of previous quinquennia when there is no particular reason that it would have to do so. The Civil Aviation Act 2012 was introduced precisely to give the CAA more flexibility in the form of price regulation, including the possibility of longer control periods and more tailored arrangements. Similarly, the capex provisions could be changed to reduce bureaucratic procedural requirements and to allow more flexibility. Again, the threat that GAL might walk away is insufficient reason to justify a higher Commitments price.

ACC concerns with the terms of the Commitments

- 8.23 The ACC set out some of its concerns with the Commitments in its interim response of 22 October, attached as Annex A. In addition, easyJet, Virgin and British Airways have made their own interim submissions emphasizing the importance of some of these issues and raising additional matters where there was not time to assess with the full ACC.
- 8.24 The comments in this section summarise and highlight the main concerns expressed in these interim submissions.
- 8.25 In summary, the ACC interim submission identified the following problems and offered solutions to them:
1. Various typographical and other errors which appear to be mistakes (including an obvious major error in the formula for service rebates);
 2. Unbalanced waiver and indemnity clauses;
 3. Unreasonable restrictions in the dispute resolution mechanism with a short limitation period and a ban on launching court proceedings before exhausting the process
 4. The ability for GAL to impose premium charges on top of the price commitment, outside contracts and without agreement or approval
 5. Serious inadequacies with the definitions of key price/revenue terms, which have the effect of creating ambiguity about key provisions and allowing GAL to determine and change at will what services are or are not covered by the price commitment,
 6. A problem with the security cost pass through formula, which already fails to allow for security cost reductions and would also allow major price increases even when costs over the period fell below the level assumed by the CAA in its “fair price” calculation
 7. A failure to protect selected ancillary charges from the 10% annual price increase cap
 8. GAL’s right to recover unlimited costs of developing a second runway regardless of whether or not the expenditure is necessary, efficient or appropriately timed;
 9. A provision automatically excluding airlines from service rebates if they have a bilateral contract that varies *any* of the Commitment terms – unless expressly included in the bilateral agreement;
- 8.26 The ACC is pleased to see that the CAA has recognized the need to make further changes to the Commitments and/or licence and has written during the consultation period to ask GAL to reflect both on the airline submissions and their own

suggestions for resolving the problems with the second runway costs and premium service charges.

Treatment of Runway 2 costs

- 8.27 As drafted by GAL the commitments could allow GAL to develop Runway 2 plans and costs without either airlines being consulted or the CAA determining that the costs are efficient. This is not acceptable to airlines at Gatwick. It is also inconsistent with the CAA's treatment of Heathrow and its expected finding that Gatwick has market power.
- 8.28 As Gatwick has market power it is not reasonable for it to be able to determine potentially very large runway 2 costs outside the licence change process. The ACC set out in its interim submission (see paragraph 2.7(g) in Appendix I) how the CAA can address this issue without requiring a change in GAL's commitments. This would be achieved by the CAA putting in place a licence condition requiring that any Runway 2 costs that GAL wants to charge to airlines must be assessed by the CAA, via the licence change process.
- 8.29 The CAA's latest proposal is to impose a licence condition requiring the costs to be efficient and the CAA to approve any such expenditure. While this is clearly an improvement, the proposed approach could lead to drip feeding of runway 2 costs by GAL and would deny airlines – and GAL – the right to appeal any CAA decision to the Competition Commission/CMA. Given the significant sums that could be involved, this is inadequate. The ACC therefore continue to believe that its own proposed condition should be implemented.

Additional uncapped charges

- 8.30 The CAA has also recognized that Gatwick should not be able to move charges/revenues for existing services outside the scope of the regulated charge. Gatwick has committed to charging airlines no more than RPI+1.5 over the Q6 period. However, if it created new charges outside this commitment then Gatwick could create additional unregulated revenues.
- 8.31 The CAA's recent proposal to deal with this through a licence change unfortunately will not work, as drafted, for the following reasons:
- It does not make sense to establish "Premium Service Charges" as a new defined term when the term is not then used anywhere in the licence. No obligations are imposed as to what GAL can or cannot do in relation to

Premium Service Charges. As such, the provision is essentially meaningless as it stands at present. It is to be noted that "Premium Service Charges" is not even used in any meaningful sense in the draft Conditions of Use. Its only appearance is in Appendix I where it is a heading for possible charges but it currently says there are none. The CAA needs to come up with an operative provision in the licence that uses the defined term.

- In addition, the definition is too narrow because it only talks about "charges for services that, as at 1 April 2013 were not covered by..." and defines "airport charges" as "charges levied...". This could be interpreted as meaning that a charge is not caught if it was not actually being levied at 1 April 2013 even if for the same sort of service for which charges were being levied at 1 April 2013 that fell within "airport charges" or "ancillary charges". Likewise, it could be said that if a service was not actually being provided at 1 April 2013 then it could not have been covered by "airport charges" or "ancillary charges". In short, the drafting focuses too much on the present situation and needs to be changed to at least incorporate the concept of services that are "similar to" or "substitutes for" services currently within "airport charges" or "ancillary charges".
- It is not clear why this suggested new licence condition would fit in as Condition CI.5B. It does not have anything to do with modifications, the subject matter of CI.4 to CI.6.

Other changes

- 8.32 The CAA letter does not deal with all the other changes highlighted by the ACC, including for example the significant flaw in the proposed treatment of the security cost pass through (the S term). The intent of this term is for Gatwick to be able to pass on any costs imposed by a change in the security regime imposed by government and regulators. This term should also be symmetrical, so passengers can benefit from any change that leads to lower costs
- 8.33 However, the drafting of this term in GAL's commitments would allow it to recover any increases in security costs, even if total costs are at levels below those at the start of the regulatory period. Further, passengers would not benefit from any reduction in costs.
- 8.34 In conclusion, the ACC considers that this is not a reasonable set of conditions. The ACC asks the CAA to ensure that either the commitments are changed to reflect these concerns or that its licence condition rectifies these flaws.

PART C – THE APPROPRIATE LICENCE CONDITIONS THAT WOULD BE ASSOCIATED WITH GAL’S PROPOSED COMMITMENTS

- 9.1 The ACC provided comments on the proposed licence framework in Section 3 of its interim response to this consultation of 22 October and those comments are confirmed. See The Annex.
- 9.2 The ACC also commented on the form of regulation section above Part B on the CAA’s two latest proposed amendments set out in a letter of 28 October to deal with the second runway costs and premium service charges. More generally, We welcome the CAA’s willingness to use licence conditions to deal with problems identified in The Commitments if GAL is unwilling to make changes. However, we are unclear whether this would be a suitable mechanism to deal with all such problems. The ACC would expect the CAA to discuss with airlines on any further changes to the commitments or the licence.

APPENDIX I

CAA's FINAL PROPOSALS – INTERIM SUBMISSION

1. Introduction
 - 1.1 This note is an interim submission by the Gatwick ACC to the CAA's final Q6 proposals for Gatwick Airport.
 - 1.2 This note is primarily concerned with the drafting of:
 - (a) *The new draft Conditions of Use prepared by Gatwick Airport Limited ("GAL") with the intention of incorporating its Commitments, as recently published by the CAA (the "Proposed Conditions of Use");¹¹ and*
 - (b) *the draft Licence appended to the Final Proposals.¹²*
 - 1.3 Whilst we have raised a number of important substantive issues - as well as drafting points - we have not sought to deal in this note in any detail with our overriding concern that GAL's proposed pricing under the Commitments is at a level that is just too high. We will deal separately with this issue in another note to be provided in response to the CAA consultation but, in brief:
 - (a) *The comparison the CAA makes between its "fair price" and the pricing in GAL's Commitments does not compare "apples with apples". A comparison based on the same assumptions as to capital expenditure, service quality rebates, duration and other terms would show that the price in GAL's Commitments is well above the "fair price"; and*
 - (b) *The "fair price" is, itself, higher than it should be for all the various reasons previously submitted and which we will revisit, where appropriate, in our forthcoming note.*
 - 1.4 The ACC would like to make it clear that we are unable to support the Commitments as currently drafted in the Proposed Conditions of Use as updated by the revised (September) Heads of Terms document.
2. The Proposed Conditions of Use
 - 2.1 We set out below our various comments on the Proposed Conditions of Use broken down as between the different sections of the document.

¹¹ See <http://www.caa.co.uk/docs/78/Conditions%20of%20Use%20%20270813%20unmarked.pdf>. A pdf copy of the document as it existed on 21 October 2013 is provided with this advice in case the document at the linked page subsequently changes.

¹² *Economic Regulation at Gatwick from April 2014: final proposals* published on 3 October 2013.

(i) *Variation of the Commitments*

2.2 There are two typographical errors in Condition 2.1.3:

- (a) *The Condition that refers to Term is Condition 1.1.23 not 1.1.2.3; and*
- (b) *It should say "other than" in the penultimate line of the Condition rather than "other then".*

(ii) *Waiver and Indemnity*

2.3 Conditions 2.1.9 to 2.1.11 are, as currently drafted, solely for the benefit of GAL. This was arguably appropriate when the Conditions of Use were purely a private document and only imposed obligations on Operators but there is no justification for this approach continuing where the Conditions of Use impose obligations of a regulatory nature on GAL. The provisions should be mutual such that:

- (a) *no failure or delay by an Operator to exercise a right or remedy under the Conditions of Use (or a partial exercise of rights) is to be taken as precluding any further exercise or acting as a waiver of any breach (Condition 2.1.9);*
- (b) *any express waiver by an Operator is to be strictly and narrowly construed (Condition 2.1.10); and*
- (c) *GAL shall keep all Operators indemnified against any losses caused by GAL's breach of the Conditions.*

(iii) *Dispute Resolution Procedure*

2.4 Although the proposed text is consistent with that in the Heads of Terms from September 2013¹³ (the "Heads of Terms"), we believe that there are certain undesirable features in the currently proposed Dispute Resolution Procedure (Conditions 2.1.12 to 2.1.21). In particular:

- (a) *Although not as clear as it could be, it appears from Conditions 2.1.12, 2.1.19, 2.1.21 and 2.1.23 that GAL's intention is that neither party should be able to take a dispute to court without first exhausting the temporarily binding expert determination process (other than to seek urgent injunctive relief). Given that the expert determination is only supposed to be binding until superceded by a court judgment, we cannot see that there is necessarily a benefit to requiring a delay to commencement of the court process. The Heads of Terms indicated that the expert determination process was supposed to follow the adjudication approach*

¹³ *Heads of terms of Airport Commitments in relation to Airport Services & Charges beyond Q5* (Finalised Draft September 2013) available at <http://www.caa.co.uk/docs/78/20SeptemberFinalCommitmentsProposals.pdf>. A pdf copy is also provided with this advice.

provided for by Section 108 of the Housing Grants, Construction and Regeneration Act 1996. The adjudication process provided for by that Act does not prevent simultaneous or alternative recourse to the courts. There may be occasions where there is no benefit in obtaining a temporarily binding resolution and where it is better to be able to go straight to court. The Parties should not be prevented from immediately pursuing their avenues of redress before the courts.

(b) Condition 2.1.19 imposes a very short limitation period for any legal proceedings in relation to a dispute or an expert determination of a dispute, namely 90 days from the expert's determination. We do not believe that this shortening of the limitation period is appropriate or helpful. Ordinarily, there would be a limitation period of six years from the alleged breach of contract. As currently drafted, it may be that one party can refer a dispute to the expert before all the facts are known and thereby force the other party either to issue a claim when not fully prepared or able to make out its case or otherwise lose its right to bring any claim. This is a particular issue for the airlines where, if all are affected, there will be a need to coordinate a response that will make it particularly difficult to comply with short deadlines. We consider that Condition 2.1.19 should be deleted in its entirety.

(iv) Operational

2.5 We have spotted an apparent typographical error in Condition 2.2.2. We believe that the last part of the last sentence should say "...prohibiting the Operator or particular services of the Operator from operating from the airport for a fixed period of time".

(v) Price Commitment

2.6 The ACC remains of the view, as indicated in previous consultation responses, that it is inappropriate for GAL to maintain a concept of Premium Service Charges that are payable even in the absence of Bilateral Contracts but outside the effective price cap. It should be sufficient that it is open to GAL and any airline to enter into a Bilateral Contract for delivery of different services. We do not understand why there might be any need for something additional. We would propose the deletion of the concept of Premium Service Charges.

2.7 We have the following comments on Schedule 2:

(a) We note that there may be scope for ambiguity and/or subjective interpretation by GAL in the reference to "charges equivalent to the Core Service Charge and Selected Ancillary Service Charges" in the definitions of 'Aggregate Blended Revenue' and 'Aggregate Core Revenue' in Paragraphs 1.1 and 1.2 respectively. This could be important given that the phrase is used to define what charges under Bilateral Contracts are taken into account in calculating compliance with the Indicative Yield Profile Commitments. We consider that it should be made clear

that Aggregate Blended Revenue and Aggregate Core Revenue include the revenue from all charges under Bilateral Contracts save to the extent that the charges are made for services that are genuinely different from and additional to those that GAL is required to provide and/or does provide in the absence of Bilateral Contracts. There should be a presumption that all Bilateral Contract charges are included unless GAL can make out a clear case for their exclusion.

- (b) The definition of 'Core Service Charge' is not adequate because defining it as "...those charges referred to in Appendix I of the Schedule of Charges as may be varied from time to time..." leaves GAL scope to unilaterally change the types of charges that fall within this crucially important definition as Appendix I of the Schedule of Charges is subject to unilateral change by GAL subject only to the requirements of the Airport Charges Regulations. The definition should, instead, indicate that it includes all charges other than a specific list of items to be provided in the first instance by GAL. If GAL considers that the list should change in the future then it can seek a modification but the presumption should be that charges fall within the effective price cap unless it is established that it is not appropriate to do so.
- (c) The defined term 'B_t' in Paragraphs 1.7, 1.10 and 1.11 of Schedule 2 is now redundant given that bonuses have been deleted. Paragraph 1.7 should be deleted and the other two paragraphs should be amended to remove reference to B_t.
- (d) For consistency with Heathrow's licence, and for greater clarity, we would propose that GAL should redefine 'RPI_{t-1}' (Paragraph 1.16) as "the percentage change (positive or negative) in the Office for National Statistics (ONS) CHAW Retail Price Index between August in year t-1 and the immediately preceding August"¹⁴.
- (e) The defined term 'S_t' (Paragraph 1.17) used to effect the security cost pass-through is problematic for a number of reasons, as follows:
 - (i) Paragraph 1.17.1 is not consistent with the Heads of Terms and Final Proposals. It currently allows GAL to pass-through 90% of the increase above £1m rather than 90% above £1.75m as set out in the Heads of Terms (September version). We suspect that this issue is simply the result of the Proposed Conditions of Use having been drafted before the changes made in September;
 - (ii) Paragraph 1.17.1 still allows GAL to pass-through increases in costs without passing-through any reduction in costs. The ACC has previously complained about this and the CAA agrees that it "does not consider that this would operate in passengers' interests and it could affect the overall price in the Commitments" (paragraph 10.99 in the

¹⁴ Text from Condition C1.2 in the Heathrow Draft Licence appended to the CAA's Final Proposals for Heathrow.

Final Proposals). Despite recognising the issue, the CAA has not offered any solution through its licence provisions or otherwise. The Proposed Conditions of Use should be amended so that reductions in security costs are also passed through.

- (iii) Paragraph 1.17.1 compounds the unfairness of only passing-through increases by looking only at increases in one year, implicitly against the amount paid in the previous year. This has the result that Operators could theoretically be charged extra even if the total cost of security is less over the duration of the Commitments than in Q5. Thus, to provide a worked example, assume the following hypothetical security costs:

2013/14 (i.e. current price control)	£100m
2014/15	£50m
2015/16	£60m
2016/17	£70m
2017/18	£80m
2018/19	£90m
2019/20	£100m
2020/21	£100m

In this situation, there would be an "increase" in every year of the control apart from the first and last year with £9m passed through in each of the years from 2015/16 until 2019/20 such that Operators pay an extra £45m in charges even though the total cost of security is £150m less than if costs had remained flat across the whole duration of the Commitments.

At a minimum, the only increase allowed should be that which is (i) an increase on the amount paid in 2013/14; and (ii) an increase on the previous highest amount of security costs paid in any year of the Commitments.

- (f) *Paragraph 5 of Schedule 2 should be amended to clarify that "GAL shall set the Core Service Charges and Selected Ancillary Service Charges in any Relevant Year with the intent that the Core Yield shall not exceed the Core Yield in the prior year by more than RPI + 10%...". We see no justification for limiting this provision to Core Service Charges when the Core Yield relates to both Core Service Charges and Selected Ancillary Service Charges (as emerges from the definitions of 'Core Yield' and 'Aggregate Core Revenue' in Paragraphs 1.5 and 1.2 respectively).*
- (g) *We note that Paragraph 6.2 of Schedule 2 continues to place little restriction on GAL's pass-through recovery of Runway 2 costs despite the CAA identifying this as*

an issue (paragraph 10.94 of the Final Proposals). The CAA's indication that it could look to modify the licence if GAL did not strictly obey its views on Runway 2 cost recovery (paragraph 10.109 of the Final Proposals) does not offer much comfort given the limits on the CAA's ability to modify the licence and GAL's ability to appeal any modification. We propose, instead, that paragraph 6.2 is deleted and there is an additional licence condition as follows:

"New Licence Condition C1.5A

If following the completion of the Airports Commission the Government supports the development of a second runway at Gatwick Airport (or if Gatwick is permitted by any other mechanism analogous thereto) then the Licensee may propose amendments to the indicative price path set out in the Commitments to allow for the recovery of the reasonable costs in respect of the development of a second runway. Notwithstanding the provisions of Condition C1.4, any such proposed amendments shall be treated as proposed modifications to this Licence, the acceptance of which would be subject to the provisions of the Act governing the modification of licences."

(vi) *Service Commitments*

2.8 Page 12 of the Heads of Terms anticipated that airlines might continue to qualify for service rebates under the Conditions of Use even if they entered into Bilateral Contracts albeit that the Bilateral Contracts would specifically provide for that eventuality. As currently drafted, Condition 6.3 anticipates that rebates will only be available to Operators operating exclusively under the Conditions of Use. Whilst the terms of any Bilateral Contract could override this restriction, we consider that it would be better to expressly recognise in Condition 6.3 that rebates will continue to be payable under the Conditions of Use unless expressly excluded by the terms of the relevant Bilateral Contract.

2.9 Paragraph 5.1 of Schedule 3 should use the defined term "Bilateral Contracts" rather than "bilateral contracts".

2.10 The Proposed Conditions of Use need to be amended to reflect the agreement reached between GAL and the airlines on the Service Rebate Percentage and Annual Reconciliation of Rebates as set out at page 13 of the Heads of Terms (September version). We would note, though, that the formula in the Service Rebate Proceedings section of the Heads of Terms is currently incomplete since it does not clarify that 'P_{it}' needs to be multiplied by the annual forecast revenue before being divided by 12. The ACC believes this should be uncontroversial as it simply reflects the approach already adopted in Q5.

2.11 We note that no standards have yet been defined for "airfield congestion / availability" in the Proposed Conditions of Use. These should be defined before the Proposed Conditions of Use are adopted by reference to the agreement reached

between GAL and the airlines as set out in the joint letter to Tim Griffiths of the CAA on 9 October 2013.

- 2.12 We note that the service quality rebates are effectively lower than they were in Q5 because GAL has claimed the right to off-set airline service quality penalties that were not imposed in the last price control and that the CAA considers could not be imposed in a price control it would be able to adopt (paragraph 10.97 of the Final Proposals). The ACC continues to oppose imposition of standards by GAL, but in the absence of any change, GAL should at least be required to provide more generous rebates in order to maintain the same level of incentives to meet its service quality standards. Otherwise GAL would have a perverse incentive to increase airline standards as a means of avoiding rebate payments for inadequate airport services.
- 2.13 It will be necessary to ensure that the carve-outs from the service quality standards in Paragraph 4 of Schedule 3 Appendix II are the same as currently apply.

(vii) *Operational and Financial Resilience*

- 2.14 Condition 7.4 imposes an obligation on GAL to consult on its draft operational resilience plan but does not say how it should do that. There should be a more detailed statement of how GAL must consult or, at a minimum, a requirement that GAL should respect the principles of adequate consultation mandated of public authorities (through such cases as *R v North and East Devon Health Authority, ex p Coughlan* [2001] QB 213). Such a requirement would ensure that GAL consults whilst proposals are still at a formative stage, provides sufficient information and time for intelligent comment and takes account of comments received.
- 2.15 Condition 7.5 sets a minimum of only one meeting per year to discuss the requirements of the operational resilience commitment. Whilst this is consistent with the Heads of Terms, we consider that there should be more frequent meetings. At a minimum, we would propose there be two meetings per year.
- 2.16 Condition 7.6 imposes an obligation on all providers of air transport services and ground handlers to "*take the actions allocated to them in [GAL's] plan(s) during periods of disruption*". The CAA has expressed concern about the idea of GAL being able to dictate what the airlines must do (paragraph 10.102 of the Final Proposals) and that issue remains despite the use of the phrase "*reasonable endeavours to cooperate with [GAL]*" in the first part of the Condition. We would propose that GAL should delete the words "*shall take the actions allocated to them in [GAL's] plan(s) during periods of disruption*".
- 2.17 Condition 7.8 (requiring GAL's directors to confirm the adequacy of financial resources) is not now consistent with the terms of the licence provision that the CAA proposes to impose. We would propose that Condition 7.8 be deleted as it is now redundant. At the same time, however, we believe that the relevant licence

conditions should adopt the approach in Condition 7.8 of requiring GAL's directors to certify that GAL has adequate resources to deliver its core services rather than merely to provide undefined airport operating services.

(viii) *Investment and Consultation Commitment*

2.18 The consultation obligations in Schedule 4 should be clarified to indicate that GAL will be required to follow the principles required of a public authority in consulting (as discussed in paragraph 2.14 above). There could also usefully be more detail on the nature of the consultation that will be conducted in relation to the Master Plan (Paragraph 3 of Schedule 4).

2.19 There should be definitions of the Master Plan and the various Tollgates.

2.20 Paragraph 4.2.5 of Schedule 4 requires GAL to report annually on differences between the latest forecast cost of the capital investment programme and "*the forecast incorporated in the CAA's 2013 price control review*". We think this phrase is ambiguous and could cause confusion and disagreement. It would be better to refer to specific paragraphs of the Final Proposals.

2.21 We note that Paragraph 6.1 of Schedule 4 only requires GAL to meet annually with the capital sub-committee of the ACC to review GAL's delivery of the Capital Investment Programme. Whilst this is consistent with the Heads of Terms, and a full review may only be needed once per year, we consider that the Proposed Conditions of Use should reflect the existing arrangements of monthly sub-committee meetings so that it is clear that no change of approach is intended.

3. The draft Licence

3.1 On Part C, we have the following suggestions:

(a) *The first heading and the first sub-heading should delete the word "price" as the relevant Commitments go beyond the price Commitments and include Commitments as to service standards, operational resilience and so on.*

(b) *Condition C1.1 needs to be modified to reflect the different way in which GAL now proposes the Commitments are given effect. They are not merely a Schedule to the Proposed Conditions of Use but are given effect throughout the Conditions. Condition C1.1 should set out precisely which elements of the Conditions of Use are to be considered conditions of the Licence (and they can then be described by the defined term "Commitments").*

(c) *Conditions C1.2 and C1.7(a) refer to the Licensee's pricing principles and, in the former case, say that they are set out in the Commitments, but they are not now set out in the Commitments at all. It would seem that there is no need for any reference to the principles at all in the Licence.*

(d) *Condition C1.3 should be amended to refer explicitly to the Commitments so that the public interest objectives unquestionably apply to GAL's performance of the*

Commitments. It should say, "In complying with the Commitments and this Condition C1..." as though the Commitments are said to be incorporated in the Licence, we are not sure that it can be said that they are specifically part of Condition 3.

- (e) Conditions C1.4 and C1.5 each refer to "the modification provisions of the Commitments". The specific provisions should be listed to referenced in order to avoid any ambiguity.
- (f) As noted in paragraph 2.7 above, we propose that there be an additional licence condition as follows:

"New Licence Condition C1.5A

If following the completion of the Airports Commission the Government supports the development of a second runway at Gatwick Airport (or if Gatwick is permitted by any other mechanism analogous thereto) then the Licensee may propose amendments to the indicative price path set out in the Commitments to allow for the recovery of the reasonable costs in respect of the development of a second runway. Notwithstanding the provisions of Condition C1.4, any such proposed amendments shall be treated as proposed modifications to this Licence, the acceptance of which would be subject to the provisions of the Act governing the modification of licences."

- 3.2 On Part D, and as discussed in paragraph 2.17 above, we note that all the obligations are linked to a very low threshold of the ability "to provide airport operation services at the Airport". We suggest that the threshold should be higher and linked to the services currently being provided. Thus, for example, it could say "to provide airport operation services at the Airport not materially less substantial than were provided at 1 April 2014". This would need to be incorporated in Condition D1.1 and in each form of the certificate wording in Condition D1.2.

Naturally, we hope that this clarifies our position.

Yours Sincerely

Jason Holt
Chairman
Gatwick Airline Consultative Committee