

Chief Executive's Office

Caroline Low

Director, Airport Capacity Directorate
Department for Transport
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28 September 2018

Dear Caroline

INTERIM UPDATE: ASSESSMENT OF AIRPORT-AIRLINE ENGAGEMENT ON CAPACITY EXPANSION AT HEATHROW AIRPORT (MAY–SEPTEMBER 2018)

In May 2018, the Secretary of State recommissioned the CAA to advise the Department for Transport (DfT) on how well Heathrow Airport Limited (HAL) is engaging with, and responding to the airline community on its plans for capacity expansion at Heathrow airport and whether this engagement is appropriately reflecting consumers' interests (the 'Enhanced Engagement' process). I set out below a summary of our assessment and advice to the Secretary of State on HAL-airline engagement between May 2018 and September 2018. Attached to this letter is a paper setting out our assessment in more detail.

This latest period of HAL-airline engagement was marked by the significant milestone of the Airports National Policy Statement (NPS) being designated in June 2018. We welcome the fact that both HAL and the airlines supported the preparation for the successful vote in Parliament by uniting behind the strategic and economic case for capacity expansion at Heathrow Airport.

We recognise that capacity expansion is an unprecedented and very complex programme and that HAL has been engaging extensively with the airline community on its plans in good faith. We are pleased that HAL and the airline community have agreed the contents of a new protocol to govern the engagement process. HAL has also made steady progress in responding to our previous recommendations aimed at making sure consumers' interests are integral to its expansion and business planning processes.

Nonetheless, there are two important areas where we have concerns. Our concerns relate to HAL's need to provide high quality information about the costs of the scheme associated with the current stage of the masterplanning process and the need for HAL to provide assurance that its revised timetable is realistic and will both credibly ensure timely delivery and continue to embody effective engagement with the airline community. HAL must address these two concerns decisively and urgently.

HAL's provision of high quality information about costs

The airline community has expressed concerns to us over the last 18 months about the lack of high quality and comprehensive information from HAL on costs and efficiency. These concerns have not yet been adequately addressed despite repeated requests from the airline community and the CAA (most recently in our April 2018 Section 16 report).

We fully appreciate that HAL is still developing its preferred masterplan so some uncertainty is inevitable given the maturity of the design. We also acknowledge that HAL has committed to

enhance its cost estimates as it approaches key programme gateways over the next year. Nevertheless, HAL must urgently and demonstrably rise to our challenge of improving the flow of high quality information on costs and efficiency if it is to secure airline confidence in its ability to deliver on the Secretary of State's ambition for future airport charges.

Specifically, HAL's M3c¹ and M4² programme gateways will provide critical tests of its credibility in providing high quality information on costs and efficiency. In addition to securing airline confidence, a step change in HAL's provision of high quality cost information is required to enable the CAA to update its April 2018 assessment of whether HAL's scheme is capable of delivering the Secretary of State's 2016 ambition to keep airport charges close to current levels (in real terms) while being commercially financeable.

Unless there is a significant improvement in this area we will consider whether there are further steps we should take to support the proper discharge of our statutory duties. These include the option of issuing a formal information request to HAL under section 50 Civil Aviation Act 2012 and/or the development of additional licence obligations to require the provision of further detailed information. We recognise such action is unlikely to fully substitute for HAL actively owning and leading on the provision of high quality cost information, but we will consider further regulatory action if HAL fails to deliver appropriate information in support of its M3c³ and M4⁴ programme gateways.

In addition to the importance placed on these matters by the Secretary of State, the CAA and the airline community, we also note the broader context provided by:

- the Transport Select Committee's commentary⁵ earlier this year that it "*would like to see evidence to demonstrate that the Northwest Runway scheme is both affordable and deliverable and that steps are being taken to address the valid concerns we heard in evidence about the high cost of the scheme and the significant risk that costs will rise.*" and
- the inclusion in the Airports NPS⁶ of the applicant's role in assisting the CAA in discharging its role as a statutory consultee: "*the applicant is expected to provide the CAA with the information it needs to enable it to assist the Examining Authority in considering whether any impediments to the applicant's development proposals, insofar as they relate to the CAA's economic regulatory and other functions, are capable of being properly managed.*"

Confidence in HAL's new timetable

HAL has recently announced some changes to its overall expansion schedule and now expects to launch its Statutory Consultation in June 2019 rather than in the first quarter of 2019. It is our view that HAL must now demonstrate to stakeholders that its new timetable is realistic, achievable and allows sufficient time for high quality engagement while ensuring timely delivery. It must clearly articulate the contingency within the timetable and the remaining key risks and mitigations.

An immediate priority for HAL is to review and provide assurance to the airline community that the M3c programme gateway (scheduled for 25 October 2018) is realistic and that it will provide appropriate information on costs and efficiency to allow for proper engagement. HAL must also provide assurance to the airline community that the critical M4 gateway (preferred masterplan)

¹ To set the strategic direction to form a preferred masterplan based on the findings from the evaluation process.

² To approve the preferred masterplan.

³ To set the strategic direction to form a preferred masterplan based on the findings from the evaluation process.

⁴ To approve the preferred masterplan.

⁵ See [link](#).

⁶ See paragraph 4.40 in the [Airports NPS](#).

is achievable and will meet their expectations. At the time of drafting this update, we understand some information on the revised schedule has been shared with the airline community. Looking forwards, we expect HAL to provide a better definition of these gateways, with a clear plan on how to achieve them.

Other issues

i) Enhanced Engagement and Governance Protocol

We are pleased that HAL and the airline community agreed a new governance protocol, but are disappointed that it could not be achieved by the 20 July deadline we had set and took until the 6 September. This document is key in underpinning how HAL and the airline community should engage throughout the period until HAL submits its DCO application and beyond. Notwithstanding the time it took to agree, we do acknowledge the efforts made by HAL and the airline community to agree this document, which now meets the expectations we set out in our April 2018 Section 16 report. We especially welcome the focus the new protocol places on consumer interests.

ii) HAL reflecting consumer interests in its expansion and business plan processes

We welcome the steady progress HAL has made on implementing its consumer research and engagement strategy in response to our previous recommendations. Looking forward, we expect HAL to continue to deliver on the strategy, engage closely and constructively with stakeholders, including the Consumer Challenge Board (CCB) and the airline community. We have asked our technical advisers, Arcadis, to review the steps HAL is taking to ensure consumers' interests are reflected in its masterplan and we expect HAL to be responsive to the review's findings.

iii) Alternative commercial and delivery mechanisms.

HAL introduced the Innovation Partners process to invite businesses/potential partners to enter an expression of interest to develop alternative design, engineering or construction proposals to deliver capacity expansion at Heathrow airport. The process appears to have merits, and we look to HAL to demonstrate the benefits that will flow to the airline community and consumers.

Nonetheless, the Arora Group has said that the conditions of HAL's Innovation Partners process do not appear consistent with its ambitions and that it is considering submitting its own DCO application. The airline community has been keen to test the credibility and feasibility of the Arora Group's plans. The CAA sought to facilitate this by asking Arcadis to conduct a 'compare and contrast' review of the HAL and Arora Group plans. While there have been extensive discussions with the Arora Group, it did not prove practicable to agree the scope of this review, and so only very limited progress has been made on understanding the detail behind the Arora Group's plans. Nonetheless, we now appear to be close to agreeing a revised scope for the Arcadis review that we hope will enable the airlines to start to test the credibility and feasibility of the Arora Group's plans. We hope that the Arora Group will work with Arcadis in such a way as to facilitate the timely completion of this study.

Next steps

We will report to you again in early 2019 on how HAL-airline engagement has progressed towards the critical M4 preferred masterplan milestone. I am sharing this letter with airport and airline stakeholders and in due course will place this letter and attached Section 16 advice on our website.

Finally, I would like to place on record my thanks to your team for their continued support and the way they have worked with us in an open and collaborative way.

Yours sincerely

A handwritten signature in black ink, appearing to be 'RM' followed by a long horizontal stroke that ends in a small loop.

Richard Moriarty
CHIEF EXECUTIVE