

RESPONSE TO HEATHROW CAPACITY EXPANSION - CONSULTATION ON REGULATORY POLICY ON EARLY COSTS

This is the response of Heathrow West Limited (**HWL**), which is part of the Arora Group, to the consultation issued by the CAA as CAP 3149.

HWL welcomes and strongly supports the Civil Aviation Authority's ("CAA") recognition of the potential benefits of competition in the delivery of capacity expansion at Heathrow Airport. There can be little doubt that competition can ultimately benefit consumers, by encouraging more efficient expenditure by promoters and more innovative capacity expansion proposals.

Therefore, HWL strongly supports the CAA's initial view that there are likely to be advantages to consumers in supporting the recovery of initial early costs of other promoters. The ability to recover efficiently incurred early costs is fundamental to ensuring that alternative promoters can participate on a level playing field. It is also key to ensuring that credible promoters are incentivised to put forward efficiently costed expansion options.

Beyond these overarching points, there are several other issues in the CAA's consultation which HWL wishes to address in the following sections (which broadly follow the structure of the CAA's consultation).

1. KEY ISSUES FOR EARLY COSTS

Regulatory mechanisms and incentives for early costs

- 1.1 CAP 3149 sets out several features of the previous cost recovery policy used to incentivise efficient early expenditure.¹ In considering the right arrangements to allow the recovery of early expansion costs, HWL urges the CAA to design a regulatory framework which genuinely protects competition and does not inadvertently undermine the possibility for a competitive dynamic in the capacity expansion process. This is especially since competition itself is likely to be a powerful incentive to ensure early expenditure is efficient.
- 1.2 There are two specific points flowing from this.
- 1.3 First, the stark discrepancy in cost estimates between HAL and HWL suggests that HAL is operating on the basis that it can proceed at pace incurring considerable expenditure regardless of stakeholder (in particular airline) buy-in. By contrast, alternative promoters do not have the luxury of knowing that their costs will be recoverable under the established practice of allowing a licensee to recover efficiently incurred costs under a fair bet or other principle. It is incumbent on the CAA to ensure that HAL is not able to leverage a competitive advantage from its reckless approach to expenditure and existing regulatory practice.
- 1.4 Moreover, HAL's comparatively high costs (particularly when accounting for the significant costs which the CAA allowed HAL to recover in relation to its previous expansion proposal) are illustrative of the risks inherent in considering only a monopoly provider's approach to expenditure and planning at Heathrow Airport. They also raise valid questions about HAL's ability to plan efficiently under the current regulatory framework. HWL urges the CAA to develop a framework which enables it properly to control expansion costs for the benefit of airlines, consumers and ultimately the wider UK economy.

- 1.5 Second, allowing alternative promoters to recover their efficiently incurred early costs is fundamental to enabling the emergence of competition and ensuring a level playing field between promoters. HWL strongly endorses the CAA's initial view that competition at this stage is likely to be beneficial to consumers and allowing the recovery of alternative providers' costs would enable consumers to harness the advantages of a process of rivalry in the development of expansion proposals.
- 1.6 More generally as regards the other incentive mechanisms considered by the CAA, HWL has no objections to being subject to independent scrutiny of costs and/or enhanced reporting requirements should the CAA consider this appropriate for alternative promoters.

The recovery of costs for alternative promoters

- 1.7 Although proposing to allow other promoters to recover efficient costs, the CAA emphasises the need for promoters to have 'credible and appropriately mature proposals' to qualify for this mechanism. HWL appreciates the need for the CAA to balance competing interests in line with its statutory duties. That said, the threshold for what constitutes a 'credible and appropriately mature proposal' must be set at a level that reflects the current, early stage of the process, with the need to promote competition in mind. The CAA recognises that proposals are currently at an early stage.² It also notes that it previously recognised that HWL's proposal had met the benchmark of 'reasonably mature and credible'.³ However, the CAA must ensure that it sets the bar at an appropriate level that does not risk prematurely excluding alternative promoters before they have a fair opportunity to develop their proposals, and accordingly undermine the possibility of competition for capacity expansion.
- 1.8 Separately, HWL supports, in principle, the CAA's proposal to modify HAL's licence to create a fund for the recovery of early costs by both HAL and other credible promoters. However, to protect alternative promoters, the CAA will need to ensure appropriate safeguards are put in place. Depending on the stage at which such a fund is established, the CAA may need to ensure that other promoters are protected against the risks of HAL being incentivised to favour its own scheme. Any fund will need to be subject to robust governance and oversight by the CAA with clear obligations on HAL.

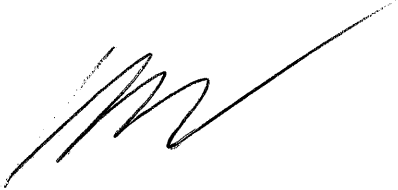
2. OPTIONS FOR RECOVERY OF EARLY EXPANSION COSTS

- 2.1 On the assumption that other promoters' proposals are fairly assessed to be credible and appropriately mature, HWL supports the initial view of the CAA that a focus on the recovery of early expansion costs for HAL and alternative promoters is the most appropriate proposal. As set out above, this is the only approach which ensures a level playing field and encourages efficient spend.
- 2.2 HWL notes the CAA's intention to consult further on the treatment of medium-term costs and to ensure that any approach addresses the potential for significant and unnecessary duplication of planning costs to be recovered through airport charges. We welcome this further consultation and look forward to engaging further with the CAA and other stakeholders.
- 2.3 The CAA refers to possible arrangements to ensure DCO applications are coordinated and complementary. HWL fully supports and concurs with the premise that duplicative and/or unnecessary costs should be minimised for the benefit of stakeholders. HWL has campaigned for measures to be put in place to avoid duplication through the DCO application process, in particular through the sharing of survey data, both from a cost and level playing field perspective.

This is within the CAA and DfT's gift to enable. Without support from the CAA (and DfT) in this regard, HAL will have no incentive to assist third party promoters to develop their proposals efficiently and to limit such duplication, particularly in a competitive situation – as HWL experienced in its pre-pandemic proposals. It will therefore be key for the CAA to monitor any proposed arrangements carefully and ensure the benefits of competition can be fully harnessed.

HWL looks forward to engaging with the CAA on these matters, and is ready to discuss any of the above points with the CAA and/or other stakeholders. We are happy for this response to be published.

Yours sincerely,



Carlton Brown

Chief Executive Officer

Heathrow West Limited

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