



Room 2044, D'Albiac House  
Cromer Road  
Heathrow Airport  
TW6 1SD  
Tel: +44 (0) 20 8757 3936  
Email: [lavers@iata.org](mailto:lavers@iata.org)



Heathrow AOC Limited  
Room 2040-2042, D'Albiac House,  
Cromer Road  
Heathrow Airport  
TW6 1SD  
Tel: +44 (0) 20 8745 4242  
Email: [Gensec@aoc-lhr.co.uk](mailto:Gensec@aoc-lhr.co.uk)

Selina Chadha  
Group Director Consumers and Markets  
Civil Aviation Authority

Sent by email to: [selina.chadha@caa.co.uk](mailto:selina.chadha@caa.co.uk)

27 May 2025

Dear Selina

### **Airline Community comments on H8 Constructive Engagement (Round 2)**

Further to the completion of Round 2 of the H8 Constructive Engagement (CE) and the recent discussions with yourself and the CAA H8 team, we wanted to put in writing our reflections and concerns both in relation to the progress achieved in CE, but also the parallel CAA activity being undertaken in advance of HAL publishing their Business Plan.

#### Round 2 Summary

The intention of Round 2 was to understand the emerging views of airlines and HAL of the price control's building blocks, reflect on current trends and performances, and seek early input and comment from the airline community on priorities and potential HAL proposals on capital choices, expenditure and service levels.

We have had useful discussions across certain areas on which we are continuing to engage with HAL. However, as set out further in this letter, we also have significant concerns, particularly in relation to what we consider a lack of transparency, engagement and prioritisation of capital and investments. We consider this to be a key pitfall in the process so far considering the significant amounts tabled by HAL, as covered further in this letter.

We are encouraged by the discussions with HAL on the traffic forecasts. Having identified the key differences between airlines and HAL, notably growth through aircraft up-gauging, we look forward to working with the CAA in further evidencing our views as part of the independent traffic forecast it has commissioned.

In relation to service levels contained in the Measures Targets and Incentives (MTI) framework, we have welcomed the engagement and collaborative work with HAL to improve the existing framework and ensure service resilience by HAL. Whilst we are yet to align on all measures, we recognise the spirit and dialogue which have allowed for constructive development of ideas, with proposals being submitted by both HAL and the airlines. For instance, we look forward to working further with HAL on its proposal to introduce a financial rebate on its performance for timely delivery of departing baggage to the airlines, which has been a key area of service failure over the past year.

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However, we would reiterate our firm position that the MTI framework is in place to incentivise the regulated entity. As such, we have tailored our proposals accordingly to ensure, particularly from a financial perspective, these are addressing matters that are reasonably within HAL's control. We are open to having discussions on how we can collectively improve the airport's performance and operation but using MTI to enforce other parties' behaviours, or exemptions, is not appropriate.

Similarly, we note the limited engagement on Other Regulated Charges (ORCs) where we continue to have concerns on HAL's proposal to move away from a purely cost recovery mechanism, such as by using ORCs as a sustainability fund raising mechanism or to unduly encroach on airline business models and service standards. Importantly, we have yet to reach agreement on a charging mechanism that resolves the airlines' and the CAA's concern in the H7 Final Decision that passengers are financing non-airline costs they do not use.

We are moreover very much encouraged by the work being undertaken by the CAA on reviewing HAL's operating costs and commercial revenues, particularly the information being sought and the use of a bottom-up approach to establish the efficient cost baseline. It will be critical that HAL appropriately responds to the CAA's templates. We look forward to working with the CAA, its consultants and our appointed consultants to ensure efficient costs for H8.

#### CE Concerns

Notwithstanding the progress above you will be aware of our growing and significant concerns on both: (i) the proposed level of investment and lack of prioritisation of the "choices" presented; and (ii) HAL's proposals for an alternative regulatory treatment regarding investment properties.

On capital choices, we were presented with broad themes and high-level proposals. Whilst useful in understanding HAL's initial thinking, and despite our repeated requests since the Round 1 sessions in December 2024, these were not followed by a detailed or transparent engagement on the nature, scope or benefits of the projects underpinning those proposals. This has not allowed us to input on how to prioritise those investments against the broader airline priorities presented in Round 1 and against the need for an overall capital envelope that is deliverable and affordable. For the avoidance of doubt, we do not believe that the total amount which HAL presented is affordable or deliverable, and significant trade-offs will have to be made based on clear engagement of the projects considered.

We are therefore unclear on what basis HAL is incorporating airline feedback into the selection of the possible capital projects to determine its H8 Business Plan portfolio. Given the late stage of the process, we are not confident this will be feasible before the expected presentation of HAL's Business Plan in July.

We have also been particularly frustrated by the lack of HAL's engagement on the H7 rollover expenditure impacting H8, currently estimated by HAL at £4.5 billion. We are fundamentally concerned that the rollover expenditure is now being 'banked' by HAL as opposed to being prioritised against H8 projects. For clarity, we are not seeking to reduce capex in H7 but to allow for the rollover to be balanced against new initiatives that have arisen and ensure sufficient headroom for other investments in H8, including capacity and occupancy. While we understand that further information is expected in due course, this was an area that engagement should have achieved progress in time for the business plan and been straight forward for HAL to facilitate given the

programmatic approach to capital expenditure that has been implemented in H7. We have written to HAL on this issue, and attached for reference and further background<sup>1</sup>

In light of those concerns, we would encourage the CAA to consider how it can incentivise HAL to deliver marked improvement on its engagement, including how to employ the newly introduced H8 business plan incentive and the threat of a potential penalty.

With regard to investment properties, we reiterate that we are not supportive of HAL's proposal to carve out and develop certain assets outside the single till. While we have engaged and carefully reviewed HAL's proposal, we have rejected it as it will add complexity and create legal and regulatory uncertainty with no consumer benefit. In fact, HAL's approach would unavoidably create perverse incentives for where HAL seeks to prioritise its investment in the context of significant physical constraints and our ongoing discussions as to how to best deliver capacity and resilience. These risks are currently mitigated by single till regulation. We have confirmed to HAL we do not believe there is merit in engaging further on this matter; for reference, our full response can be found in the attached email sent to HAL<sup>2</sup>.

For clarity, we firmly reject any attempts to move away from single till regulation and re-iterate the rejection of the Competition Commission of previous attempts to compromise single till regulation at Heathrow on the grounds of regulatory uncertainty and the consumer harm this would generate.

#### Business Rates

Alongside the concerns on capital, the Airline Community remain deeply concerned on the potential impact business rates will have in H8; we estimate that this could be one of the single biggest cost headwinds impacting the level of the charge.

At the airlines' requests, HAL have provided high-level updates that it is in negotiations with the Valuations Office Agency (VOA) which have unfortunately not allowed for any assessment or judgement to be made on the potential impact. Importantly, HAL has not demonstrated to us the plan it has deployed to mitigate the expected increases which, contrary to other UK airports, it would seek to pass on fully to airlines. Importantly, we note that the CAA had written to HAL in September 2023 that, in view of the very significant increases expected in the 2025-26 re-evaluation, it would expect HAL to put in place a mitigation plan and that business rates would be passed through where there is evidence of a robust negotiation with the VOA to minimise those costs.

It is therefore critical that the CAA fully reviews not just the outcome of HAL's negotiations, but in line with other airport examples, the extent to which HAL has put early and timely mitigations in place.

#### CAA Workplan and clarity of approach on WACC

Finally, we are cognisant that, alongside the work in CE, the CAA are undertaking a number of Heathrow related activities, both H8 and non-H8.

We firmly support the CAA's H8 priority to ensure that only efficient costs are passed on to the consumer. In line with our previous submissions to the H7 lessons learned and the H8 method

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<sup>1</sup> Email from the Airline Community to HAL, "Capital Prioritisation (H7 – H8) Escalation", dated 22<sup>nd</sup> May 2025

<sup>2</sup> Email from Airline Community to HAL "Heathrow Constructive Engagement Round 2 CE Lite Session: Commercial Property Investment", dated 14<sup>th</sup> May 2025

statement, we would very much welcome a clear workplan from the CAA on the constituent elements of the price control, particularly with regards to those activities where early engagement will be required ahead of Initial Proposals. Alongside the building blocks being addressed through CE, we would highlight the need for clarity on delivering the CAA's focus areas for the cost of capital (WACC) and the financial framework, as highlighted in the final H8 method statement. We note that, alongside Business Rates, those issues will be a key determinant to the level of charges for H8 and therefore clarity is needed on the CAA's approach to ensure that only financing that is efficient is allowed, that the level and growth of the Regulatory Asset Base (RAB) is sustainable and that insulating HAL from all eventualities is inconsistent with the risk of a regulated business.

We also note the need for early engagement on wider activities, for example around expansion and the review of the regulatory framework, including the extent these may have an impact on the H8 price control.

We thank you for your consideration on these matters and the ongoing openness and engagement.

Yours sincerely,

A handwritten signature in black ink, appearing to read "Gavin Molloy".

Gavin Molloy  
Chair – LACC  
London (Heathrow) Airline Consultative Committee

A handwritten signature in black ink, appearing to read "Nigel Wicking".

Nigel Wicking  
Chief Executive – AOC  
Heathrow AOC Limited

cc: Rob Toal, Programme Director, CAA

## Annex I: Referenced Emails to HAL

### **I.I: Email from the Airline Community to HAL re Commercial Property Investment Proposals**

**Simon Laver**

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**From:** Simon Laver  
**Sent:** 14 May 2025 16:13  
**To:**

**Cc:**

**Subject:** RE: Heathrow Constructive Engagement Round 2 'CE Lite' Session: Commercial Property investment - material

**Importance:** High

Mike, Richard and Heathrow team,

Further to Heathrow's proposed alternative approach to commercial property investments shared on 9<sup>th</sup> May 2025, and in advance of the meeting on Thursday 15<sup>th</sup> May; having discussed more widely we thought it would be useful to set out the airline community position.

As an airline community we have been carefully reviewing the proposal and have concluded that we are not supportive. We believe the existing framework is, and has demonstrated itself to be, capable of incorporating commercial property investments as part of an overall balanced capital portfolio, provided these present a positive business case for the consumer.

Bearing in mind our positions on the regulatory "till" clearly expressed during Rounds 1 and 2 of CE, whilst we recognise efforts by Heathrow to respond to the comments shared, ultimately we believe the proposal compromises single till regulation. We believe it will add a high degree of complexity and legal/regulatory uncertainty with no clear or obvious improvement in consumer benefit. In fact, we consider the approach would unavoidably create perverse incentives in the context of significant physical constraints at Heathrow and our ongoing discussions as to how to best deliver optimisation and resilience. It could equally have wider and unintended financial consequences (e.g. in relation interest rates on debt); and ignores alternative delivery / commercial models – for example the Gridserve / Gatwick partnership or T2 Hotel.

We also note that, at this stage and despite our continued feedback in H8 CE, we are yet to have a fully informed discussion on the overall capital prioritisation and constraints in H8. Furthermore, we would also highlight that there are wider considerations in relation to the ongoing considerations about the regulatory model for creating capacity and expansion, as highlighted by the CAA in their recent letter to Heathrow and airlines.

Given all of the above and on full reflection please note this is not an area we are therefore open to progressing.

We are still agreeable to running the meeting if you believe there is merit but would reiterate the above positioning. Alternatively, we could look to repurpose the time to address some of the other outstanding matters, particularly on Capital Choices, or otherwise return time to peoples' diaries.

Kind regards  
Simon.

Simon Laver  
London (Heathrow) Airline Consultative Committee (LACC)  
&  
Assistant Director, Airport Infrastructure



## I.II: Email from the Airline Community to HAL re Capital Prioritisation

**Simon Laver**

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**From:** Simon Laver  
**Sent:** 22 May 2025 11:48  
**To:** [REDACTED]  
**Cc:** [REDACTED]  
**Subject:** Capital Prioritisation (H/- H8) Escalation

Dear Rhinannon et al,

Following on from recent discussions in which the airline community have been raising our concerns and frustration with the capital prioritisation activity, we wanted to formally follow up on the discussions held at the Future Portfolio Group (FPG) and Capital Portfolio Board (CPB) on 15<sup>th</sup> May, which sought to bring this together.

Whilst we welcome Heathrow's proposal to now set up a specific CE Lite session, leaving until mid-June for a further session is simply too late.

As noted at the Constructive Engagement (CE) sessions in Round 2, whilst the presentations were helpful in understanding and encouraging discussion where investment may be required, it was not of a level of detail to be able to validate the proposed initiatives nor consider how they might be prioritised against each other. Furthermore, it raised significant concerns on the potential size of the overall capital envelope, even before the potential capacity / terminal occupancy costs that were missing were overlaid. As such we have been keen, and sought to work with HAL, on better understanding and tackling this in advance of the Business Plan, as raised during CE.

A significant portion of expenditure (£4.5bn) was presented as coming from rollover from H7. As such and given the direct relationship with the ongoing H7 approvals, we sought to focus on better understanding – and addressing where necessary – the rollover now, to allow a greater degree of headroom for those potential H8 potential 'choices'.

Having submitted our feedback to HAL on the pre-G3 H7 projects (which will have a material bearing on the level of rollover) on 25<sup>th</sup> April, it has therefore been deeply frustrating that the proposed meeting to discuss on 9<sup>th</sup> May was subsequently cancelled and at FPG only proposed to be picked up in the CE session in June.

As flagged, it is difficult to see how this timeline will: (i) allow due consideration in time / as part of HAL's Business Plan; or (ii) allow us to have confidence in committing to projects within H7 that are contributing to the non-prioritised H8 rollover bow-wave.

One of the benefits HAL proclaimed for moving to a "programmatic approach" in H7 was that it would allow greater foresight of projects and initiatives over the longer period and avoid artificial capital peaks and troughs at the start and end of regulatory periods, particularly on those areas where ongoing expenditure would continue to be required, e.g Asset Management and Compliance. At the time of establishing the H7 programmes at P2 (programme definition), whilst airlines advised they could / would only be able to approve those projects within H7, Heathrow set out a plan for H7 and H8. By its nature therefore, unlike other control periods, whilst the delivery of the large scale, inter-related projects, notably T2 Baggage and Security Programmes always would be the case, applying this approach to those 'portfolio' programmes (projects that have been grouped through broadly common benefits but are otherwise independent of each other) means we are seeing an unprecedented level of rollover on which we have not engaged on but is seemingly being 'banked' within the H8 plan. The programmatic approach should enable prioritisation to be a continuous process throughout the regulatory period. In fact, a prioritisation of the remainder of the H7 portfolio against the H8 choices may result in suggested H8 capital expenditure being brought forward to replace lower priority H7 spend.

Since the summer of last year, we have been calling for a fuller review and prioritisation of the portfolio, particularly as we get closer to the end of H7 and this issue becomes more acute. When this has been presented through the Future Portfolio Group, primarily it has focussed on how H7 was performing as a whole to the settlement. That is, we have not prioritised the remaining portfolio across programmes or at a project / tranche level. Also, what we have not covered – nor have we given agreement to – is what this means for H8. It is also worth noting that in the CE slides on 26 Mar 2025, HAL presented that the £4.5bn pre-G3 rollover could be considered as a 'Choice'.

As mentioned in the meetings on 15<sup>th</sup> May, this is not about seeking to reduce expenditure in H7 but to ensure that the 'rollover' that has already been created is understood in the context of what potential new initiatives have arisen – and presented – on which we have also not sufficiently tested. This is in addition to ensuring that the H8 portfolio has headroom to undertake the potential significant investments in creating capacity and demand rebalancing (occupancy) to which we have not yet had a consolidated figure.

Whilst there may likely be some differences of views on the proposed capital plan in the H8 Business Plan that we will need to work through as part of subsequent rounds of CE (including ensuring it is affordable), as mentioned we are keen to work with you on this in a much more expedient manner to: (i) ensure we can continue to confidently approve those upcoming H7 business cases that will have a bearing on the H8 rollover; and (ii) seek to find consensus on as much as we realistically can in advance of the Business Plan.

We remain available to discuss further how and when this might be achieved.

Given this issue of rollover, we will also be keen to review as part of Round 3 Constructive Engagement the appropriateness of using a programmatic approach as it has been applied within H7 for the purposes of our engagement and developing the capital plan in future.

With regards to the H8 Choices presented in Round 2 of CE, we have also not yet had the opportunity for a discussion with Heathrow on the relative priorities of the different projects being proposed. The high-level thematic prioritisation suggested was too simplistic to be meaningful. We are therefore unclear, on what basis HAL are incorporating airline feedback into the selection of the possible capital projects to determine their Business Plan H8 portfolio.

Kind regards  
Simon

**Simon Laver**  
**H8 Co-Chair (Airlines) &**  
**London (Heathrow) Airline Consultative Committee (LACC)**

  
[lavers@iata.org](mailto:lavers@iata.org)

International Air Transport Association  
The Metro Building, 1 Butterwick,  
Hammersmith, W6 8DL, London, UK  
[iata.org](http://iata.org)