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British Airways response to CAP3232
H8 Initial Proposals

Dear Rob

This document sets out British Airways' response to the Civil Aviation Authority's (CAA) Initial Proposals for the H8 price control for Heathrow Airport Limited (HAL) for 2027–2031.

While BA supports several elements of the CAA's approach, the overall package remains insufficiently challenging and materially imbalanced in favour of HAL, does not represent efficient costs in line with the CAA's statutory duties on consumer protection and efficiency, and will have significant implications for consumers, connectivity and the competitiveness of the UK aviation sector.

1. **Level of charge and impact on connectivity:** The proposed level of charges is materially understated and has been assessed in isolation from the cumulative impact of the CAA's concurrent regulatory decisions on Heathrow. On steady-state conditions post-pandemic, the proposed charge results in a 7% increase in real terms and, when combined with expansion-related costs and other policy pressures, will impact affordability and undermine Heathrow's role as a global hub. There is limited evidence that the CAA has assessed the impact on affordability and consumer choice, despite clear evidence that higher charges weaken connectivity and the CAA's own commitment to use affordability as an evaluation criterion for the regulatory models on expansion.

2. **Capital envelope and governance**: We support the CAA's proposed capital envelope of £5.8 billion as a credible and deliverable midpoint, and the methodology employed by the CAA to derive it. However, the proposed governance framework does not sufficiently address longstanding structural weaknesses. Without strengthened airline involvement, full transparency across the portfolio, independent assurance and robust challenge mechanisms, there is a material risk that the programme will be delivered inefficiently to the detriment of consumers. We remind the CAA that our calls for

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reform preceded the revival of Heathrow expansion, and we encourage a holistic perspective rather than limiting reform efforts exclusively to expansion.

3. **Opex and commercial revenues methodology**: We support the CAA's methodology for assessing opex and commercial revenues, including the bottom-up assessment, which represents a clear improvement on previous price controls. However, persistent deficiencies in HAL's information quality have constrained scrutiny by both the airlines and the CAA's consultants, and the allowances proposed are inherently cautious despite evidence of a more robust challenge. We propose further evidence-based adjustments beyond the CAA's efficiency targets to ensure truly efficient costs (additional challenges of £309 million and £412 million in 2024 CPIH prices for opex and commercial revenues respectively).

4. **Cost of capital and overall regulatory balance**: We strongly contest the CAA's proposed WACC, which is materially overstated and would result in at least £1.2 billion (more than £3 per passenger) in unjustified additional costs for the consumer, based on independent advice from CEPA and two leading academic experts provided to the airline community. This is against the CAA's statutory duties to protect the consumer and ensure efficient costs. The CAA's analysis is internally inconsistent, is premised on factual errors and non-transparent information, diverges from its own precedent and fails to reflect airport-specific evidence. It further creates regulatory unpredictability by relying on approaches, data and assumptions that are not applied coherently and do not reflect HAL's actual risk profile. This is inconsistent with HAL's low-risk profile as a capacity-constrained monopoly in single till and risks breaching the CAA's duty to protect consumers by allowing higher charges and inefficient costs. The CAA has rejected more robust, better-evidenced approaches without sufficient justification or credible alternatives.

   In addition, the proposal to allow an actual cost of debt has lacked transparency, creates perverse financing incentives, risks embedding expectations of cost pass-through and could lead to higher costs for consumers for decades including for expansion. Our independent advice, including the independent academic experts, propose materially better alternatives and a consistent evidence-based approach to calculate the WACC more accurately and ensure efficient costs. Our independent advice recommends that a pre-tax CPIH-real WACC of 4.68% (3.74% vanilla), in line with the airline Alternative Business Plan from October 2025, continues to be justified.

   The overall regulatory package is significantly imbalanced, providing several layers of protection to HAL against multiple sources of risk and resulting in overcompensation at the consumer's expense. We propose remedies to address this imbalance.

5. **Service quality incentives (MTIs):** The current calibration of MTIs is insufficient to address persistent underperformance. For instance, while we welcome the introduction of a financial rebate on the critical area of departing baggage, the proposed incentive will not capture the consumer detriment arising from major and recurring system outages at Heathrow over the past years. We further propose improvements to security queue measurement, the Terminal 5 Track Transit system and Pre-Conditioned Air. We also remain concerned that the use of service quality bonuses creates perverse incentives and should be removed.

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6. **Traffic forecast:** While we support the use of an independent forecast, the CAA's approach remains conservative and risks continuing the pattern of systematic under-forecasting from previous regulatory periods. The application of the shock factor has exacerbated downward bias, resulting in higher charges for consumers. We support the removal of the shock factor or, in the alternative, its recalculation. Our proposal, based on independent advice provided to the airline community, is for a forecast of 447.6 million passengers over H8.

7. **Process integrity**: We have repeatedly expressed concerns regarding HAL's lack of transparency in the Constructive Engagement process and the quality of its Business Plan, which the CAA has rightly assessed as "low quality". Strong safeguards are required to prevent the introduction of late information outside the structured process. These deficiencies clearly justify a Business Plan Incentive penalty and preclude any basis for a bonus.

8. **Traffic Risk Sharing mechanism**: The TRS ought to be recalibrated to prevent HAL from passing onto consumers the cost of its own failure to deliver critical capacity-enhancing projects, [**REDACTED**].

Our proposed package, based on the above adjustments, **results in an average charge of £24.48 (2024 CPIH) over H8**, compared to the CAA's proposal of £28.80 – representing a reduction of 15%. Based on a comparison against the average charge of £27 over 2024-2026, where traffic reflects steady-state conditions after the pandemic, our proposal represents a 9% decrease (all prices 2024 CPIH).

We consider this to represent a package grounded in efficient costs, with a balanced risk-return profile, an affordable and deliverable capital programme, and improved protections for consumers, while supporting long-term connectivity and competitiveness.

We use **bold** text in our response to indicate our areas of emphasis and ease of reading. For the avoidance of doubt, unless expressly stated otherwise all our comments should be given equal weight whether or not they are in bold.

We welcome further engagement with the CAA as the process moves towards Final Proposals and remain committed to working constructively to ensure the H8 settlement delivers for consumers and the wider UK economy.

Yours sincerely,

Michael Petrides

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1. Summary of our response

1.1. British Airways (BA) welcomes the CAA's Initial Proposals for the H8 price control for Heathrow Airport Limited (HAL) for 2027-2031 and the continued focus on strengthening Heathrow's regulatory framework. BA has been extensively engaged throughout the H8 Constructive Engagement (CE) process that began in October 2024 and the development of HAL's Business Plan, including through the airline community's Alternative Airline Business Plan submitted to the CAA in October 2025.

1.2. Heathrow represents a critical piece of national infrastructure and an effective monopoly airport. It therefore requires robust economic regulation to ensure that charges are efficient, service quality meets consumer expectations and investment deliver value for money. This is particularly important given Heathrow's position as a global hub, supporting UK connectivity, trade and economic growth.

1.3. However, consumers at Heathrow continue to experience poor value for money. Passengers face the highest airport charges at a major airport globally, while service quality outcomes remain inconsistent and, in key areas, below expectations. At the same time, airlines face increasing cost pressures, which risk undermining connectivity and the competitiveness of the UK aviation market at a time of global uncertainty.

1.4. The H8 price control therefore represents a critical opportunity for the CAA to reset the balance of the regulatory framework. In BA's view, this requires a stronger focus on cost efficiency, improved incentives for service delivery, more effective governance of capital investment, as well as an allowed return and balanced financial framework that reflects the limited risk faced by HAL as a regulated capacity constrained airport monopoly without overcompensating it.

1.5. While BA supports elements of the CAA's approach, including the analytical approaches for assessing opex, capex and traffic forecasting which deliver an improvement to the CAA's assessment of the H7 price control, the overall package remains insufficiently challenging.

1.6. In particular, the CAA's proposals on HAL's Weighted Average Cost of Capital (WACC), HAL's allowed return, would over-reward Heathrow by at least £1.2 billion (more than £3 per passenger) above its true level of risk over the regulatory period. There is a material risk that the settlement will allow excessive costs to be recovered and will overcompensate HAL, ultimately to the detriment of consumers and against the CAA's duties to protect consumers and ensure efficient costs.

1.7. BA's position on the cost of capital has been informed by three independent reports for the airline community from CEPA and two leading academics on the cost of capital: Professor Robin Mason and Professor Donald Robertson. These three reports indicate that the CAA has, among other things, inconsistently applied the principles of stability and predictability, relied on data that are not representative and non-transparent and applied its chosen approaches inconsistently. It further made factual errors, failed to take into account airport-specific evidence and relied

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on approaches that do not accurately reflect HAL's risk profile. All three reports propose materially better and evidence-based alternatives to improve the CAA's estimation of HAL's WACC in a targeted, predictable and disciplined manner, to ensure efficient costs and avoid the consumer paying over the odds. We urge the CAA to take those recommendations into account in the setting of the WACC to avoid higher charges and inefficient costs contrary to its statutory duties.

1.8. We challenge the CAA's proposal to allow HAL's actual cost of debt despite acknowledging that this weakens financing incentives and risks increasing costs for consumers. This is all the more important given the longer-term perverse incentives by embedding expectations that future debt costs will be passed through, particularly in the context of potential expansion.

1.9. In fact, the overall regulatory package is significantly imbalanced in favour of HAL. We strongly consider that the compensation provided to Heathrow, both through the WACC and the financial framework, to be higher than the level of risk it faces. This in turn results into consumer harm through higher charges and inefficient costs. We discuss HAL's overcompensation in our response on the CAA's proposals on the WACC and the financial framework. We propose appropriate remedies for the WACC estimation to reflect HAL's multiple risk protections, aligned with regulatory precedent from other airports, such as the choice of the lower point estimate in the WACC range.

The CAA's charges proposal and the impact on connectivity

1.10. The CAA's assessment underestimates the impact of proposed charges on Heathrow's role as a hub and on UK connectivity. While the headline increase may appear moderate, it is understated by comparisons against H7 that rely on pandemic-distorted averages. On steady-state conditions post-pandemic, the increase is materially higher, at 7% in real terms, and must be assessed in the context of cumulative cost pressures, including expansion-related costs, the SAF transition and Air Passenger Duty.

1.11. More fundamentally, the H8 assessment appears to have been conducted in isolation from parallel CAA workstreams that will directly affect the overall level of charges faced by passengers at Heathrow. HAL's Business Plan already implied a real charge increase of up to 47% by 2031, yet there is no evidence that the CAA has undertaken a top-down assessment of the combined impact of H8, early expansion cost recovery and the wider regulatory model review. Taken together, these will materially increase the cost of operating at Heathrow, impact affordability and choice, and undermine the competitiveness of the UK aviation market at the expense of the consumer. Indeed, the CAA has acknowledged the risk that modernisation and expansion at Heathrow could more than double charges in real terms.

1.12. The CAA's stated intention to consider the direct impact of charges, and to include affordability as an explicit evaluation criterion for the future regulatory model for Heathrow expansion, makes its decision not to do so for H8 – despite H8 establishing the cost baseline for expansion – particularly striking.

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1.13. There is clear evidence that higher charges lead to reduced connectivity, particularly through the loss of marginal and less profitable routes, creating a negative impact for hub strength. Heathrow remains the most expensive hub airport globally, and higher charges further increase the risk of worsening its competitive position. Despite prior engagement, the CAA has not assessed the impact of its proposals on consumer choice.

1.14. Without a more explicit assessment of the cumulative impact of charges on connectivity and choice, there is a risk that the regulatory settlement will weaken Heathrow's hub role and ultimately harm consumers through reduced choice at a time of global uncertainty.

1.15. Against this backdrop, the CAA should ensure charges are based on truly efficient costs for HAL that do not result in overcompensation of the regulated monopoly at the expense of consumers, as the current Initial Proposals suggest.

H8 Constructive Engagement and HAL's Business Plan

1.16. BA has supported the CAA's H8 objective of a structured, transparent Constructive Engagement process under a single Business Plan framework. However, persistent deficiencies in HAL's transparency, information quality and engagement have materially constrained effective scrutiny throughout the process. These shortcomings, repeatedly evidenced by airlines and recognised by the CAA, have resulted in a Business Plan assessed as "low quality".

1.17. The absence of a clear "golden thread" linking consumer research, investment proposals and outcomes has limited meaningful prioritisation and undermined the effectiveness of Constructive Engagement. Material information asymmetries and incomplete data further constrained challenge and forced reliance on assumptions.

1.18. We are therefore concerned by the risk that HAL may seek to introduce substantive new information after the conclusion of Constructive Engagement. Acceptance of such late submissions would undermine the integrity of the process, bypass structured scrutiny and create perverse incentives, including regulatory gaming. A very high bar must apply to any late submissions, limited to narrow clarifications with clear consumer benefit and subject to meaningful airline scrutiny.

Delivering for customers: consumer engagement and service level incentives

1.19. BA broadly supports the CAA's direction on customer outcomes. We acknowledge the CAA's intention to continue with the structure of the Outcome Based Regulation (OBR) framework premised on specific Measures, Targets and Incentives (MTIs) and recommend specific improvements to those MTIs. However, we note the inherent limits of the service quality regime in a single-operator setting in replicating the discipline of customer choice, particularly in the absence of appropriate calibration in the measures and targets the regime is setting.

1.20. The current calibration of the MTIs is insufficient to address persistent underperformance and does not adequately reflect the benefits of proposed

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investments. Significant and ongoing system outages by HAL of departing baggage systems ought to be included as a key priority.

1.21. In particular, the continued use of service quality bonuses is inappropriate, creating perverse incentives whereby HAL is rewarded for delivering expected performance despite ongoing service issues. Evidence shows that HAL has earned more in bonuses than paid in rebates despite continued underperformance.

1.22. Specific proposed measures, notably departing baggage performance, remain inadequately calibrated. The proposed targets fail to capture the consumer harm of major system outages, which have been significant and recurring. Without stronger incentives, including backstops or tighter targets, such as on security queue measurement and the Terminal 5 Track Transit, the framework risks failing to drive meaningful improvement and reflect the benefits of investments paid for by consumers. We also continue to reject HAL's proposal for airline eligibility criteria which would encroach upon competitive services that are already incentivised commercially and would create unnecessary regulatory complexity.

Traffic forecast

1.23. BA supports the CAA's decision to commission an independent traffic forecast by Steer, recognising its central importance to the price control. However, key elements of the approach are likely to underestimate demand. The airline community has commissioned Skylark to review the CAA's independent forecast conducted by Steer.

1.24. Evidence demonstrates that previous CAA forecasts have consistently under-forecast traffic, generating windfall gains for HAL and higher charges for consumers. In contrast, airline forecasts have historically been precise. Skylark's analysis confirms that current assumptions remain conservative, particularly on seat factors and traffic evolution. While Skylark identifies a potential short-term impact on movements in 2026 linked to the current geopolitical tensions in the Middle East, it emphasises that any effect is likely transitory and highlights Heathrow's resilient demand and hub model, including strong transfer passenger growth in recent months.

1.25. More fundamentally, the application of the shock factor has failed to improve forecast accuracy and instead exacerbates under-forecasting, overlaps with the TRS mechanism and increases regulatory complexity. This results in higher charges. Skylark therefore considers that the shock factor has failed on its objective to deliver a more precise traffic forecast.

1.26. Without removal or recalibration of the shock factor and a more robust forecasting approach, the resulting traffic forecast will continue to be biased downwards, leading to systematic overcharging of consumers.

1.27. Our proposal for the traffic forecast, based on the independent advice of Skylark, is 447.6 million passengers over H8 against the CAA's base case estimate of 442.0 million passengers (438 million passengers shocked).

Operating expenditure

1.28. BA strongly supports the CAA's base-step-trend framework, including its bottom-up analysis supported by top-down benchmarking, and the rigorous application of need, additionality and efficiency tests in the rejection of most of HAL's proposed overlays. This represents a clear improvement on previous price controls and aligns with our feedback during Constructive Engagement and in the Airline Business Plan.

1.29. However, persistent deficiencies in HAL's transparency and information quality have constrained scrutiny, both by airlines and the CAA's consultants, and led to reliance on assumptions that understate inefficiency. In fact, the CAA has adopted an inherently cautious approach in several areas, or did not adopt efficiencies in certain areas, where its own evidence supports a more robust challenge.

1.30. This is particularly evident in key cost categories such as security, staff costs and major operating lines, where independent evidence demonstrates significant inefficiency. Despite Heathrow ranking near the bottom of the CAA's comparator benchmarks – 40th out of 43 airports in 2022 – the resulting efficiency challenge remains conservative. Similarly, the CAA has also not applied an efficiency target on other operating costs that cumulatively amount to more than £310 million.

1.31. Without a materially strengthened efficiency challenge, the removal of unsupported costs and strict controls on late submissions, the cumulative effect would be an opex allowance that is materially too generous and not reflective of efficient costs, to the detriment of consumers.

1.32. Our proposal for opex is £7,480 million, compared to the CAA's proposal of £7,790 (2024 CPIH).

Commercial revenues

1.33. BA strongly supports the CAA's base-step-trend framework for assessing commercial revenues. However, similar transparency and information deficiencies have constrained effective scrutiny and resulted in conservative efficiency targets.

1.34. There is clear evidence of underperformance relative to comparator airports across key revenue streams, including retail, catering and property. The CAA's assumptions do not fully reflect this gap, nor do they capture revenue upside or the interaction between different revenue streams such as surface access.

1.35. Certain modelling choices further suppress the baseline, including TDOC assumptions and treatment of other revenue streams. In addition, mechanisms such as Business Rates pass-through are not fully reflected in revenue forecasts.

1.36. Without a stronger efficiency challenge and more accurate baseline calibration, commercial revenue allowances will be understated, resulting in higher charges than necessary for the consumer and failing to capture HAL's true revenue potential.

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1.37. Our proposal for commercial revenues is £5,905 million, compared to the CAA's proposal of £5,493 (2024 CPIH).

Other regulated revenues (ORCs)

1.38. BA considers that the current ORC framework has materially deteriorated and now functions as a cost pass-through mechanism with limited incentives for efficiency or effective governance. Airlines lack visibility and influence over cost drivers, and the intended collaborative model has not been realised in practice. This has resulted in significant cost increases without adequate scrutiny, to the detriment of consumers.

1.39. While BA supports the CAA's decision not to expand ORCs to include further aeronautical costs as proposed by HAL, this does not go far enough. The continued inclusion of key aeronautical services, particularly baggage/HBS, within a low-powered incentive regime creates a risk of inefficient cost pass-through and perverse incentives.

1.40. Without structural reform, including a reduction in scope and reclassification of key services into aeronautical charges, the ORC framework will continue to undermine cost discipline and fail to protect consumers. The CAA's proposal to oblige HAL to communicate the drivers of any potential increase is simply insufficient.

1.41. Our proposal for ORCs is £614 million, compared to the CAA's proposal of £1,289 million (2024 CPIH). This includes the integration of baggage/HBS and the taxi feeder park out of ORCs into aeronautical charges.

Commercial revenue incentives

1.42. BA supports the CAA's rejection of proposals to move away from the single till framework, which remains the most effective and proportionate mechanism to protect consumers and promote efficient investment. However, we are concerned that the CAA has not definitively excluded alternative approaches to commercial property investment despite a clear absence of evidence to justify change, and we set out why maintaining a clear and unambiguous single till is essential to avoid consumer harm, regulatory complexity and regulatory uncertainty. We refer the CAA to the findings of the CEPA report commissioned by BA setting out the concerns over altering the single till boundary, submitted with the Airline Business Plan.

1.43. We also highlight material risks associated with HAL's incentives to increase charges on directly or indirectly consumer-facing services, including Terminal Drop-Off Charge and Fast Track. In both cases, HAL has demonstrated perverse incentives by increasing tariffs mid-way through the H7 period despite no apparent increase in costs, and without those additional revenues fully accruing to consumers.

1.44. We propose targeted safeguards to ensure that any upside revenues are fully returned to users and guarantee that the price control framework is not circumvented.

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Capital expenditure assessment

1.45. BA strongly supports the CAA's approach and methodology to setting the capex envelope at a mid-point of £5.8 billion (2024 CPIH), which is consistent with deliverability constraints and affordability. The methodology, including the needs assessment and prioritisation framework, represents a clear improvement and appropriately constrains investment.

1.46. We caution CAA not to extend the size of the capex envelope beyond £5.8 billion. This envelope represents a significant increase in invested capital over the H7 period and will significantly stretch HAL's ability to efficiently deliver investments. When considered alongside the potential demands of Heathrow expansion, there are clear concerns regarding HAL's ability to manage investment at this scale.

1.47. In addition, persistent deficiencies in HAL's Business Plan, including lack of a "golden thread" and insufficient business case detail, have constrained effective scrutiny and led to information asymmetries for airlines.

1.48. BA supports the CAA's decision not to mandate specific projects, but this requires robust governance and continuous airline involvement from project initial identification to delivery. Without this, there is a risk of inefficient spend, unjustified re-prioritisations and late-stage changes.

1.49. We further support the CAA's prioritisation of asset management and compliance and highlight the need that spending is focussed on clearly defined safety-critical, mandatory needs and that discretionary scope is subject to robust scrutiny and prioritisation.

1.50. There are also risks related to the delays of critical capacity projects and incentive misalignment. Delays to Terminal Occupancy risk constraining growth and creating perverse incentives under the Traffic Risk Sharing mechanism that must be addressed.

1.51. Without strict controls on late submissions, strengthened governance, rigorous accountability and robust deliverability and efficiency safeguards, the framework risks being undermined.

1.52. We retain the capital envelope at the CAA's proposed mid-point of £5.8 billion (2024 CPIH).

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Capital governance and incentives

1.53. BA considers that the current capital governance framework is not fit for purpose and that the CAA's proposed minor refinements do not sufficiently address its structural weaknesses. We remind the CAA that our advocacy for regulatory reform predates the renewed focus on Heathrow expansion and, accordingly, reforms should be applied comprehensively for H8 rather than being limited to expansion-related matters.

1.54. CAA cannot afford to miss the opportunity for meaningful H8 reform, and failure to act would represent a clear dereliction of its duty to consumers.

1.55. Key issues include late airline involvement, information asymmetry, weak delivery obligations, ineffective portfolio governance and prioritisation, as well as insufficient breadth and true independence of assurance processes. These weaknesses allow inefficient or unsupported projects to progress, limit effective challenge, and reduce transparency and accountability across the investment programme.

1.56. Without fundamental reform, there is a high risk that the significantly larger H8 capital programme will be delivered inefficiently, with higher costs ultimately borne by consumers.

1.57. BA therefore sets out proposed solutions for strengthened governance in H8, including earlier airline involvement, full portfolio transparency and prioritisation, genuinely independent assurance, a formal pause mechanism and escalation mechanisms to deal with disputes or major concerns at project lifecycle stage gates. These would ensure that investment decisions are effectively scrutinised and deliver value for consumers. Our objective is for the capital governance process to guarantee that capital investment is efficient, justified and aligned with the interests of users, ahead of potential bolder reforms for expansion such as the airlines' request for a Capital Investment Committee to oversee and approve major capital investment at Heathrow.

1.58. Similarly, the ex-ante Delivery Obligation framework should be reviewed once more projects have completed the process, and appropriately strengthened, to prevent regulatory gaming, increase accountability and ensure effectiveness.

Cost of capital

1.59. BA considers that the CAA's proposed WACC of 5.87% pre-tax CPIH-real is materially overstated by around 120 basis points and is not consistent with the level of risk faced by HAL. The CAA's proposal results in excessive charges and overcompensation of the regulated monopoly by at least £1.2 billion (yielding an additional £3 per passenger in unjustified returns to HAL). This is against the CAA's statutory duty to protect the consumer and ensure efficient costs.

1.60. Our evidence demonstrates that the CAA's approach to the beta estimation, the cost of debt and the gearing assumptions is internally inconsistent, relies on factual errors and non-transparent information and departs from CAA precedent with

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inconsistent or inadequate justification. It fails to take proper account of airport-specific evidence and relevant precedent from other airport regulators and disregards the views of the CAA's own advisers. The CAA introduces policy changes that will harm the consumer without a proper or consistent assessment. It further creates regulatory unpredictability by relying on approaches, data and assumptions that are not applied consistently and do not reflect HAL's actual risk profile.

1.61. The CAA has rejected more robust, better-evidenced approaches without sufficient justification or credible alternatives. The cumulative effect of the CAA's approach, combined with multiple layers of risk protection within the regulatory framework, results in a materially imbalanced settlement in favour of HAL, with several protections against multiple sources of risk, at the expense of the consumer.

1.62. BA's position on the cost of capital has been informed by three independent reports from CEPA and two leading academics on the cost of capital: Professor Robin Mason and Professor Donald Robertson. These three reports confirm that the CAA has inconsistently applied the principles of stability and predictability, relied on data that are not representative, applied its chosen approaches inconsistently, made factual errors, and relied on approaches that do not accurately reflect HAL's risk profile.

1.63. In particular, the academics find that the CAA used unstable, inconsistent and inefficient beta estimates that contain embedded volatility and that are not aligned with the regulatory horizon. This is combined with the CAA's failure to adjust for HAL's lower systematic risk as a capacity-constrained single-till hub relative to diversified and less constrained comparator airport groups. **All three reports propose materially better and evidence-based alternatives to improve the CAA's estimation of HAL's WACC in a targeted, predictable and disciplined manner**. CEPA's and Professor Mason's approaches yield the same result, demonstrating that the CAA is overestimating the beta by around 20%, inflating charges by £1.30. We urge the CAA to take those recommendations into account in the setting of the WACC to improve its methodology.

1.64. We also challenge the CAA's proposal to allow an actual cost of debt for HAL, as opposed to a notional one, despite its acknowledgment that this would weaken financing incentives and risk increasing costs for consumers. This policy choice by the CAA alone could increase costs by up to £2 per passenger. It could also risk longer-term ramifications ahead of expansion by embedding an expectation that future debt costs will be passed through to consumers.

1.65. Without adopting a more robust, evidence-based approach to WACC and addressing the interaction of risk protections across the financial framework, HAL would be overcompensated at the detriment of consumers.

1.66. Based on the independent advice by CEPA, Professor Robin Mason and Professor Donald Robertson we retain a pre-tax CPIH-real WACC of 4.68% (equivalent to 3.74% vanilla).

1.67. In fact, the overall regulatory package is significantly imbalanced in favour of HAL by protecting the regulated monopoly against multiple sources of risk. We strongly

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consider that the compensation provided to Heathrow, both through the WACC and the financial framework, to be higher than the level of risk it faces. There are several layers of risk protections, including exposure to traffic shocks, inflation protection, financing conditions, input cost pressure and uncertain investment needs, with risks allocated to users. We discuss HAL's overcompensation below in the chapters of our response on the WACC and the financial framework. An allowed return above truly efficient costs, coupled with an overly generous regulatory package, generate the perverse incentive on HAL to maximise the RAB regardless of consumer value.

1.68. In addition to the independent findings on the parameters of the WACC, we propose appropriate remedies through the choice of a lower point estimate in the WACC range to reflect the multiple layers of the additional risk protections awarded to HAL by the regulatory package. These remedies are in line with the recent precedent by prominent airport regulators, notably the French Transport Regulatory Authority.

Financial framework

1.69. BA considers that the CAA's proposed financial framework does not deliver a fair and balanced allocation of risk and reward and, when combined with the overstated WACC, results in a regulatory package that materially overcompensates HAL relative to the risks it faces. These include multiple protections from exposure to traffic shocks, inflation protection, financing conditions, input cost pressure and uncertain investment needs.

1.70. While BA supports elements of the framework, including the move towards partial fixed inflation indexation, we are concerned that the CAA has not undertaken a fundamental reassessment of the framework despite repeated evidence from H7 and its own lessons learned that this embeds multiple overlapping risk protections.

1.71. In particular, a lack of transparency and scrutiny in areas such as depreciation, the absence of a robust assessment of HAL's effective tax rate, and continued reliance on outdated or inconsistent assumptions weaken the credibility of the framework and limit effective stakeholder challenge.

1.72. At the same time, key risk protection mechanisms – such as the Traffic Risk Sharing mechanism – create perverse incentives and moral hazard by protecting HAL from traffic shortfalls arising from its own delivery failures while exposing consumers to downside risk in a capacity-constrained environment, resulting in a one-sided risk allocation.

1.73. These issues are compounded by insufficient safeguards against inflation windfalls, limited consideration of long-term financeability and affordability, and a failure to reflect the cumulative impact of multiple protections within the broader regulatory package.

1.74. Without a fundamental recalibration of the financial framework, including removal of overlapping protections or the choice of a lower point estimate in the WACC range, strengthened transparency and governance, and alignment with a true "fair bet" principle, the settlement risks enabling over-recovery of revenues and passing undue

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cost and risk onto consumers. The TRS ought to be equally reviewed to remove any perverse incentives on HAL to benefit from its delays to deliver key capacity investments for the consumer.

Our price cap proposal & price profiling

1.75. Based on the above recommendations, **we propose an average price cap of £24.48 over H8**, which is 15% lower than the CAA's proposed average of £28.80. It also represents a 14% reduction to the H7 average of £28.40 assumed by the CAA, and 9% against the average charge of £27.0 over 2024-2026 where traffic reflects steady-state conditions post-pandemic (all prices 2024 CPIH).

1.76. We consider the proposed 2027 holding cap to be overstated and recommend a lower level, noting further charge increases from the CAA's proposal to allow HAL to recover early expansion costs from users.

1.77. The CAA should also address risks from its design of the holding cap to avoid a repeat of the unintended consequences from the 2022-2023 holding caps it had set, including inflation-related windfalls for HAL.

1.78. We do not support the CAA's proposed front-loading of increases, as a smoother profile better enables our business planning and reflects our investment constraints.

Business Plan Incentive

1.79. We agree with the CAA's classification of HAL's H8 Business Plan as "low quality", reflecting the persistence of H7 shortcomings in transparency, engagement and evidencing. The CAA's assessment identifies widespread and fundamental deficiencies across core areas, including inadequate cost and financing evidence, lack of a "golden thread" linking proposals to demonstrable consumer benefits or priorities, insufficient optioneering, lack of efficient targets and incomplete and inconsistent financial and operational data.

1.80. These failures have materially constrained effective scrutiny, undermined the Constructive Engagement process, and resulted in a plan that is neither sufficiently evidenced nor appropriately ambitious, as reflected in the material downward adjustment in the CAA's Initial Proposals.

1.81. We consider that these deficiencies clearly justify a penalty under the Business Plan Incentive and require the CAA to apply a very high bar to any late information, limited to narrow clarifications subject to effective airline scrutiny. They also preclude any justification for a BPI bonus.

1.82. We also request the CAA to address the repeated airline concerns on transparency and engagement, which are aligned to its own findings, in its Final Proposals.

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2. The CAA's charges proposal and the impact on connectivity

The CAA's comparison of H8 against H7 **materially understates the scale of the proposed increase**, as H7 averages are distorted by pandemic-era traffic levels. On a steady-state comparison (2024–2026), **H8 charges imply a significantly higher increase of around 7%**, which the CAA should explicitly recognise in its Final Proposals. Higher charges will directly affect airline yields in a competitive market, with limited ability to pass through costs, particularly in a context of geopolitical uncertainty.

More broadly, **H8 charges cannot be considered in isolation, given the cumulative impact of expansion-related costs**, including early expansion allowances and significant anticipated expenditure during H8. This will lead to **consequences for affordability, connectivity, consumer choice, and ultimately undermine the strength of Heathrow as a hub**.

This **consumer harm has not been adequately assessed by the CAA and should be addressed explicitly**. Indeed, the CAA's stated intention to consider the direct impact of charges, and to **include affordability as an explicit evaluation criterion for the future regulatory model** for Heathrow expansion, makes its decision not to do so for H8 – despite H8 establishing the cost baseline for expansion – particularly striking.

Against this backdrop, the CAA should ensure **H8 charges are set on truly efficient costs** for HAL that **do not result in overcompensation** of the regulated monopoly at the expense of consumers, as the current Initial Proposals suggest.

Comparisons against H7 underestimate the effect of the H8 proposals

2.1. The CAA presents its Initial Proposals as representing a modest increase between H7 and H8. The CAA notes that its proposed average price cap for H8 of around £28.80 per passenger (2024 CPIH) is around 1.4% higher compared to the price cap average of H7 (£28.40).

2.2. This comparison is misleading and should be treated with caution. The H7 average incorporates years in which traffic remained materially below pre-pandemic levels, which has the effect of inflating the average price cap. For example, in 2022 and 2023 traffic was 24% and 10% below 2019 levels respectively. This depressed demand base increases the implied unit charge and does not provide a steady-state comparison with H8, where traffic has fully recovered post-pandemic. For instance, based on the "unprofiled" price caps in the CAA's Final Decision for H7[1], the cap for 2022 was 22% higher than the average price cap for the remaining years of the regulatory period (2023-2026).

2.3. A more appropriate comparison is to focus on the years in which traffic more closely reflects steady-state conditions (i.e. 2024–2026). On this basis, the H8 proposals imply a materially larger increase of around 7% (against an average of £27 in 2024 CPIH), rather than the 1.8% headline increase cited by the CAA. The CAA should

[1] CAA H7 Final decision, March 2023. We are using the unprofiled cap of required revenues over passengers, and not the holding caps or the annual Maximum Allowable Yield, to better pick up the effects of traffic on the revenue requirement per pax for that year. We note that the unprofiled price caps may differ slightly following the outcome of the CMA H7 remittals decision in 2024.

recognise the full extent of its proposed increase and reflect it appropriately in its Final Proposals.

The proposed increase affects affordability, connectivity, consumer choice and Heathrow's role as a hub

2.4. Contrary to HAL which operates an airport with significant market power, airlines operate in highly competitive markets and are continually seeking to maximise yields. In this context, increases in airport charges cannot simply be passed through without impacting affordability and choice. This constraint is particularly acute in periods of heightened geopolitical uncertainty.

2.5. Given that increases in airport charges will inevitably affect yields, airlines will have to reassess the viability of less profitable routes. This may require deploying smaller aircraft, reducing frequencies, or, in some cases, withdrawing services and routes entirely. This in turn risks creating a negative feedback loop, whereby reduced connectivity diminishes the strength and attractiveness of the network and affects the availability of choice to consumers.

2.6. Indeed, the risk on choice represents a direct consumer harm and should be explicitly recognised by the CAA in its assessment of the impact of higher charges. [REDACTED], we are disappointed that the CAA has not engaged with the issues of affordability and choice in its assessment.

2.7. The CAA should address these issues explicitly in its Final Proposals, and we remain available to re-engage on this issue as necessary. In fact, the CAA's stated intention to consider the impact of charges and to include affordability as an explicit evaluation criterion in the context of its recent consultation on the regulatory models for Heathrow expansion makes its decision not to do so for H8 particularly striking, especially as H8 will be establishing the cost baseline for expansion.

A charge evolution from an H8 two-runway scenario cannot be viewed in isolation from other headwinds

2.8. Indeed, it is important to consider the broader context in which the CAA is setting charges, including the cumulative impact of its policy decisions across other areas affecting costs at Heathrow. This is not solely a question of H8, but of the multiple and concurrent headwinds currently facing airlines and consumers.

2.9. As set out in its Method Statement, H8 is intended to establish the level of charges required to operate a two-runway airport. However, the CAA has already issued a draft decision on early expansion costs for 2025–2026, allowing HAL to recover approximately £320 million (2024 CPI) from passengers[2]. In addition, HAL has indicated its intention to incur around £6 billion of early expansion-related expenditure during H8, with further expansion costs expected to run to several billions irrespective of the regulatory model adopted[3]. The CAA itself has

[2] See CAP3238.
[3] See CAP3238, paragraph 1.11.

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acknowledged that the impact of modernisation and expansion at Heathrow could more than double charges in real terms.

2.10. As set out in our responses to the various CAA consultations on Heathrow, the CAA should assess therefore the combined impact of these costs on charges in the round on affordability, choice and connectivity. This is critical given that H8 will establish the baseline for consumer charges ahead of expansion over the coming decades. It would also be in line with the CAA's decision to include affordability as an explicit evaluation criterion for the regulatory framework on expansion.

2.11. This assessment must also be viewed in the wider context of significant and growing cost pressures on airlines, including increased expenditure associated with energy transition, increased geopolitical uncertainty as well as passengers facing some of the highest levels of aviation taxation globally. The impact of H8 charges must therefore be assessed cumulatively, taking into account expansion-related costs, the transition to SAF, and Air Passenger Duty.

2.12. While the CAA may not control all of these cost drivers, it is important to recognise the cumulative burden currently faced by consumers and the very likely prospect of further increases. In this context, there is a clear risk to Heathrow's competitiveness and long-term attractiveness as a hub, which will turn impact choice and growth.

2.13. Against this backdrop, the CAA must ensure that H8 charges are set at a truly efficient level. We observe that in many areas of its Initial Proposals, the CAA has erred on the side of caution despite the available evidence (e.g. cost efficiency targets) or has significantly overestimated costs (e.g. the level of the WACC). While we recognise the principle that H8 should represent a "fair bet", it should not lead to unjustifiably high charges, inefficient costs, an imbalanced regulatory package protecting HAL from multiple sources of risk, and an overcompensation of the regulated monopoly at the consumer's expense. This would be contrary to the CAA's statutory duties to protect consumers and ensure efficiency.

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3. H8 Constructive Engagement and HAL's Business Plan

BA and the airline community have engaged extensively with HAL throughout the H8 Constructive Engagement process, in support of the CAA's objective of enabling a structured and transparent scrutiny of HAL's Business Plan under a single-plan framework designed to address H7 shortcomings. However, **persistent deficiencies by HAL in transparency, information quality and engagement** – raised consistently by the airlines to the CAA throughout Constructive Engagement – have materially **limited meaningful challenge and assessment of HAL's proposals**. These issues have been **recognised by the CAA** in its Initial Proposals, which identified significant weaknesses in HAL's Business Plan rating it as "low quality".

Against this backdrop, we have **strong concerns regarding the potential acceptance of substantive new information from HAL after the conclusion of CE, which would undermine the integrity of the process, bypass structured scrutiny, risk perverse incentives and regulatory gaming, and risk reintroducing allowances previously rejected due to insufficient evidence**. This would be at the detriment of the consumer. We therefore consider that **a very high bar must apply to any late submissions**, limited to narrow clarifications with clear consumer benefit that the airlines can test meaningfully and respond to. We set out the conditions under which the CAA should weigh such information subject to scrutiny and aligned with the principles of transparency, proportionality and effective stakeholder engagement underpinning the H8 framework.

The shortcomings of H8 Constructive Engagement and HAL's Business Plan

3.1. Since its start in October 2024, British Airways and the airline community engaged extensively with HAL in the H8 Constructive Engagement (CE) process and have firmly supported the CAA's objective for CE to provide a structured and transparent process through which HAL's Business Plan can be scrutinised, tested and refined so that it delivers for the consumer.

3.2. The CAA's H8 Method Statement clarifies the key role of airline engagement and challenge in shaping HAL's Business Plan: "*[The CAA] consider[s] that a high-quality business plan submission that is well-evidenced and* ***is shown to be in the interest of consumers furthers the interest of consumers because it would: enable airlines appropriately to engage with and challenge HAL's proposals for H8; and facilitate our conduct of the H8 review in a timely and proportionate manner****, as a result of the high-quality information* ***and airline engagement.***" (our emphasis)[4]

3.3. The CAA designed the H8 process around a single Business Plan submission, which was as explicitly designed to address the shortcomings of H7 identified following the CAA's lessons learned exercise. The single Business Plan framework was adopted precisely to avoid incomplete submissions.

3.4. However, we repeatedly raised concerns over the lack of transparency across key building blocks, the quality of information provided, HAL's unwillingness or refusal to share certain information with airlines and the lack of progress between Rounds

[4] See CAP3044, paragraph 3.5.

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1 and 3 of CE. This did not allow for a detailed and meaningful discussion of the elements of the price control or whether HAL's proposals are delivering in the consumer interest. More specifically, we repeatedly set out those concerns in our following letters to the CAA:

i. **The letter of 27 May 2025** following the conclusion of Round 2 of CE, setting out our concerns on the lack of detail and transparency by HAL that prevented meaningful engagement on capital optioneering and prioritisation, asking the CAA to consider how to incentivise HAL to deliver a markedly improved engagement.

ii. **The letter of 8 August 2025** following HAL's publication of the H8 Business Plan ("BP") setting out five action areas for the CAA, including clarifying the true extent of the increase proposed by HAL (up to 47% in real terms with current Business Rates), establishing a suitable evaluation framework for the impact of higher charges on consumers and ensuring coordination with the long-term impact of potential capacity expansion at Heathrow.

iii. **The letter of 13 October 2025** containing our feedback on the shortcomings of Round 3 of CE, including HAL's continued lack of transparency, the pronounced information asymmetries and HAL's refusal to share information requested by airlines, the lack of meaningful engagement, the continued absence of a clear 'golden thread' in HAL's BP and the CE process, opacity of information on key cost categories and refusals to share information on its financing and depreciation. We set out how the specific areas of lack of transparency had impacted our ability to engage, influence and assess HAL's proposals, and set out suggested areas of focus for the CAA to remedy those issues.

iv. **The letter of 30 January 2026** on our proposed design on Round 4 of CE on the CAA's Initial Proposals ("IPs"), including the failure by HAL for meaningful engagement in Round 3 and the significant gap with airlines on the size and scope of the capital envelope.

v. **The letter of 5 March 2026** responding to the CAA's proposed approach for Round 4 of CE, consolidating previous concerns and setting out the need for the last round of CE to finally address longstanding issues on transparency and information asymmetry.

The CAA's assessment of the shortcomings

3.5. Unfortunately, our concerns above have remained addressed throughout the process up until the conclusion of the final Round 4 of Constructive Engagement in April 2026. HAL's persistent lack of transparency has precluded an effective engagement, including an effective prioritisation at the crucial time of HAL's preparation of its Business Plan, and further demonstrated the pronounced information asymmetries built into the current regime

3.6. Indeed, the CAA explicitly recognised many of our concerns over the quality of the information provided in its assessment of HAL's Business Plan and has identified

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material deficiencies in relation to completeness, robustness and evidential support. The CAA notes that these include the absence of a clear "golden thread" linking consumer research to identified needs, options and outcomes, the lack of assurance on the underlying consumer evidence, and material weaknesses in the presentation and granularity of opex. The CAA has itself assessed HAL's Business Plan as being of "low quality", meeting only three of seven criteria of the Business Plan Incentive (BPI). We set out our views on the CAA's assessment under the Business Plan Incentive further below.

3.7. We also strongly support the CAA having taken the lack of transparency into account in its scoring of HAL's business cases for the purpose of setting the proposed capital envelope and rejecting key requests by HAL for operational expenditure such as the majority of its proposed overlays. We set out our views further in the sections of our response on the capital envelope and operating expenditure.

Lack of CAA analysis of airline concerns on HAL's lack of transparency

3.8. We are disappointed that the CAA has not substantively responded to the repeated airline concerns regarding HAL's lack of transparency and refusal to share key information contained in the letters by the airline of community of 27 May 2025, 8 August 2025, 13 October 2025, 30 January 2026 and 5 March 2026. A letter was subsequently sent by the community on 8 May 2026 regarding the CAA's lack of response on instructing HAL to share its debt book and Fixed Asset Register to enable the community to interrogate the respective cost of debt allowances and depreciation retained by the CAA. We request that the CAA reflects those concerns in its Final Proposals.

3.9. We are equally disappointed that the CAA and its advisers do not appear to have engaged fully with the detail of certain aspects of the airline Alternative Business Plan which the CAA requested airlines to produce. A number of specific challenges raised by airlines, including on individual opex cost lines, do not appear to have been substantively addressed. We set out these gaps, and the required corrections, in the relevant building block chapters of this response.

Acceptance of further information after the conclusion of CE and the single BP

3.10. We understand that HAL may seek to submit extensive new information and evidence at this stage, including reopening business cases, reprioritising projects and re-arguing benefits and cost overlays. We are strongly concerned regarding the integrity, fairness and effectiveness of the Constructive Engagement process in relation to the potential acceptance of additional information submitted by HAL following the end of Constructive Engagement.

3.11. Allowing HAL to introduce substantive new material after the conclusion of Round 4 would fundamentally undermine the core principles and the purpose of the Constructive Engagement framework. A BP that fails to meet the CAA's own quality standards should not be capable of being remedied through late submissions outside of the defined process. This is particularly the case where the outcome of the CAA's

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assessment of any new evidence may result in final decisions on H8 that the airline community has not had an opportunity to engage with or been consulted on.

3.12. It would equally risk harming consumers by permitting the reintroduction of proposed allowances that the CAA has already discounted in its Initial Proposals, often on the basis that they fell materially below the required standard of evidence.

3.13. Whilst there may be merit in the CAA considering representations that demonstrably improve decision-making, the adoption of a single Business Plan framework for H8 – explicitly intended to address the shortcomings identified in H7 – requires that **a very high bar be applied to the acceptance of any such information at this late stage**.

3.14. In this context, we would expect the CAA to ensure, as set out in the H8 Method Statement and Business Plan Guidance', that its assessment under the Business Plan Incentive (BPI) will explicitly take into account any attempt by HAL to remedy known deficiencies through late evidence, and that such evidence will only impact the CAA's provisional assessment for BPI purposes.[5] In particular, it is important that **any such new evidence will not will not be afforded the same weight as material submitted on time and in accordance with the CE process** as this would create the wrong incentives for HAL to not put the best business plan forward in the first instance. In addition**, any material changes in allowances to HAL resulting from this process should not be undertaken without further Constructive Engagement and consultation** given the CAA's primary duty to further the interests of users of air transport services whose voice is represented through the airline community.

3.15. We note that the CAA's H8 Method Statement states that information submitted late in the price control may be accepted where this is necessary, appropriate and in the interest of consumers[6]. This standard **must be applied strictly to ensure that regulated entities do not seek to circumvent the appropriate scrutiny during the price control process**.

3.16. Across UK regulators, Ofwat stated during its most recent PR24 price review that companies would need to provide convincing evidence why new information or claims could not have been submitted as part of their original business plans[7]. Ofwat also explained why late claims were problematic in later documentation. **The reasons included the risk of information asymmetry (companies are only likely to submit claims where they increase allowances), the inability to face the same scrutiny (through BP assurance, regulatory assessment and customer assessment) and the need to keep draft determination responses focused**.

3.17. The issue is even more acute in the regulation of HAL, given the CAA's reliance on the Constructive Engagement process and the airline challenge which is a key aspect of the price control consistent with its primary duty to further the interests of users

[5] "*[A]ny additional information that HAL might submit to us late in the price control process is appropriate and HAL can justify why the further submission is necessary, appropriate and in the interests of consumers*" (page 28 of CAA Method Statement and Business Plan Guidance).
[6] See CAP3044, paragraph 3.15.
[7] IN2402-2024-price-review-—update-for-water-companies-.pdf

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of air transport service. If HAL submits significant new evidence late in the process, this would undermine Constructive Engagement and remove the airlines' ability to engage with and challenge the evidence. We have also seen during H8 that information submitted outside the business plan process is often not shared with airlines.

3.18. The CAA should therefore only consider narrowly defined, targeted clarifications where there are clear, demonstrable and unambiguous benefits for consumers. In doing so, the CAA should recognise the following:

i. **Extensive or material new information would amount to a re-litigation of HAL's single Business Plan**, rather than clarification. The single Business Plan framework was adopted precisely to avoid iterative and incomplete submissions, and HAL should not be afforded a further opportunity to address deficiencies outside that process.

ii. **Airlines would not have a meaningful opportunity to respond, thereby creating a clear asymmetry in the process**. HAL would be able to **introduce new, untested evidence without scrutiny**, while airlines would be denied the opportunity to challenge it. This would directly undermine the purpose and credibility of the Constructive Engagement framework and dilute the effectiveness of the Business Plan Incentive.

iii. CE is designed as a structured and iterative process in which evidence is shared, tested and refined across successive rounds. **Round 3 which concluded in November 2025 represented the appropriate stage for detailed testing of the Business Plan**, with Round 4 intended to consolidate positions based on the CAA's Initial Proposals. Allowing material new submissions after this point would bypass that structured scrutiny. Indeed, HAL was provided with the opportunity to address airline questions and information requests during Round 3, following publication of its Business Plan, but repeatedly failed to do so. Allowing materially revised information and amendments to the originally submitted Business Plan now would effectively reopen the Business Plan outside the agreed process.

iv. The CAA's methodological framework, including on areas such as opex and capital prioritisation, has been known to stakeholders since the Draft Method Statement in November 2024. HAL has therefore had sufficient opportunity to align its submissions with the regulatory framework without appropriate scrutiny.

v. **There is a clear risk of perverse incentives, whereby HAL seeks to reverse-engineer its submissions to artificially meet the CAA's methodology** at this stage. We are acutely concerned, for example, that HAL may seek to create a confusing narrative around asset maintenance projects or misrepresenting projects already assessed by the CAA and its consultants.

vi. The **CAA's rejection of a significant proportion of HAL's technology, resilience and digital overlays is one of the strongest elements of the Initial Proposals** and is strongly supported by the airline community. These proposals were characterised by poor quality evidence, and the CAA was right to apply the need,

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additionality and efficiency tests rigorously. That level of rigour must be maintained through to Final Proposals.

3.19. Should HAL provide further information on specific capital business cases, we consider that the CAA should treat such information in accordance with the following principles:

i. Such information may inform prioritisation within the CAA's defined capital envelope but should not materially alter the size of the envelope itself, which has been assessed against deliverability constraints and overall affordability.

ii. The regulatory framework is concerned with setting the overall capital envelope, not mandating individual projects.

iii. The emergence of additional projects at this late stage further reinforces the need for robust prioritisation within a constrained envelope.

3.20. More broadly, we consider that **the process should not move into a phase of re-litigation of the Business Plan**. The single Business Plan framework was explicitly designed to address the shortcomings of H7 identified during the CAA's lessons learned exercise, and this objective should be upheld. **HAL should not be allowed to benefit from prior shortcomings in transparency, nor from any form of regulatory gaming**.

3.21. We therefore request that the CAA:

i. Clarifies the threshold for accepting additional information post-Round 4, limiting this **to minor and strictly defined clarifications**. The CAA should state that it only considers new evidence where HAL can demonstrate a compelling reason why it could not have been submitted earlier.

ii. Clarifies that it will only consider new evidence where it is **balanced and clearly supports consumer outcomes**.

iii. Confirms that any material **new evidence will not be considered without providing airlines with a proportionate opportunity to respond and where such new evidence does not materially alter the overall capital envelope.** Any evidence submitted by Heathrow should be made immediately available to airlines, with a clear process and a reasonable timeline for airlines to respond within the regulatory timetable.

iv. Clarifies that **HAL should face a penalty under the Business Plan Incentive if relevant information was available but not submitted**, particularly where this has undermined the effectiveness of the CE process.

v. Confirms that it **will not consider any representations made by HAL after the deadline for responses to Initial Proposals on 29 May 2026**.

vi. Ensures that any such decisions are aligned with the core principles of transparency, proportionality and effective stakeholder engagement.

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4. Delivering for Customers

BA welcomes Steer's assessment, which highlights inconsistencies in how priorities have been derived, with key areas omitted or insufficiently reflected. We **agree with the CAA that the research has not been linked to the Business Plan through a "golden thread",** and that this weakens the overall evidential basis of the plan. We also note that **departing baggage performance is a clear priority** given recent disruption and harm on consumers.

We acknowledge the CAA's intention to retain the overall structure of the OBR/MTI framework, including the rebate envelope, and we recommend specific improvements. However, we highlight the inherent limits of a service regime in a single-operator setting in replicating the discipline of customer choice. These limits are exacerbated **by the insufficient calibration of certain measures and targets**, which have failed to address persistent underperformance in areas such as departing baggage or reflect investment benefits. BA reiterates its position that **service level bonuses are not appropriate**, as they reward expected performance from a regulated monopoly, create perverse incentives, and have resulted in **HAL earning more in bonuses than paying in rebates despite ongoing service issues**. The **MTIs therefore require material tightening** in both design and calibration to ensure incentives properly target performance, strengthen accountability, and protect consumers from continued service failings.

While we **strongly support the introduction of a financial rebate for departing baggage**, the proposed 98% target **fails to capture the scale and harm of ongoing and repeated major system outages by HAL on the consumer**, meaning the measure does not provide effective incentives for resilience or consumer protection. We therefore continue to argue for the **introduction of the backstop** to capture such events and incentivise performance. We propose similar improvements across other MTIs, notably reflecting the **additional train capacity for Track Transit System, improve security queue measurement** and **incentivise PCA performance**, in order to ensure realisation of the benefit of investments for the consumer.

BA agrees with the CAA's assessment that **HAL has not demonstrated the consumer benefit of its proposed airline eligibility criteria** for certain rebates and **cautions against placing complex regulatory structures around activities that are incentivised competitively** and that would dilute HAL's accountability.

Consumer engagement

4.1. We welcome the CAA's commissioning of Steer to review HAL's consumer research and engagement activity, including the robustness and completeness of the evidence base. We note Steer's findings highlighting material shortcomings in HAL's evidence, including less well-developed analysis of the cargo sector and the absence of primary research on consumers' views of minimum acceptable service levels.

4.2. We agree with Steer's assessment that it is unclear how HAL derived its list of 18 priorities. In particular, the prioritisation is not consistent with the underlying evidence (e.g. Table 33 of the Business Plan), where several attributes with relatively high importance are not identified as priorities (for example, seating, walking distances and wayfinding). In addition, the absence of prioritisation between the

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identified priorities further limits their usefulness in informing effective capital allocation and service level design.

4.3. We agree with the CAA's conclusion that there is an absence of a clear "golden thread" linking HAL's consumer research to its Business Plan. In particular, there is no clear process through which identified customer needs have informed the prioritisation of options and the resulting plan. Instead, the research appears to have been used primarily as a high-level "sense check", rather than as a substantive driver of decision-making.

4.4. We note our strong concerns in relation to departing baggage system, given the frequency and scale of significant system failures at Heathrow in recent years and the resulting consumer harm, alongside significant operational, financial and reputational impacts for airlines. Ensuring that passengers travel with their baggage is therefore a critical issue. Airlines are competitively incentivised to deliver timely baggage performance, given its visibility to customers and impact on satisfaction. This dynamic is equally relevant for transfer baggage, where airlines already prioritise timely delivery to protect onward connections and minimise missed bags. We expand on baggage in the section on Measure, Targets and Incentives below.

4.5. We agree that accessibility should be a key theme within the Business Plan. We also agree that the justification provided by HAL for "look and feel" aesthetics is weak.

4.6. While wellbeing is identified as a priority area, the scope of proposed interventions is broad and insufficiently defined. It remains unclear how specific measures (e.g. retail offering versus quiet spaces) align with passenger priorities, and further engagement with airlines is required to ensure that investment is appropriately prioritised and targeted.

4.7. We agree that disruption and delays represent a significant customer pain point and support the CAA's focus on resilience, which was also identified by airlines as a key priority during Constructive Engagement, alongside consumer outcomes, affordability, infrastructure and capacity, and sustainability. We address these issues further in the context of the capital envelope and prioritisation.

Outcome Based Regulation and Measures, Targets and Incentives

4.8. BA acknowledges the CAA's intention to retain the overall framework the Outcome Based Regulation in incentivising ongoing service performance through service level rebates premised on individual Measures, Targets and Incentives (MTIs). We recommend specific improvements to the framework.

4.9. However, we highlight the inherent limits of a service regime in a single-operator setting in replicating the discipline of customer choice. These limits are exacerbated by the insufficient calibration of certain measures and targets, which have failed to address persistent underperformance by HAL or reflect investment benefits.

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4.10. Importantly, the MTIs require material tightening in both design and calibration to ensure incentives properly target performance, strengthen accountability by HAL, and protect consumers from HAL's continued service failings.

4.11. Consistent with previous airline community submissions, the outcomes should focus on the aspects of airport service most valued by consumers, while remaining simple, transparent and readily understood. They should also recognise the impact of the airport operator's performance on other stakeholders. The framework should drive continuous improvement, including through the tightening of targets where justified, for example where investment has delivered expected service improvements or where significant underperformance by the airport operator is experienced. Our comments in this chapter are therefore guided by this logic.

Bonus/Rebates

4.12. BA agrees with the CAA's proposal to maintain the current rebates at 7% of airport charge revenues. We have specific comments on how individual MTIs underpinning the rebate system ought to be tightened to incentivise performance, reduce ongoing underperformance harming the consumer (such as the repeated baggage system outages) and reflect the benefits brought in by investments (such as in the Terminal 5 Track Transit Train and security).

4.13. BA reiterates its long-standing position that there should not be any bonuses for service quality levels. We disagree with the principle of HAL awarding itself a bonus for maintaining service levels that are to be expected from a monopoly airport infrastructure provider, and the perverse effects this is generating. During H7, HAL awarded itself several bonuses, including a service level bonus in the 2024 charges of £0.11 per passenger for year 2022 (totalling almost £9 million) despite significant disruption at Heathrow after the pandemic owing to HAL's lack of resourcing of critical functions. We therefore ask for this bonus to be removed for H8.

4.14. In fact, we note that the bonus system has resulted in a fundamental imbalance and insufficient ambition for HAL. As the CAA has confirmed in its IPs, over 2023-2025, HAL has earned 50% more in bonuses than paying out in rebates despite incurring an almost 5 times higher exposure to rebates. Given ongoing service level issues at HAL (such as the ongoing baggage outages) there is in our view a clear demonstration that rebates ought to be tightened to target underperformance and reflect the benefits brought in by significant capital expenditure.

Year	Rebate	Bonus
2023	£1.4m	£2.2m
2024	£2.5m	£2.8m
2025	£2.6m	£5.0m
Total	**£6.5m**	**£10m**
Exposure to airport charge revenues	**7%**	**1.44%**

Source: CAA IPs and CE Round 4

4.15. In addition, we are worried that the bonus system leads to an unnecessary increase in costs by HAL. For instance, the EE/YA report on opex for the CAA notes the

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existence of inefficiency in security costs due to the MTI scheme, and since there is a bonus element in it, we believe that some of this additional inefficiency could be linked to the desire to achieve a bonus.

4.16. Without prejudice to our position that the bonus must be withdrawn, we welcome the CAA's proposal to reject HAL's request to double the bonus pot and instead retain at the current level (1.44%). This proposal would fundamentally alter HAL's risk exposure and require an adjustment to HAL's cost of capital.

4.17. In line with the community's previous submissions to the CAA and HAL, including in the ABP, we believe that certain principles ought to apply to HAL's bonus measures:

i. The measure needs to be within HAL's control.

ii. The measure must mirror the rebate MTI.

iii. The weighting of the bonus measure should not be more than half of weighting of the equivalent rebate.

iv. The measure is a true reflection of outperformance that is not factored into proposed allowances. If the additional performance has been delivered through higher opex, such opex should not become the baseline for the following regulatory period.

v. The measure does not apply where alleviation has been granted or there has been material disruption event within HAL's reasonable control.

4.18. In addition, we have argued for a principle that bonuses or rebates cannot be assigned to activities delivered under the pass-through mechanism of Other Regulated Charges (ORCs). This is because any inefficiency generated to meet the targets could be passed through higher charges. This is discussed in the ORC section of our submission.

Baggage (Timely Delivery from Departures Baggage system)

4.19. We welcome the CAA's proposal to introduce a financial rebate for the timely delivery from the departures baggage system, which is currently a reputational measure. The airline community has repeatedly requested the introduction of such a financial rebate to incentivise performance and accountability by HAL in light of the repeated and extensive departing baggage system outages over the past years – which we set out in a table below. These outages have had a significantly disruptive impact on consumers, our operations and our reputation. We note that the airlines had made a similar request for such a financial rebate during the H7 OBR mid-term review. We also support the CAA's proposal to change the measure of timely delivery from Departures Baggage system from 30 minutes to 20 minutes which airlines and HAL agreed during Constructive Engagement.

4.20. In line with the airline proposal during Round 2 of CE and in the ABP, we propose a weighting of 0.6% within the 7% rebate package for the measure. This would be

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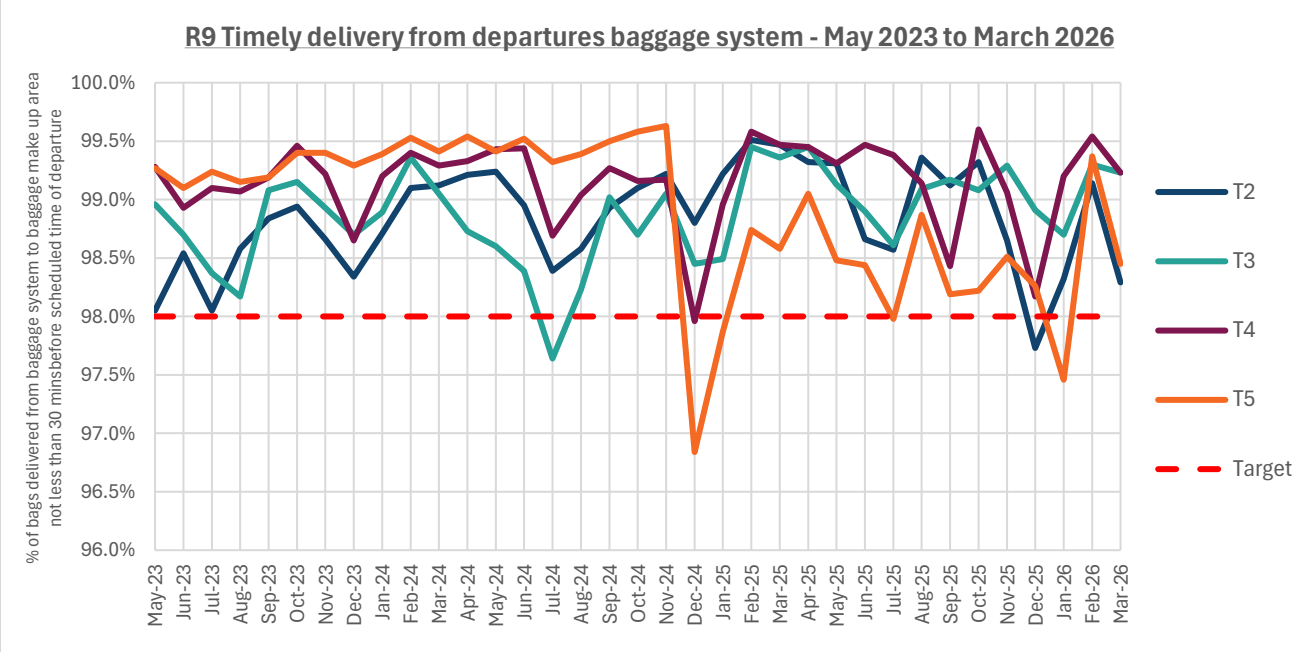
funded through a reallocation from existing measures, allocating 0.2% through the removal of the existing Hygiene Testing measure and the reduction in the weighting for the measures on Wayfinding and Cleanliness (0.2% and 0.2% respectively).

a. Proposed target is imbalanced as it does not reflect recurrent major outages impacting the consumer

4.21. However, we contest the CAA's proposal to maintain a target of 98% as this fails to reflect major system outages by HAL – which have been recurrent, extensive and often impacting during particularly busy times – and have a pronounced impact on the customer and airport resilience. We urge the CAA to reconsider its approach to take forward the airlines' Alternative Business Plan proposal to add a backstop to the measure designed to capture major system outages, incentivise performance and resilience, and reduce the heavily disruptive impact of those systematic incidents on users. We explain why this matters for the balance of the incentive, for the consumer and for airlines below.

4.22. As the CAA's own analysis from Round 4 of CE demonstrates, the current 98% target would fail to kick in during the majority significant outages over the past 3 years, with the exception of 4 incidents across all terminals[8]. We set out a non-exhaustive list of major incidents at the terminals where BA operates below to demonstrate that the majority would fail to be captured by the 98% target.

CAA analysis of current of timely baggage delivery against the current 98% target



Source: CAA analysis from Round 4 of CE, session of 21 April 2026, using HAL's publicly available performance reports (updated 15 May 2026)

[8] We note the CAA analysis is based on bags being delivered no less than 30 minutes before scheduled time of departure as opposed to 20 minutes which is what was agreed in Constructive Engagement.

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[REDACTED]

4.23. Indeed, an MTI seeking to incentivise performance should not ignore such material incidents where HAL is clearly underperforming, otherwise it risks being ineffective and imbalanced. In fact, HAL itself publicly acknowledged on 19 May 2026 following the most recent system outage in Terminal 5 that "Heathrow's baggage system operated with 99 per cent reliability despite the airport operating at full capacity", demonstrating that a 98% target would constitute a service degradation.

b. Proposed target would not focus the incentive on the harm of major outages on the consumer and airlines

4.24. The impact of HAL's major baggage system outages is highly disruptive and harmful on the consumer. Thousands of passengers have experienced delays, uncertainty and inconvenience while travelling without their belongings at Heathrow in recent years.

4.25. Our customer research demonstrates that the impact on customers of travelling without their baggage is very significant and represents one of the most acute impacts in a disrupted journey. [REDACTED]

[REDACTED]

4.26. The baggage journey within the airport is a component of the overall travel experience where passengers place a high degree of trust in both the airline and the airport operator to deliver their belongings reliably and on time.

4.27. When a bag does not arrive as expected, this trust is fundamentally undermined. The absence of baggage is often perceived as a direct failure of the airline, regardless of where accountability sits, and can have a lasting impact on a passenger's willingness to travel with that airline again. There is therefore a direct impact on our reputation.

4.28. These incidents also have a significant financial and operational impact on airlines through no fault of their own. [REDACTED].

4.29. Moreover, the airport demonstrates a clear and ongoing lack of resilience. So far in 2026, T5 alone has experienced three major outages. These incidents follow of pattern of operational failures by HAL exposing a lack of system resilience and an inability to contain issues before they escalate. Their recurring nature points to a more fundamental concern: that Heathrow's critical infrastructure and contingency arrangements are not delivering the level of robustness required for an airport of its scale and importance.

4.30. The introduction of the backstop in the MTI is therefore required to capture the significant disruption caused by those major outages, incentivise performance and protect consumers from their highly disruptive impact. We recognise that the CAA may have concerns over the way in which such a backstop would work (for instance, the airline proposal in the Alternative Business Plan for a fixed fee per bag) and we therefore propose an alternative structure by which the monthly rebate allocated within the measure kicks in immediately upon the incidence of a major outage. In

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line with the Airline Business Plan, we retain the definition of a "major outage" as "50 or more bags miss their departing flights on a single day in a single terminal due to single system issue (or multiple issues if they worked in combination to cause the event)"[9].

4.31. In the alternative, we would urge the CAA to adopt a target of 99% to effectively capture those major outages. This target in line with HAL's public acknowledgement following the most recent major outage in Terminal 5 that "*Heathrow's baggage system operated with 99 per cent reliability despite the airport operating at full capacity*", demonstrating that a 98% target would constitute a service degradation[10].

c. Proposed airline eligibility criteria

4.32. We agree with the CAA that HAL has not demonstrated a clear and material impact from its proposal to reflect airline and ground handler performance within the overall departing passenger system. In fact, we reject any proposal for criteria on airlines to render them eligible for the departing baggage rebate, which would encroach upon competitive services that are appropriately incentivised under our relevant contracts. In other words, encoding regulatory arrangements for a non-regulated activity is not a proportionate response where these activities are already incentivised competitively to deliver for the consumer. HAL, as the regulated monopoly provider, should remain the focus of performance obligations, particularly given the limited competitive pressure to drive improvements to the significant underperformance shown above.

4.33. In addition, any such criteria would also introduce unnecessary regulatory complexity and result in reduction in HAL's risk exposure that would have to be appropriately reflected in the regulatory package. For instance, if HAL were to withhold and retain an otherwise rebate due to an airline, this would reduce its risk exposure and an appropriate recognition in the cost of capital would be required.

d. Baggage Reclaim

4.34. We contest HAL's proposal for an eligibility criterion on airlines for baggage delivery waiting times. We agree with the CAA that this is a priority for consumer and note that this is already competitively incentivised. Indeed, airlines are already strongly incentivised to deliver customer bags quickly, as performance is highly visible to customers and directly impacts satisfaction and reputation.

4.35. A similar incentive applies to transfer baggage. Airlines prioritise the timely delivery of these bags to protect onward connections and reduce missed bag rates, supported by ongoing operational improvements and prioritisation initiatives. However, during system disruption, transfer processes are often restricted first, increasing the likelihood of missed connections and highlighting that system performance, rather than airline activity, is the driver of disruption.

[9] See Airline Business Plan submitted to CAA in October 2025.
[10] Financial Times, "British Airways seeks up to £10mn from Heathrow after baggage system chaos", 19 May 2026 https://www.ft.com/content/42cc3bc4-f33a-415b-ae75-cd36fe43ed67?syn-25a6b1a6=1

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Security

4.36. We support the CAA's proposals to maintain the current monthly measurement for security search queues. We agree that there are currently no reliable data demonstrating the benefits of a move to daily measures. We also agree with the CAA that HAL's proposals for adjusting the metric, target levels and incentive would appear to weaken the incentive and a therefore result in a deterioration of performance. The benefits of moving to daily measures have thus not been demonstrated.

4.37. However, the entry into service of the XOVIS system during H8 will allow for automated per passenger queue measurement improving how queues are measured. While this may not be ready for entry into service across all terminals by the time of the H8 determination in mid-2027, we believe we should not be waiting to derive the benefit of the new system until the subsequent price control.

4.38. In line with the airline proposal in the Alternative Business Plan, we therefore propose that the CAA introduces a licence condition containing a committed go-live date for a new measure using XOVIS data, that will more accurately measure queue time at an individual level. The development of new measure must run in parallel to the rollouts across the individual terminals, to enable calibration of a daily measure, ready for the go-live date. Such a target date could be, for instance, 1 January 2028 when the system is expected to be fully operational.

4.39. Separately, given the significant improvements in security processes that will be achieved through the Next Generation Security investments, there is a need to reassess the security targets. We would welcome further discussions with the CAA on this issue.

4.40. Furthermore, we reject HAL's proposal for an eligibility criterion on airlines to qualify for the security queue rebate linked to airlines providing passenger forecasts to inform HAL's security staffing plans. We agree with the CAA that the impact of this proposal is unclear. This encroaches upon the airlines' business models, reduces HAL's risk exposure and introduces unnecessary regulatory complexity considering that airlines already provide this information to HAL.

Track Transit System (TTS)

4.41. The Track Transit System (TTS) in Terminal 5 is the automated link to transport departing and arriving customers between T5A, T5B and T5C where BA operates. An investment of [REDACTED] to purchase 20 new cars was approved at G3 in 2019. The business case for this purchase was to enable an increase in the capacity of the TTS. This is because the existing system with 10 cars would frequently have insufficient capacity in the morning for arriving customers, resulting in customers either being uncomfortably crowded on to a train, or needing to wait for the next service.

4.42. The objective of the investment is for the 20 new cars to replace the 10 old ones, and hence double the capacity of the system, enabling an enhanced customer

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experience in the short-term and protecting for future growth within T5 in the longer term. The 10 old cars are generally operated as 2 trains of 4 cars each, with 2 spare cars in the maintenance facility. The 20 cars will enable up to 4 trains of 4 cars each to be running in the system at any one time, with 4 cars in maintenance. The project also included enhancements to the maintenance facility to enable the injection of a train as a standby if required.

4.43. Running additional trains within the TTS system will therefore increase the frequency of the trains, and passenger throughput per hour. The demand for the TTS in T5 is such that 4 trains are not required to operate at all times. There is a trade-off between running sufficient train capacity to deliver a comfortable customer experience versus the operational maintenance costs of running more trains than required.

4.44. During Constructive Engagement, agreement in principle was reached with HAL for the existing two MTIs for the TTS to be replaced by two new measures with the same allocated weightings to reflect these new cars coming into service. One measure is based on capacity matching against forecast passenger demand using train-hours and the other acts as a backstop and ensures a minimum level of service.

4.45. The train-hour measure has been agreed in principle with HAL, whereby 98% of baselined planned train-hours must be operated in a month[11].

i. A variable daily timetable is determined in advance such that it delivers sufficient capacity to meet the forecast passenger numbers.

ii. This timetable would be the number of trains, operating at a given frequency, for particular hours, hence determining the train-hours per day and per month.

iii. In order to confirm that this timetable delivers sufficient capacity for the required customer experience, the capacity of each train-hour needs to be known. This requires the capacity of an individual train to be baselined, that is the number of cars per train, where each car has a capacity of 60 passengers.

4.46. **However, BA has reached a point of fundamental disagreement with HAL regarding the definition of a train in terms of the number of cars and hence its baselined capacity. A measure based on demand and capacity should define both elements as described above.** Without the agreement of the number of cars that make up an individual train, the capacity of a train hour for a particular mode of operation or frequency, cannot be calculated and baselined and therefore cannot be aligned to passenger demand.[12]

4.47. HAL's MTI proposal does not define a train as 4 cars which would mean that there could be times of the day during which shorter trains are run. This would be to the

[11] Recognising that additional hours are not banked, that is, HAL cannot exceed the target or earn additional train-hours to catch up or mitigate an outage.
[12] If, for example, on the day of operation, a train-hour can be achieved by a train that is 1, 2, 3 or 4 cars long, the measure could be achieved, but the customer experience significantly impacted. Without an agreement as to the capacity of an individual train (number of cars) this measure does not deliver any protection to the consumer and is of little benefit.

detriment of the consumer if shorter trains or less capacity were to be operated during a peak period, HAL would still achieve the MTI if only defined at a train level without specifying the number of cars.

4.48. This is not a hypothetical risk. [REDACTED]. There is therefore a need to specify the definition of a train as 4-cars in length in this new specific demand- capacity measure.

[REDACTED]

4.49. Under this measure, there could be periods when no trains are run. For this reason, we have also proposed the second backstop measure to HAL to ensure delivery of a minimum level of capacity. This would be premised as the operation of 2 trains (each of 4 cars in length) running 99% of the time, over the month, between [REDACTED] and [REDACTED].

i. Although this gives some protection to the consumer, ideally this would be measured at a daily level to ensure a minimum level of service operating on a particular day, however that has not been agreed with HAL.

ii. Although the backstop measure is simpler in nature, it also requires a train to be defined as consisting of 4 cars, to again protect the consumer experience and make efficient use of the assets purchased. However, as noted above, there has been no agreement by HAL on defining capacity as HAL will not commit to the number of cars making up a train.

4.50. For both of these measures, we have agreed with HAL that they could start 6 months after the final new car has been commissioned into the system to allow sufficient time for any snags or issues to be addressed. However, we are not clear from HAL on this date.

4.51. Train capacity aligned to the forecast passenger demand enables a good customer experience and a non-crowded comfortable journey. Customers should not be unnecessarily crowded on to a train, when sufficient capacity in the system exists but a decision has been made not to use it.

4.52. The fact that the full available capacity of the TTS system is only required for a short period at peak times is not relevant. That will come out in the discussion around the timetable for the next month, which creates the baseline against which the MTI is measured.

4.53. We understand that there will be instances when a single car rather than a train needs to be taken out of service, however the process of getting a replacement car or train injected into the system needs to be efficient and generate minimal impact to our customers.

4.54. In summary, we agree with one of the MTI measures being based on train-hours operated per month against a baseline agreed in advance. However, the baseline requirement needs a train to be defined as "4 cars each carrying up to 60

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passengers", such that the capacity over the hour is calculated by the number of trains operating at an agreed frequency (the timetable). **Without defining the capacity of a train, it is not clear how the required number of train hours to meet the forecast demand will be calculated.** The second measure creates a backstop ensuring a minimum level of service is operated for customers across the operational day.

4.55. If agreement cannot be reached on the definition of a train as having 4 cars, this measure should revert to ones that are constructed and measured at an individual car level (i.e. car-hours). This will add unnecessary complexity; however, without the definition of the capacity of a train, and in turn the capacity of the system over the hour, these measures will not protect consumers.

PRM (Passenger Assistance Service - overall satisfaction)

4.56. We note the CAA's proposal to introduce a financial incentive for the MTI for Passengers with Reduced Mobility (PRM). It is important to state that BA fully recognises the importance for the consumer of having a reliable, safe and efficient PRM service and together with our shareholder IAG we are closely following PRM performance and have actively participated in the discussions for the new supplier contract that entered into force earlier this year.

4.57. In fact, in view of the existence of this contract, we are not convinced that there is a need to add an additional financial incentive that is [REDACTED] and may worsen customer experience.

4.58. In 2026, HAL signed a contract with a new supplier, ABM, that is expected to last until [REDACTED].

4.59. [REDACTED]

4.60. In addition, allocating an MTI to a service that is already incentivised elsewhere is not a proportionate regulatory response and would require reducing the weightings on other measures in order to accommodate it within the 7% cap for rebates. This will in turn reduce the effectiveness of those other measures, at the expense of the consumer. [REDACTED]

4.61. Similarly, it is important to note that PRM is currently an ORC. Given the low powered incentives on cost efficiency that exist within the ORC framework, which is effectively a cost pass through mechanism, the implementation of a financial incentive on an ORC could lead to HAL passing on potential cost inefficiencies to meet the target. We do not believe it is appropriate that a service quality framework should lead to such inefficient outcomes.

4.62. In view of the above, we request the CAA to review the targets within the existing PRM contract to satisfy itself that there are appropriate incentives in place for PRM performance, and thus and reconsider whether there is a real need to implement an additional, [REDACTED], and potentially ineffective financial MTI.

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4.63. Finally, we reject HAL's proposals for airline eligibility criteria on PRM services. As the CAA has rightly pointed out, HAL's rate card already contains tariff modulations based on pre-notification rates. Adding eligibility criteria would therefore be redundant as airlines are already commercially incentivised through the significant differentials in those modulations. It would equally add unnecessary regulatory complexity.

Preconditioned Air (PCA)

4.64. As previously highlighted to the CAA, we believe that it is important that the MTI on PCA be tightened. While having a measure of PCA availability is clearly essential, this does not measure the quality of the service provided. In this regard, we welcome the CAA's openness to further explore a measure on "serviceability" to reflect the improvements from significant capital expenditure.

4.65. Such a measure would need to be linked to the delivery of air volumes, pressure and temperature provided. The measure would need to consider the variations in requirements due to aircraft specifications. Similarly, it is not sufficient to measure outputs at the PCA equipment point and must ensure that serviceability is not affected by leaks in the air delivery hoses. We would welcome further discussions with the CAA to determine a measure.

4.66. We note further that the PCA availability target is still set at 98%. Following the findings of the H7 OBR mid-term review, this should be increased to 99%.

5. Traffic Forecast

BA supports the CAA's decision to commission an independent traffic forecast in line with the H8 Method Statement, recognising its central role in determining allowed charges. However, we consider that key elements of the approach have not been independently scrutinised, particularly the application of the shock factor. Experience from Q6 and H7 demonstrate that the CAA's forecast has materially underestimated traffic relative to outturn and airline forecasts, resulting in sustained under-forecasting, windfall gains for HAL and consumers paying higher charges than necessary.

A report by Skylark for the airline community confirms that while Steer's core modelling inputs for the CAA are broadly reasonable, several assumptions remain conservative – particularly on seat factors and traffic evolution – leading to an underestimate of demand over H8. **Skylark proposes a forecast of 447.6 million passengers against the CAA's base case estimate of 442.0 million passengers.**

More fundamentally, Skylark finds that the shock factor has failed to deliver on its stated objective of improving forecast accuracy, instead exacerbating under-forecasting, overlapping with the TRS mechanism and introducing additional regulatory complexity. This has a direct impact on charges. In light of this evidence, **BA agrees with Skylark that the shock factor should be withdrawn for H8 or, at a**

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minimum, recalibrated to correct identified errors, remove inappropriate assumptions and reflect improved industry resilience.

5.1. We agree with the CAA's decision to commission an independent traffic forecast in line with H8 Method Statement. The passenger forecast is a crucial part of the price control as it has a significant impact on the maximum level of allowed charges.

5.2. However, we note that Steer's independent assessment does not extend to the entirety of the parameters feeding to the calculation on the forecast, notably the application of the shock factor and whether this has delivered on its objective of improving the traffic forecast.

H7 shortcomings and state of play

5.3. As highlighted by BA during the H7 Lessons Learned process, the H7 process suffered from important shortcomings as HAL's forecast was high-level and opaque. HAL also invoked confidentiality and intellectual property over the model, depriving users the opportunity to cross-examine robustly the drivers, assumptions and any differences to the airlines' forecast. This led to the use by the CAA of a disputed passenger forecast model that defied commercial reality.

5.4. Indeed, there have been significant discrepancies between the CAA's forecast and outturn passengers since the setting of the H7 price control in March 2023. In contrast, outturn passengers confirmed the accuracy of the airlines' forecast.

	2022	2023	2024	2025	2026	Total
Actual passengers (million)	**61.6**	**79.2**	**83.9**	**84.5**	***85.0***[13]	**394.1**
Delta Vs Airlines' H7 mid-scenario	n/a[14]	-2% (80.4)	+2% (82.0)	+1% (83.6)	0% (85.0)	-0.5% (396.0)
Delta Vs HAL mid-scenario		+19% (66.6)	+20% (69.8)	+15% (73.4)	+12% (75.6)	+14% (346.1)
Delta Vs CAA H7 FD mid-scenario		**+8% (73.0)**	**+6% (78.9)**	**+5% (80.7)**	**+5% (81.3)**	**+5% (375.5)**

Source: HAL Traffic Statistics[15], CAA H7 FD

5.5. In addition, the traffic under-forecasting in H7 has widened the level of under-forecasting observed since the Q6 price control, giving rise to continued windfall profits for HAL and the consumer consistently paying over the odds despite the introduction of the Traffic Risk Sharing (TRS) mechanism. The shock factor applied

[13] HAL forecast, 25 February 2026, https://mediacentre.heathrow.com/pressrelease/detail/24843. On 11 May 2026, HAL announced a reduction in passenger numbers for April 2026 vs April 2025 due to the impact of the 2026 Middle East conflict on some markets with a revised forecast for 2026 expected in June 2026. However, HAL expects this to be short-term disruption with underlying demand remaining strong and resilient, strong transfer passenger demand of +10% YoY in April 2026, and current fuel supplies stable.

[14] The CAA H7 FD was adopted in March 2023.

[15] https://www.heathrow.com/company/investor-centre/reports/traffic-statistics

by the CAA has further increased the level of under-forecasting and has therefore failed to deliver on its objective of improving the traffic forecast.

Skylark assessment of CAA's traffic forecast

5.6. The airline community has commissioned Skylark to assess the traffic forecast produced by Steer for the CAA and the CAA's overall approach to the traffic forecast. Skylark assessed the CAA's Initial Proposals, HAL's Business Plan and the airline forecast submitted as part of the Alternative Business Plan. Skylark assessed the following elements:

i. The inputs to Steer's traffic forecast model

ii. The rationale of the shock factor retained by the CAA

iii. The calculation to derive the shock factor figures.

5.7. We refer to Skylark's report for the detailed findings and provide an overview below.

Inputs to Steer's traffic forecast model

a. Passenger ATMs

5.8. Heathrow is constrained to cap of 480k annual Air Traffic Movements (ATMs). In 2025, the airport handled 477.9k ATMs, of which 475,6k were passenger ATMs. This builds on 471.3k passenger ATMs in 2024, which forms part of Steer's input. In comparison, Steer's model assumed 473.7k passenger ATMs for 2025 and 474.95k movements in 2031.

HAL's 2025 passenger ATMs

Heathrow Annual Report 2025

Other traffic performance indicators [1]	2025	2024	Var %[3]
Passenger ATM	475,596	471,298	0.9
Seat factor (%)	80.2	80.7	(0.5)
Seats per ATM	221.5	220.6	0.4
Cargo tonnage ('000) [2]	1,592	1,580	0.8

(1) For the year ended 31 December.
(2) Calculated using unrounded passenger figures
(3) Cargo tonnage includes mail volumes

Heathrow Annual Report 2024

Other traffic performance indicators[3]	2024	2023	Var %[4]
Passenger ATM	**471,298**	450,194	4.7
Seat factor (%)	**80.7**	79.6	1.4
Seats per ATM	**220.6**	221.0	(0.2)
Cargo tonnage ('000)[5]	**1,580**	1,431	10.4

Source: HAL annual reports 2024-2025

5.9. Skylark finds that due to the impact of the current US/Israel-Iran conflict, movements could decline in 2026. It projects 474k passenger ATMs for 2026, a

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-0.3% year-on-year change to 2025. However, Skylark recognises the impact could be transitory in line with HAL's latest expectations[16] and highlights Heathrow's resilient demand and hub model which saw a 10% increase in transfer passengers in April 2026.

5.10. Using Steer's passenger ATM forecast for 2026, Skylark proposes a recovery of passenger ATMs to the 2025 level by 2031 – i.e. 475.6k passenger ATMs. This assumption is conservative as, despite the transient nature of the conflict-induced shock, it assumes that several years are required to return to the 2025 level.

b. Average Aircraft Size

5.11. Skylark considers that Steer's base case assumption of growth in the average aircraft size from 222 to ca.231 in 2031 is reasonable. This increase in aircraft size reflects the upgauging of existing narrow-body aircraft operations to larger narrow-body and wide-body aircraft, the upgauging and new fleet orders for long-haul aircraft by Heathrow carriers, and the shift of short-haul slots to long-haul.

5.12. As the main carrier out of Heathrow, BA expects delivery of 12 long-haul aircraft to be delivered in 2027-2030 (Airbus A350-1000 and Boeing 777-9). IAG further ordered 32 Boeing 787-10 for delivery from 2028-2033.[17] [REDACTED].

5.13. However, within the assumption, Steer has assumed a broad decline in A380 usage in H8. Skylark stresses that this is a conservative assumption given airline use of the aircraft at Heathrow, such as the continued use and ongoing refurbishment by BA of its A380 fleet, as well as the recent reactivation of the aircraft by Singapore Airlines.

c. Seat Factor

5.14. In 2025, Heathrow had a seat factor of 80%. Skylark considers that there is reasonable opportunity for airlines at Heathrow to increase the seat factor in the medium-term, especially for European flights (76%), when compared to the higher seat factors of the long-haul regions (82%-89%). Heathrow's seat factor is low compared to benchmark major European hub airports (82%-84%), demonstrating the potential for further improvements. Skylark finds that, even with a focus on premium passengers, airlines will be expected to improve the ability to take more passengers within a slot constrained airport. Ongoing improvements in yield management and further advancement in Artificial Intelligence in the context of revenue management will also drive a step change in supporting the medium-term seat factor improvements.

5.15. For those reasons, Skylark finds that Steer's proposed seat factor growth (80% in 2025 to 81.5% in 2031 in the base case scenario) is conservative compared to the potential seat factor optimisation in the medium-term, which Skylark estimates at 83.3% by 2031.

[16] HAL forecast, 25 February 2026, https://mediacentre.heathrow.com/pressrelease/detail/24843.
[17] See IAG Q1 results, May 2025, https://www.iairgroup.com/media/daslsesb/interim-management-statement-for-the-three-months-to-31-march-2025.pdf.

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d. Skylark's proposed adjustments to Steer's model

5.16. Based on the combined adjustments of passenger ATM, optimised seat factor and increased aircraft size, Skylark estimates that 2031 passengers will reach 92.2 million, 2.3% higher than Steer's forecast of 90.2 million passengers. Skylark's estimate is in line with Steer's unconstrained forecast which shows continued high growth of demand for Heathrow, with 99.1 million passengers by 2031. The main adjustments are to the seat factor. Total passengers over H8 estimated by Skylark are 447.6 million. We employ Skylark's forecast in our BA proposed price cap detailed in our response.

5.17. We summarise the results of Skylark's adjustments to the unshocked passenger forecast, and compare them against Steer's analysis, HAL's H8 Business Plan and the airline Alternative Business Plan below.

In 2031 (unshocked)	Steer base case	HAL H8 BP base	Airline ABP	**Skylark (May 2026)**
ATMs	475.0	473.9	474.0	**475.6**
Aircraft size (seats)	232.8	234.1	227.8	**233.1**
Seat Factor (%)	81.5%	81.2%	84.7%	**83.3%**
2031 pax	90.2m	90.0m	91.4m	**92.2m**
H8 pax	442.0m	439.6m	446.0m	**447.6m**

Shock factor

a. Skylark's assessment of the rationale for the shock factor: the shock factor has not delivered on its intended objective and should not be used to set the basis for the TRS mechanism

5.18. The CAA's states in the IPs that the rationale for the shock factor is to "*improve the accuracy of the [traffic] forecast*" by reflecting "*the risks of shocks within the regulatory period resulting from asymmetric non-economic downside risks (such as adverse weather, volcanic eruptions, terrorist events and international conflicts), that lead to acute falls in passenger numbers which are difficult to predict*" [18].

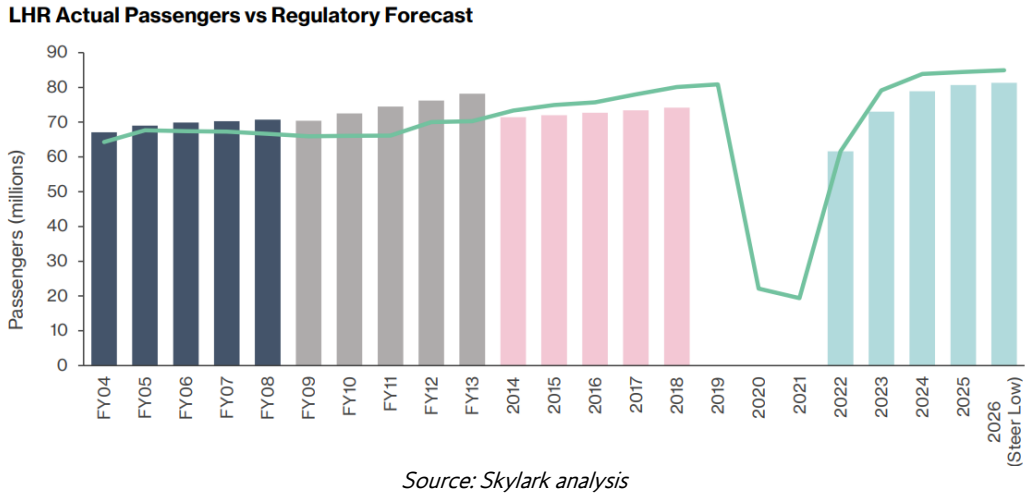
[18] See H8 Initial Proposals, paragraph 2.23.

5.19. Indeed, in its H7 review of CAA's proposed Traffic Risk Sharing (TRS) mechanism for the CAA, Deloitte highlighted that "*the purpose of applying the shock factor to the passenger forecasts is so that the forecast more accurately reflects the expected number of passengers, rather than a mechanism to compensate HAL for asymmetric risk*" and that, on that premise, it would appear "*reasonable for the TRS mechanism's baseline to be based on the passenger forecasts after they have been adjusted by the shock factor*".[19]

5.20. However, the CAA has not asked Steer to verify whether the shock factor has delivered on its objective of improving the accuracy of the forecast. We consider that the shock factor has not delivered on its intended objective. The CAA ought to revisit regulatory policy to assess if it has delivered on its objectives.

5.21. In fact, Skylark has found that the application of the shock factor in the most recent regulatory periods has widened the under-forecasting of traffic, by around 5% in Q6 (2014-2018) and H7 (2022-2026). The shock factor estimates 15 million lost passengers over the past 30 years, in addition to historical under-forecasting of traffic that has harmed consumers and yielded ongoing windfall profits for HAL. This evidence alone should warrant the CAA reassessing whether the shock factor is working and whether it ought to be revisited and removed.

Heathrow actual passengers vs Regulatory Forecast 2004-2026



Source: Skylark analysis

5.22. Skylark also finds that it is unreasonable for the TRS mechanism to be based on a shocked passenger forecast instead of the unshocked forecast. Skylark has not seen a direct interlink between the assumed shock factor and the TRS mechanism, except for using the shocked passenger forecast as the baseline for the TRS. In fact, we consider that there is a high likelihood that the shock factor and TRS mechanism are likely to overlap. The CAA appears to recognise that overlap in its Initial Proposals:

> "*Business-as-usual traffic shock events are already catered for through existing traffic risk policies such as the "shock factor" adjustment in our traffic forecast for the H8 Period [.] Reducing the outer band [for the TRS] to 5%*

[19] Deloitte Review of the CAA's proposed traffic risk sharing (TRS) mechanism (23 June 2022)

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could risk the TRS overlapping with existing traffic policies designed to deal with less extreme traffic deviations".[20]

5.23. In view of the shock factor failing to have delivered on its intended objective, the apparent overlap with other traffic protections, notably the TRS, and the unreasonableness of using a shocked forecast as the basis for the TRS mechanism, we ask for the shock factor to be withdrawn for H8. Regulatory policy ought to be periodically reviewed for effectiveness, accuracy and regulatory certainty, and reconsidered if those objectives have not been delivered.

b. Skylark's findings on the calculation of the shock factor

5.24. In addition, and without prejudice to our request to the CAA to withdraw the shock factor, we believe the calculation of the shock factor requires revision for H8 to account for errors, the inclusion of economic shocks and reflect the improvements in industry resilience over the decades.

5.25. The CAA has stated that the shock factor was designed to reflect the possibility of non-economic shock events. However, it has also concluded in the H7 remittals that Desert Storm in 1991 does not constitute an event of this definition as it was "contaminated" by an economic downturn with a fall in UK GDP.[21] Skylark therefore proposes to review the shock factor to exclude this event. Skylark proposes assuming a fixed 30-year period, moving the period of the shock event analysis beyond 1991, with 1992-2019 and 2024-2025 being the latest 30-year period.

5.26. Alternatively, if Desert Storm is retained in the shock factor estimation, Skylark proposes adjusting its impact to reflect the overlap of the economic and non-economic shock event. This could be done based on assumed counterfactual traffic growth driven by GDP elasticity (assumed at 1.5x) and the implied unshocked passengers that were being assumed by HAL (+3.5 million passengers). The high-level analysis shows that the impact, excluding the overall economic GDP decline, is -3% against the -8% assumed within the shock calculation. This in turn reduces the shock factor from -0.84% to -0.7%, having a material impact on the forecast and charges.

5.27. The inclusion of further shock events is also unclear. As an example, HAL identified a "shock event" of the 2016 EU referendum that was assumed to have occurred between August 2016 and October 2016, with an impact of ca. -0.3 million passengers. It is not clear what is the rationale for the "shock event" associated with the EU referendum vote, which occurred in June 2016. The outturn traffic for 2016 of 75.7m passengers was effectively 2 million higher than the Q6 forecast of 72.7 million passengers (shocked). This event ought to be removed from the calculation.

5.28. Moreover, Skylark proposes applying a straight-line weighting curve recognising the ongoing improvement in airline industry resilience since early 1990s through risk management, mitigation and efficiencies. The curve applies as a straight-line from a

[20] See IPs, paragraph 10.93.
[21] See CAP3001, paragraphs 3.18-3.19.

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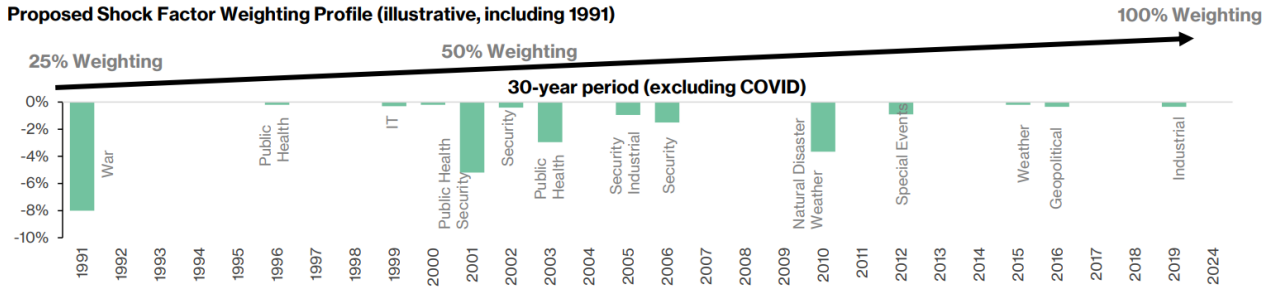
notional 25% at the start of the 30-year period to 100% at the end of the shock-period. This reflects that mitigation and traffic resilience are twice better than they were 20 years ago. Applying the proposed weighting to the original shock event profile could reduce the shock factor to c. -0.4%.

Skylark's proposed shock factor weighting profile reflecting industry improvements



Source: Skylark analysis

c. Skylark's proposals are a materially better alternative to the CAA's existing approach

5.29. BA strongly considers that Skylark's proposals provide a materially better alternative to the CAA's existing approach to improve the accuracy the traffic forecast and avoid ongoing under-forecasting at the detriment of the consumer. The CAA must duly justify how it has assessed those views for its Final Proposals, provide sufficient reasons for a possible rejection, and set out how it will improve the accuracy of its forecast.

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6. Operating expenditure

BA strongly supports the CAA's base-step-trend framework for assessing opex, including the use of bottom-up analysis as its main form of analysis and the top-down benchmarking as a cross-check. We firmly support the rigorous application of the need, additionality and efficiency tests which resulted in the rejection of most of HAL's requested overlays. These represent **a clear improvement on previous price controls** and deliver on the CAA's H8 commitments.

However, **persistent deficiencies in HAL's transparency, information quality and engagement** – recognised by the CAA in its assessment of the Business Plan as "low quality" and by its consultants – have materially constrained effective scrutiny and forced reliance on assumptions that likely understate inefficiency. Indeed, at several points where the CAA's evidence permitted a stronger challenge, **the CAA has adopted the more cautious target (or did not adopt efficiencies in certain areas)**, with the cumulative effect being an opex allowance that is materially too generous. These include critical areas such as security, staff costs and major operating cost lines. Importantly**, Heathrow is ranked near the bottom of a 43-airport comparator set**, multiple independent lines of bottom-up evidence confirm the scale of its inefficiency, and yet the resulting catch-up adjustment is 4%. That outcome is not consistent with the weight of evidence the CAA itself has assembled. Similarly, **the CAA has also not applied an efficiency target on other operating costs that cumulatively amount to more than £310 million**.

Without a materially strengthened efficiency challenge, the removal of one-off and unsupported costs and tighter safeguards on late submissions by HAL, the cumulative effect would be an opex allowance that is materially too generous and does not reflect an efficient level of costs for Heathrow, to the detriment of consumers.

Our recommendation is for a revised opex allowance of £7,480 million, which is £309 million lower than the CAA's proposal (2024 CPIH).

We are **concerned regarding the potential acceptance of substantive new information from HAL after the conclusion of CE**, such as on reviving the rejected overlays, which would undermine the integrity of the process, bypass structured scrutiny, risk perverse incentives and regulatory gaming, and risk reintroducing allowances previously rejected due to insufficient evidence. This would be at the detriment of the consumer. We therefore consider that **a very high bar must apply to any late submissions**, limited to narrow clarifications with clear consumer benefit that the airlines can test meaningfully and respond to.

Support for the CAA's overall approach

6.1. We strongly support the CAA's overall approach of estimating opex using the base-trend-step approach. The CAA is equally right in applying the need, additionality and efficiency tests rigorously to reject unsupported cost additions. The CAA's approach aligns with the approach employed in the CEPA report on opex submitted by the airline community alongside its Alternative Business Plan in October 2025.

6.2. In particular, we welcome the CAA's proposal to use a systematic bottom-up analysis as a tool for assessing inefficiency for the baseline year, while using a top-

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down econometric benchmarking to cross check the results. We equally strongly support the CAA's clear approach to overlays. These are aligned with the CAA's commitment in the H8 Method Statement to strengthen the evidence base for opex, the outcomes of the CAA's H7 Lessons Learned exercise, and deliver a marked improvement on previous price controls.

6.3. However, we note that at several points where the CAA's evidence permitted a stronger challenge, the CAA has adopted the more cautious approach of the available positions (or did not apply an efficiency challenge, such as on other opex), and the cumulative effect is an opex allowance that is materially too generous by more than £300 million.

HAL's lack of transparency

6.4. We further note the lack of transparency by HAL both during Constructive Engagement and in its Business Plan on critical issues concerning its operating cost proposals. The airline community wrote to the CAA on several occasions regarding those issues[22] and set them out in its Alternative Business Plan. These included HAL's refusal to provide a bottom-up approach to opex and commercial revenues forecasting, a lack of transparency in its underlying calculations, lack of evidence on overlays and delays in responding to information requests. This has precluded our effective participation in Constructive Engagement to interrogate whether HAL's proposed allowances represent efficient costs for the consumer.

6.5. The CAA has recognised those issues in its assessment of HAL's Business Plan under the Business Plan Incentive (BPI), noting that HAL did not provide the required granularity on opex mandated by the CAA's Business Plan guidance. The CAA has equally found that the lack of a "golden thread" did not provide a consistent clear link between HAL's consumer research, proposed outcomes, capital investment, opex and commercial revenues which made it difficult to assess efficiency and value for money.

6.6. Similarly, in the bottom up analysis, the CAA consultants EE/YA repeatedly highlight that HAL did not provide them with the requested information to enable them to carry out their analysis. This has led to EE/YA making certain assumptions which in our view have led to an underestimation of the level of inefficiency at HAL. It is important that the CAA addresses this issue ahead of Final Proposals as well as future price controls.

6.7. We agree with CAA's and its consultants' assessment on the low quality of opex information provided by HAL and stress that HAL should not be allowed to benefit from its own information asymmetries in the opex allowances. As noted above, we have strong concerns regarding the potential acceptance of substantive new information from HAL after the conclusion of Constructive Engagement, which would undermine the integrity of the process, bypass structured scrutiny, risk perverse incentives and regulatory gaming, and risk reintroducing allowances previously rejected due to insufficient evidence. This would be at the detriment of

[22] See for example, letter of 13 October 2025 from the airline community to the CAA.

the consumer. We therefore consider that a very high bar must apply to any late submissions, limited to narrow clarifications with clear consumer benefit that the airlines can test meaningfully and respond to.

Base step trend approach

6.8. The CAA has used a base-trend-step approach for the calculation of opex by:

i. Setting an efficient baseline

ii. Rolling forward the baseline, and

iii. Assessing and adding overlays.

6.9. The CAA has also used a bespoke methodology for forecasting Business Rates and pension deficit recovery costs.

6.10. Based on this approach, the CAA has included in its Initial Proposals a total opex of £7,862m (2024 CPI) or £7,790 (2024 CPIH) for H8.

6.11. While we are strongly supportive of the methodology, in this section we provide views on the CAA's analysis and decisions underpinning the application of this methodology, including where the CAA could have adopted stronger targets based on the available evidence. We request the CAA to consider and implement these views ahead of its Final Proposals.

Setting the efficient baseline – Baseline year

6.12. We strongly support the CAA's rejection of HAL's proposal that its 2024 baseline is efficient. The evidence that Heathrow's costs are materially above an efficient level is not in serious dispute. This was made evident in HAL's own top down benchmark analysis conducted by KMPG. In its analysis for the airlines' ABP, CEPA analysed the KPMG model and identified that the model results an inefficiency between 6% and 13%.

6.13. We note that the CAA has requested EE/YA to carry out a separate top-down model, using data from the Jacobs. Airport Performance Indicators dataset. The CAA concludes that HAL is ranked 39th out of 43 airports in 2019 and 40th out of 43 in 2022. In other words, HAL is close to the worst performers in the sample.

6.14. However, despite this evidence, CAA indicates an efficiency gap between HAL and the frontier of just 4%. Such a small gap appears inconsistent with HAL's ranking among the worst performing airports of the sample.

6.15. Having reviewed the CAA's calculations, it appears that the reported percentage gap (4%) has been expressed as the ratio involving logged differences rather than as a percentage difference in cost levels, which may understate the true implied gap once fitted log costs are converted back into cost levels.

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6.16. Given that the CAA can now have at its disposal Jacobs data for 2023, we recommend that it updates its top-down benchmark and calculate the efficiency gap by presenting it as the difference in cost levels (rather than logged differences). Based on our calculations the efficiency gap appears to be more likely between [REDACTED].

6.17. It is important to highlight that the top-down model should only be used as a cross check. Although the efficiency gap suggested by the top-down benchmark may be significantly higher once the correction highlighted above is made, we believe that the bottom-up analysis already provides ample evidence that the efficiency challenge should be much higher than the one proposed by the CAA. The recalculated top-down gap will provide additional reassurance.

Setting the efficient baseline – Scope adjustments

6.18. We note that the CAA removes related costs for the Pod service from the baseline, as this activity is deemed "off-RAB". The CAA assumed Pod costs to be £2.7 million (2024 CPI). We agree with the removal of the amount being proposed by the CAA. However, we highlight our concerns on the corresponding commercial revenues assumed for Pod parking for the scope adjustments in the CAA's commercial revenue calculations (which we address in the commercial revenue section of our response).

6.19. We also note that while HAL proposed to move noise and vortex costs to capex, the CAA considers that it is better to treat it as an opex item and is currently consulting stakeholders on the matter.

6.20. In this regard, we support the CAA's proposals of treating these costs as opex throughout H8. However, we highlight the following concerns that would have to be addressed:

i. Since opex outperformance would be retained by HAL, it is important to ensure that this is not achieved by "cutting corners". It is therefore important that the noise and vortex opex allowance is directly linked with expected outcomes (e.g. number of properties to be insulated over the period) and that the CAA takes action if these expected outcomes are not delivered by the end of H8.

   We reject HAL's proposal to treat these costs as an Other Regulated Charge (ORC). As indicated in the ORC section of our response, the current low powered cost management incentives of the ORC scheme allow for the inefficient delivery of outcomes and an effective pass-through of costs.

ii. The CAA will need to be satisfied that the opex allowance is necessary for the delivery of the outcome committed above (i.e. HAL needs to justify why it needs c.£50 million over the period).

iii. The views expressed above are based on a two-runway H8 price control. It should not be assumed that our views will be the same when dealing with expansion related noise and vortex expenses.

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iv. The allowances made in the H8 determination should not be used in any expansion related activity.

A stronger challenge based on the CAA's available evidence

6.21. We are concerned that the CAA has applied a cautious approach despite evidence from its consultants suggesting pointing to stronger efficiency challenges, or did not apply any efficiency in certain areas, and that the cumulative effect is an opex allowance is materially too generous and not reflective of efficient costs.

6.22. Indeed, EE/YA's bottom-up analysis identifies evidence of inefficiency across several cost categories but consistently resolves uncertainty at the most cautious end of the available range. The result is a bottom-up assessment that materially understates the efficiency gap the evidence supports.

6.23. We describe below our views on the CAA's cost assessments, including its bottom-up analysis:

a. Security staff costs

6.24. We note that the CAA has carried out three main adjustments to the security staff baseline accounting for the effects of VCP outsourcing (£8.3 million), an efficiency adjustment (5%, equivalent to £9.4 million) and an additional efficiency component due to CTiX familiarity (3.2%, equivalent to £5.7 million).

6.25. We understand that the efficiency adjustments resulted from comparisons between HAL productivity estimates of the CTiX lanes against that achieved by other UK airports. Benchmarks of staff salaries across airports are subsequently factored in. Based on this analysis, the CAA estimates an inefficiency gap of 5%-10% and determines that a 5% adjustment to be applied to the baseline. There is a further 3.2% efficiency applied based on expectations from other airports.

6.26. However, there appears to be a material mismatch between these assumptions and the higher efficiency gains in HAL's Security Programme business case.

6.27. We reproduce below [REDACTED] the Security Programme H8 business case, which forecasts the opex savings achieved:

[REDACTED]

6.28. The opex effect in the table above is calculated against a 2019 baseline and therefore the effects of the Security Programme implementation for H8 need to be recalculated accordingly against a 2024 baseline year. Indeed, the comparison ought to be made between the start of the price control in 2027 (and onwards) against a 2024 baseline for H8. For instance, the opex expectation in 2027 is [REDACTED] against a 2019 baseline. However, as the comparison for 2027 needs to be made against 2024, this needs to factor in the [REDACTED] efficiency gap identified between 2019 and 2024. This in turn results in a higher efficiency gap between 2024 and 2027 of [REDACTED] which must be factored in at the start of H8.

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6.29. Moreover, the calculations above are only for [REDACTED] of the Programme. The business case also provides estimated savings from [REDACTED] of around [REDACTED] from 2030. These additional savings should also be taken into account[23].

6.30. The results of rebasing the numbers in the previous table to 2024 and adding the effects of Tranches 3 and 4 (using a mid-point efficiency gain of [REDACTED] in 2030) are shown below:

[REDACTED]

6.31. If we now compare efficiency assumptions in the business case against those that the CAA has included in its security staff cost analysis[24], a significant gap is demonstrated (as shown in the table below):

Comparison of security programme business case opex efficiency vs. CAA IP security efficiency assumptions (2024 baseline)

Opex efficiency vs. 2024 (£m, 2024 CPI)	2027	2028	2029	2030	2031	Total
Business Case	[…]	[…]	[…]	[…]	[…]	[…]
CAA Initial Proposals*	18.0	18.0	18.0	15.2	15.2	84.2
Difference	[…]	[…]	[…]	[…]	[…]	[…]

** CAA assumes baseline efficiency adjustment (£15.2m) + overlays for 2027-29 (£2.8m p.a.). Does not include elasticity effects.*

Source: HAL Business Plan, Security Programme Business Case, CAA IPs

6.32. Therefore, using HAL's own figures, the CAA should increase opex savings by at least [REDACTED] (2024 CPI).

6.33. We also have concerns on the rationale employed by EE/YA should recommend a lower efficiency target.

6.34. Firstly, EE/YA assume that there is no efficiency achieved from the processing improvements involved in changing from Advanced Threat Identification X-ray (ATiX) to next-generation 3D computed tomography X-Ray (CTiX) lanes. We are concerned that EE/YA deliberately ignore the improvement between ATiX and CTiX in security lanes, arguing that it is not relevant because CTiX would be fully installed [REDACTED], and therefore the end of H7[25]. This is wrong in our view, since 2024 is used to baseline costs that will be rolled forward and hence must factor in for those improvements expected by [REDACTED]. If the CAA does not take into account the efficiencies generated from the move of ATiX to CTiX, security staff

[23] HAL Security Programme Business Case, H8 Business Plan, […].

[24] We see that the business case includes opex changes not only on staff costs, but other opex lines. Since the EE/YA has only considered effects of the security programme only on staff costs, we compare the total opex effects of the business case vs. staff costs effects on IPs.

[25] "*Although the processing capability of conventional (ATix) lanes and CTix lanes differ, we have focussed on HAL's expected efficiency with its new CTix lanes as the appropriate efficiency measure. This implicitly assumes that HAL's relative efficiency or inefficiency will be the same across both types of lanes in the 2024 baseline. However, as we are focussed on assessing an efficient baseline for the purpose of H8, the processing capability of the conventional (ATix) lanes is not relevant to the roll forward of costs beyond 2025 as CTix will be fully installed by the end of H7*". EE/YA Opex/Commercial revenue report, page 92.

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costs will be overestimated by a significant amount and ignore the benefits brought in by the very sizeable Security Programme.

6.35. Secondly, EE/YA have not corrected for one-off costs incurred in the transition between the different types of lanes (costs that will be included in the 2024 and 2025 regulatory accounts). This is clear in the Business Case figures (e.g. [REDACTED]). This needs to be corrected for in the baseline as otherwise HAL would be unjustifiably allowed for costs in H8 that would not exist.

6.36. Thirdly, with regards to the 5% efficiency gap identified by EE/YA, we note that the consultants have consistently opted for the most cautious end of the relevant range. For example, we note that the consultants show that HAL could potentially be some 30% inefficient on its CTiX lanes based on the performance against a comparator but then opt to drop the comparator due to lack of information. Rather than dropping the airport altogether, the CAA could have attempted to collect such information from the specific UK airport, particularly when such a big inefficiency is being suggested.

i. Even after eliminating this comparator, EE/YA indicate that HAL would be at the lower end of the resulting range (0%-12%) because of HAL's nature of operations and service standards (e.g. security related MTIs). However, we have not seen a quantification of how these effects point to the bottom end of the range.

ii. Moreover, after establishing that HAL staff salaries could be between 4%-7% higher than comparators (after adjusting for regional differences), the consultants estimate an overall inefficiency range of 5%-10% (performance and salary costs) and choose the bottom end of the range as the efficiency gap to apply to the baseline.

iii. We believe that more evidence must be provided to justify reducing a potential inefficiency of more than 30% to a much lower gap of 5%. Based on the available evidence, we consider that the CAA may opt to move away from the bottom end of the range.

6.37. Finally, EE/YA took a very conservative approach in their efficiency resulting from increased experience in the usage of CTiX. While EE/YA indicate that the scope for additional efficiencies is between 8% and 36%, they only assume that only 40% of the lowest end of this range to be achievable by 2027 (8% x 40% = 3.2%) and then add an 1.6% overlay. There is no reasoning as to why the consultants opted for the lowest number in the range or why 40% of that lowest range is appropriate.

6.38. In conclusion, we believe that the combination of the factors described above would cumulatively lead to a much higher efficiency gain based on the available evidence from the CAA's consultants. We also urge the CAA to review its efficiency analysis of the effects of the Security Programme and make the necessary amendment in its Final Proposals. In the absence of those corrections, we are concerned that the cumulative effect is an opex allowance for security costs that is materially too generous and represents inefficient costs.

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6.39. For the elaboration of the BA estimated price cap, we have used the following assumptions based on HAL's business case:

BA adjustments to HAL baseline – security staff costs[26]

Opex - effects of Security programme (2024 CPI)	2024	2027	2028	2029	2030	2031
Adjustments to HAL Baseline (£m)	[...]					
Overlays (£m) – annual efficiency and effect of Tranches 1 to 4		[...]	[...]	[...]	[...]	[...]

Source: BA calculations, HAL security business case

6.40. The above translated into the following adjustments to the CAA IPs:

BA adjustments to CAA IP assumptions – security staff costs

	2024	2027	2028	2029	2030	2031
Adjustments to CAA "efficient" IP baseline (£m)	[...]					
Adjustments to CAA overlays		[...]	[...]	[...]	[...]	[...]

Source: BA calculations, HAL security business case, CAA IPs

6.41. We emphasise that there is more scope for efficiency than those highlighted in the table above. This is because a portion of the scope for efficiencies identified by EE/YA have not been picked up by the business case figures. In light of this, we request the CAA to consider a deep dive on security cost allowances for the Final Proposals.

b. Other staff costs

6.42. We observe that the CAA's consultants estimate that HAL's 2024 staff costs per passenger were almost 29% higher than the H7 determination (36% when adjusting for actual passengers), but then appear to dismiss much of the gap by stating that the CAA was too aggressive (even "relatively arbitrary") in its H7 assumptions. EE/YA opt to apply a 3.75% efficiency adjustment which is almost ten times lower.

6.43. The CAA must address the statement that it set its opex target for H7 in a "relatively arbitrary" way. No justification has been provided why the regulatory settlement for opex was wrong, and we note that the opex allowances were not appealed to the CMA in the H7 appeals. If the CAA decides that did not arbitrarily set opex, then the inefficiency gap must be factored into the proposals to a greater extent.

6.44. A 30% difference cannot be simply ignored. The CAA should verify why outturn costs did not turn out as expected. While the consultants have attempted to do this, it is necessary for the regulator to assess those costs to further understand what has driven those changes. We also note that the consultants have indicated that HAL provided limited information and therefore allowing HAL to benefit from its lack of transparency through higher allowances would, in our view, be inappropriate.

[26] The savings pertain mainly to staff costs but also impact other opex lines. For simplicity, we have added these to staff costs.

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6.45. The benchmark was carried out based on 2022 financial information, where passenger numbers were still well below 2019 figures at various airports. The CAA should update its analysis now that more recent information is available.

c. Facilities, Maintenance and Cleaning

6.46. While we acknowledge the 5% efficiency challenge applied, there a appears to be an inconsistency in the EE/YA analysis of cleaning costs. EE/YA acknowledge that terminal area is the main driver of cleaning costs but then carries out its benchmarking against other airports on a per passenger basis. A per passenger assessment will tend to benefit Heathrow as it is operating near capacity (so will appear be performing better against other airports that have a lower capacity utilisation). Even based on this assessment, unit costs still increased by 26% between 2019 and 2024.

6.47. We also note that the consultants refer to the increases in cleaning costs per passenger at Dublin airport to corroborate the increases at Heathrow. This ignores that the Irish Aviation Authority's consultants identified this as an area of inefficiency.[27]

6.48. Moreover, the data shown in the graphs for AdP appear to contain errors. It appears that the consultants may have used AdP's consolidated statements (which includes several international airports) but then used passenger numbers at Parisian airports as the denominator (instead of all consolidated airports). When using the annual accounts solely related to the Parisian airports, the unit cost is much lower than that shown in the EE/YA chart. Similarly, when compared to 2019 the unit costs (in 2024 French CPI prices) imply a real reduction of 6.3%[28]. This compares with the 26% increase at Heathrow suggesting a sizeable inefficiency for HAL.

6.49. In view of the above, we believe that the CAA must reconsider and increase the efficiency challenge allocated to this expense. Based on the EE/YA analysis, we propose to match the unit cleaning costs at Amsterdam Schiphol (£0.57), which represents a 9.5% efficiency challenge versus HAL's baseline.

d. Insurance

6.50. We believe that a one-off 30% increase in the baseline insurance costs does not reflect the current market trends. As previously indicated in CEPA's opex report produced for the Airline Business Plan, insurance rates have a downwards trend. This can be seen in the evolution of the March Global Insurance Market Index (as well as the UK-specific index) below.

[27] CEPA, Dublin Airport Operating Expenditure: Bottom-up Efficiency Assessment, Report for the Commission for Aviation Regulation / Irish Aviation Authority, 2022 (final report).
[28] Cleaning costs at AdP's Parisian airports: EUR 75m (2019) and EUR 79m (2024). Rebasing 2019 to 2024 French CPI prices: EUR 88m. Passenger numbers: 108m (2019) and 103m (2024). This leads to unit costs (in 2024 prices) of EUR 0.82 (2019) and EUR 0.76 (2024), which implies a real reduction of 6.3%.

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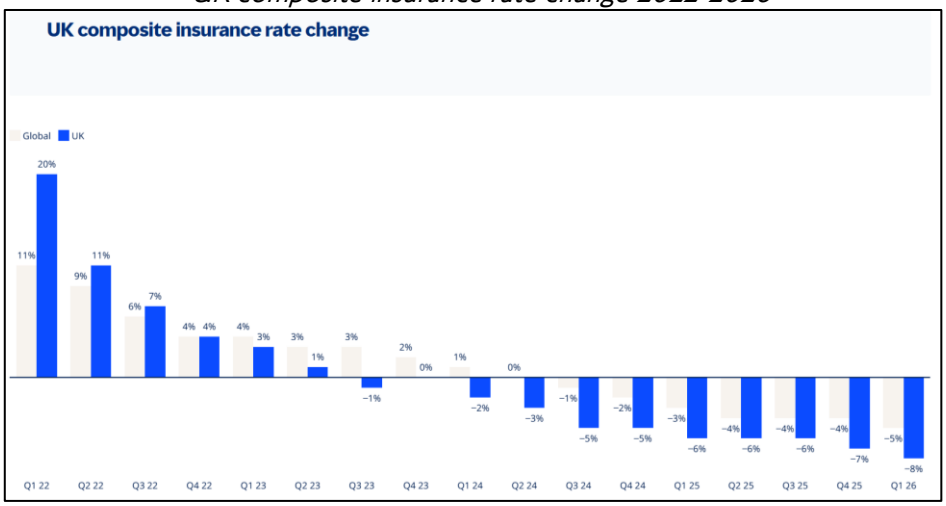
6.51. Based on current evidence, we believe a 30% uplift is not justified. In our view, insurance cost should fall, or at the most, be kept at 2024 outturn levels (i.e. no uplift).

UK composite insurance rate change 2022-2026



Source: Global Insurance Market Index (GIMI): Q1 2026 – UK rates decline for all major product lines[29]

e. Utilities

6.52. We support the CAA's efficiency challenges on electricity costs due difference in market prices and the price being paid by HAL.

6.53. In its 2025 sustainability report, HAL reports a significant reduction in energy consumed related to "Fuel consumption utilities" of about 100 GWh between 2024 and 2025.

Extract from HAL 2025 Sustainability Report "Calculating our footprint" section

Energy		Energy (MWh)			
		2019	2023	2024	2025
	Fuel consumption utilities	134,289	176,633	230,790	104,366
Scope 1	Operational vehicles and equipment	6,732	4,988	4,806	4,895
	LPG for fire training	5	3	-	4
Scope 2	Grid electricity consumption	283,229	271,080	272,103	273,266

Source: HAL Sustainability report 2025, page 97

6.54. We do not know what the driver of the reduction is. It could be, among other things, due to reduced consumption or the replacement of polluting energy to energy generated from renewable sources. If the reduction is from lower consumption or due to usage of more renewable energy generated at HAL (e.g. the ongoing installation of solar panels[30]), then this could reduce HAL's utilities over H8. In any case, we believe it would be prudent for the CAA to analyse the cause of this reduction and amend the H8 forecasts as needed.

[29] https://www.marsh.com/en/services/international-placement-services/insights/uk-insurance-rates.html
[30] Page of the 27 mentions the installation of photovoltaic panels in 2025 (with more planned in 2026).

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6.55. In the same report, HAL states its intention to implement energy efficiency initiatives. As an example, it mentions the initiative to replace motors of conveyor belts with models that reduce energy use, generating some £2 million annual in reduced consumption. Given that the CAA is not assuming a "frontier shift" in electricity, it may need to add these initiatives as overlays that reduce operating costs over H8 (or, alternatively, assume a frontier shift).

f. Electricity Distribution Contract

6.56. We consider that it would not be prudent for the CAA to simply allow for an RPI adjustment to the costs associated to the Electricity Distribution Contract. It appears that the CAA is allowing an RPI adjustment because HAL indicates that this is a clause in the contract. However, as highlighted by CEPA in its opex report for the airline Alternative Business Plan, the historic evolution of these costs is not consistent with an RPI-adjusted contract. In fact, these costs have decreased in real terms over the past years (in RPI terms). Therefore, we believe that H8 costs for the Electricity Distribution Contract should be indexed by CPI, rather than RPI. We request the CAA to review the contract and reassess its H8 allowance for these costs.

g. Other Operating Costs

6.57. The CAA uses an "Other Operating Cost" baseline of £566 million which it then adjusts to £554 million as the efficient baseline. The adjustments include:

i. Adjustments for outsourcing (VCP, trolley): +£9 million.

ii. Adjustments for scope (Pod costs): -£0.5 million.

iii. Efficiency assumptions (PRM costs and IT): -£13 million and -£8 million respectively.

6.58. There is no other adjustment to the baseline besides those highlighted above. However, we believe that further efficiency adjustments are warranted.

6.59. For example, the Other Operating Cost category includes £15 million of **MTI-related costs** that should be removed from the baseline (i.e. baseline costs should be reduced by £15 million). HAL's regulatory accounts indicate that the £15 million figure is a combination of the cash rebates (£2.5 million) and provisions (c. £12 million)[31]. This confirms that these are one-off expenses related to MTIs.

6.60. The inclusion of MTI costs in the baseline goes against the principle that consumers should not be paying for expenses linked to lack of service quality. This is in addition to the fact that it is a one-off cost. Keeping these costs in the baseline implies that

[31] "*Specific provisions of £12 million are included in the accounts in 2024 as the outcome of Heathrow's alleviation requests were pending. These provisions are driven by 2 failures against our MTI targets. One failure occurred in relation to a Security evacuation of Terminal 2 in July 2024 triggered by an unattended suspicious bag (£0.8m). The second one is linked to a reporting error affecting Campus Security (Control Post 12) during the Q6 to H7 transition (£11.2m). Heathrow and the airline community are working together to resolve these divergences of view.*"

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HAL would be allowed £15 million per year during H8 for costs that do not exist. We therefore request the CAA to exclude these costs from the baseline.

6.61. We also note that EE/YA propose a 20% reduction on PRM baseline costs on the basis of HAL's forecast reduction of these costs in 2031. We consider that the reduction in 2031 constitutes an indication that PRM costs are currently inefficient and therefore an efficiency challenge should be included in the baseline.

6.62. HAL has recently awarded a multiyear PRM contract. While it is possible that inefficiency is built in the contract (as users have not been able to participate in the process), PRM costs are recovered through Other Regulated Charges (ORCs) and, under current governance arrangements, challenges on efficiency are practically unenforceable (we explain more on those low-powered incentives in the ORC chapter of our response). Any such efficiency challenge should therefore be factored in under the high powered efficiency incentives of the opex allowance set at the start of the price control. It is equally important for the CAA to review the contract to determine whether the forecast overlays are justified.

6.63. We support the efficiency challenge set for IT expenses.

6.64. We note an expense line called "General Expense, Consultancy, Advertising, and marketing" which amounted £75 million in 2024, which EE/YA have not addressed. Similarly, there are various other elements with significant costs attached, such as rail[32] (£46 million), Other operational costs (£40 million), car parks (£36 million), Contingency planning (£31 million), Heathrow consolidation Centre (£26 million), Intra group (£20 million), Heathrow helpers (£19 million), Bussing (£11 million) and rent (£9 million) that have not been subject to a bottom up or external benchmarking analysis. Because of this, no efficiency assumptions are made for those costs[33].

6.65. Making no adjustment to any of above costs, which cumulatively amount to more than £312 million, risks implying that those costs are efficient. Given that the CAA has identified inefficiencies in the opex costs subject to bottom-up analysis, it is reasonable to expect that elements of inefficiency are also present in the remaining costs. This would also be supported by the top-down econometric analysis demonstrating significant inefficiency for HAL against other airports.

6.66. We see that the CAA has identified an efficiency challenge for the entire opex of 4%. This increases to 5.4% when the opex expenses highlighted above are excluded. This efficiency gap further increases 9.1% when taking into account the airline challenges highlighted so far in this submission.

6.67. While acknowledging the specific nature of some of the efficiency challenges, we consider appropriate to assume a 5% baseline efficiency challenge for the costs detailed in paragraph 6.64.

[32] EE/YA analysed Rail revenues, not costs. The only comment it provided with regards to costs is that these were increasing, whereas revenues were decreasing.
[33] MTI costs (£15m) are also part of this cost category. However, this cost line been dealt with separately in our submission, as we argue that this cost should be removed in its totality due to its inadmissibility.

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6.68. Finally, we note that the EE/YA report does not assume an efficiency challenge for Air Navigation Services despite its cost being higher than its benchmarks due to the perceived historical differences in regional staff costs. However, we note that EE/YA requested access to the contract but that was rejected, which has prevented the CAA's consultants from verifying that assumption or assessing any efficiency performance clauses between HAL and its third party supplier. Airlines also asked access to the contract during the Constructive Engagement process which HAL did not effectively respond to. Not having access to the contract limits the ability for users to properly scrutinise the baseline and forecast costs. For the purpose of the calculations of the BA proposed price cap, we will assume that these costs are subject to the same efficiency challenge of 5% as the "Other costs" identified in paragraph 6.64.

Rolling forward the efficient baseline

6.69. In general, we are in broad agreement with the elasticities and frontier efficiency adjustments being proposed, with the exception of the Electricity Distribution Contract (for which we propose a move from RPI to CPI indexation above).

Overlays

a. Technology, resilience and digital

6.70. We strongly support the CAA's rejection of HAL's proposed overlays on Technology, resilience and digital investment since there is no justified case for incurring such additional costs. This is in line with the recommendations of CEPA's opex report HAL's submitted with the airline Alternative Business Plan. The CAA's rejection of the majority of HAL's technology, resilience and digital overlays is one of the strongest elements of the Initial Proposals, and BA strongly supports it. Despite HAL's proposed overlays being large, the quality of evidence submitted to justify the overlays was poor. The CAA was right to apply the need, additionality and efficiency tests rigorously, and it should maintain that rigour at Final Proposals.

6.71. HAL is expected to seek to revive some or all these overlays through representations or additional evidence. The Business Plan Incentive (BPI) framework exists in part to address this situation. The CAA assessed HAL's business plan as "low quality", meeting only three of seven criteria. A business plan that fails the CAA's own quality test should not be capable of being repaired through late submissions. The CAA should make clear that its assessment of the BPI will take into account whether HAL attempts to remedy known deficiencies in its business plan through late evidence, and that such evidence will not be accorded the same weight.

6.72. Indeed, we have strong concerns regarding the potential acceptance of substantive new information from HAL after the conclusion of Constructive Engagement, which would undermine the integrity of the process, bypass structured scrutiny, risk perverse incentives and regulatory gaming, and risk reintroducing allowances previously rejected due to insufficient evidence. This would be at the detriment of the consumer. We therefore consider that a very high bar must apply to any late submissions, limited to narrow clarifications with clear consumer benefit that the

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airlines can test meaningfully and respond to. We refer to our positions and safeguards for the H8 process above and our response on the BPI.

b. MSCP4

6.73. We note that the CAA has accepted HAL's requested additional opex overlay of £25 million for the costs related to the closure of the MSCP4 short-stay car park, with a slight adjustment in relation to efficiency challenge on PRM costs. In this regard, we believe that a further adjustment would need to be made.

6.74. While HAL is currently spending opex to operate the car park (e.g. maintenance, cleaning, electricity, etc), such costs will cease once the car park is closed. This reduction in costs has not been accounted for and must be incorporated in the forecasts. A properly calculated overlay should reflect the net additional cost to HAL of the transitional period, not the gross additional expenditure without accounting for the costs that will simultaneously fall away.

6.75. As well, it is expected that the project will deliver opex efficiencies, as highlighted in HAL's business case: "[REDACTED]"[34]. While we understand that these efficiencies may be difficult to quantify, it seems inappropriate to include the additional costs in H8 but not net them off the potential efficiencies achieved.

6.76. Based on the above, we request that the CAA:

i. Remove opex that will not be spent because of the closure of the car park in 2027-2029, and

ii. Incorporate any expected savings once the car park opens in 2030 and 2031.

c. Security

6.77. We support the inclusion of security overlays. As highlighted in the earlier in the section of security staff costs, the savings identified in HAL's Security Programme business case must be factored in. We request the CAA to update the overlays on the basis of our proposals.

Bespoke assessments – Business Rates

6.78. We understand that the CAA has accepted HAL's updated forecast for Business Rates for H8 (£1,071 million) and adjusted it downwards by £104 million (2024 CPI) for the unutilised H7 logged-up allowances from the H7 remittals. These are very significant amounts having a material impact on the level of the charge.

6.79. Unfortunately, despite repeated requests by airlines during CE, HAL has not explained how it is effectively managing its Business Rates liability, including how has engaged in its negotiations with the Valuations Office Agency (VOA) in its most recent re-evaluation that became effective in April 2026. There is no evidence in the

[34] HAL BP Business case [REDACTED] (Terminal 4 Front Door and Car Park), [REDACTED].

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Initial Proposals that HAL has engaged seriously with the VOA to challenge or moderate its assessment. [REDACTED][35].

6.80. A robust negotiation matters because the VOA has no incentive to volunteer that its own valuations are too high. The absence of a challenge to the VOA's assessment is not evidence that HAL has negotiated to the best of its ability; it is simply the expected outcome when the assessed party has not pushed back. HAL, unlike an unregulated business, does not bear its own rates liability: the cost falls on airlines and passengers regardless of how actively HAL manages it. That misalignment means the regulatory framework needs to make HAL's engagement obligation explicit. HAL should be required to demonstrate serious and substantive engagement with the VOA on its assessment. HAL should report to airlines on what engagement has been undertaken, what has been achieved, and what further activity is planned.

6.81. Similarly, the CAA must be satisfied that HAL has demonstrated its best efforts before allowing such costs and set out the evidence for its assessment.

6.82. The upcoming 2029 revaluation creates a specific and foreseeable risk within the H8 period. Given the trajectory of airport rateable values at recent revaluations, the direction is expected to be upward. Our position is that any increase arising from the 2029 revaluation should only be recoverable in full if HAL can demonstrate that it engaged seriously with the revaluation process before the assessment was set. Where HAL cannot make that demonstration, it should absorb a proportion of the increase rather than passing it through unconditionally. The CAA should set out this expectation clearly at Final Proposals so that HAL has the incentive and the time to act accordingly.

6.83. Separately, we have identified an issue in how the business rate increases are being recovered. Currently, the CAA is assuming that these would be recovered through aeronautical charges. However, there are several commercial activities within the airport that would need to pay their fair share of those costs (as they do not pay business rates, but instead they are embedded within HAL's business rate bill, which is then passed on to them through rentals). We discuss this in more detail in the commercial revenues section of our response.

Bespoke assessments – Capitalisation of "Rents and Rates" costs

6.84. We note that the CAA has set the baseline and rolled-forward operating costs net of costs capitalised. This is appropriate since capitalised costs would form part of capex and therefore eliminating them from opex would avoid double counting for the same costs.

6.85. However, we note that this must hold true for all costs that have been subject to the base-trend-step approach. We are less clear if the CAA has done the same for rates.

6.86. In its Business Plan appendices, HAL reports a "*Rents and Rates*" cost category of [REDACTED] for 2024. This is then broken down into Business Rates

[35] [REDACTED]

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([REDACTED]) and "*Capitalised rent and rates costs deduction (if/when applicable)*" ([REDACTED]). It should be noted that, based on HAL's own tables, the airport has had such capitalisations since at least 2015 [36]

6.87. While the CAA has conducted a bespoke forecast for H8 Business Rates, it is less clear if it has included a capitalisation figure in its forecasts. It is possible that HAL's operating costs have been overestimated by at least [REDACTED] over the period. We request the CAA to review and make the necessary amendments so that the consumer does not overpay.

Opex – Summary and our recommendations

6.88. Based on our analysis above, we recommend that the CAA:

i. Maintain the base-step-trend methodology, including the use of bottom-up analysis to set the baseline and top-down econometric benchmarking as a cross-check.

ii. Apply a stronger overall efficiency challenge to opex, reflecting the full extent of inefficiency evidenced in both bottom-up analysis and benchmarking.

iii. Update the top-down econometric assessment using latest available data and express the efficiency gap in cost levels rather than logged differences.

iv. Ensure that HAL does not benefit from information asymmetries by placing the burden of proof on HAL where data is missing or incomplete.

v. Apply a very high bar to any late submissions from HAL, including on any attempts to revive the CAA's rejections of most overlays, limited to narrow clarifications with clear consumer benefit that can be properly tested by airlines.

vi. Increase the efficiency challenge applied to security costs, taking account of the efficiency gains set out in HAL's Security Programme business case and correcting overly cautious assumptions not supported by EE/YA's evidence.

vii. Remove one-off and transitional costs from the baseline, including inefficiencies during the CTiX transition and MTI-related costs that do not persist into H8.

viii. Reassess efficiency assumptions for other staff costs in light of the gap to H7 determinations and the lack of supporting evidence for dismissing that gap.

ix. Increase the efficiency challenge applied to facilities, maintenance and cleaning costs based on corrected comparator data and appropriate benchmarking metrics.

[36] HAL Business Plan Appendix A8 – Supporting Spreadsheets, Filename "H8 Opex and Revenue Data Tables", worksheet "Opex", row 39 contains the evolution of this account since 2015 (cell X39 contains the value for 2024: [REDACTED]).

x. Eliminate the 30% uplift to insurance costs and align allowances with observed market trends.

xi. Review utilities forecasts to reflect reductions in consumption and the impact of energy efficiency initiatives, including incorporation of associated savings.

xii. Change the inflation index for the Electricity Distribution Contract from RPI to CPI and reassess allowances based on actual historic trends.

xiii. Apply an efficiency challenge to operating cost lines that have not been subject to bottom-up analysis, reflecting inefficiency observed elsewhere.

xiv. Remove £15 million of MTI-related costs from the baseline and ensure users are not charged for penalties arising from service failure otherwise HAL would inappropriately be granted opex during H8 for a cost that does not exist.

xv. Maintain the CAA's rejection of unsupported overlays, particularly in technology, resilience and digital, and ensure that any reassessment adheres strictly to the need, additionality and efficiency tests.

xvi. Adjust the MSCP4 overlay to reflect net costs by removing opex that will cease following closure and incorporating expected efficiency savings.

xvii. Ensure that noise and vortex costs remain within opex and are linked to clearly defined output delivery, with safeguards against under-delivery.

xviii. Strengthen requirements on HAL to demonstrate robust engagement with the VOA on business rates, including ahead of the 2029 revaluation.

xix. Review the treatment of capitalised rents and rates to ensure no double counting and avoid over-recovery in opex allowances.

6.89. Based on our analysis, the implementation of the above should lead to the following opex changes:

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Summary of recommended changes to operating costs vs. CAA IPs

Opex Recommended changes (vs. IPs)	CPI 2024 £m	2024	2027	2028	2029	2030	2031	Total over H8 [37]
MTI rebate	Baseline	-15.0						-75.2
Insurance	Baseline	-5.9						-29.6
Distribution contract	RPE	CPI	-1.0	-1.3	-1.6	-1.7	-1.8	-7.5
Security programme (staff costs & opex)	Baseline	[...]						[...]
Security programme (staff costs & opex)	Overlay		[...]	[...]	[...]	[...]	[...]	[...]
Facilities/Maintenance	Baseline	-2.4						-11.9
Other Opex (excluding IT, PRM)	Baseline	-17.9						-89.5
Other Opex (Capitalized rents)	Baseline	[...]						[...]
Source: BA calculations								[...]

6.90. Applying the above changes to the CAA's opex and commercial revenues model, and after adjusting for volume and price effects, our recommendation is for a revised opex allowance of £7,549 million, representing an additional efficiency of £312 million compared to the CAA's forecast (2024 CPI). We subsequently rebase to 2024 CPIH, which revises our proposed opex allowance to £7,480 million, representing an additional efficiency of £309 million. We employ our proposed allowance in the calculation of the BA proposed price cap.

Opex - Comparisons between BA proposals and CAA IPs (CPI 2024)

Opex (£m)	Index	2024*	2027	2028	2029	2030	2031	Total
CAA IP	2024 CPI	1,520	1,556	1,590	1,582	1,570	1,563	7,862
BA proposals	2024 CPI	1,457	1,499	1,531	1,520	1,503	1,497	7,549
Difference	2024 CPI	-62	-57	-60	-62	-68	-66	-312

* 2024 Efficient baseline

Sources: CAA IPs, BA calculations

Opex - Comparisons between BA proposals and CAA IPs (CPIH 2024)

Opex (£m)	Index	2024*	2027	2028	2029	2030	2031	Total
CAA IP	2024 CPIH	1,520	1,544	1,577	1,568	1,554	1,545	7,790
BA proposals	2024 CPIH	1,457	1,488	1,518	1,507	1,487	1,480	7,480
Difference	2024 CPIH	-62	-56	-59	-62	-67	-65	-309

* 2024 Efficient baseline

Sources: CAA IPs, BA calculations

6.91. Comparisons against HAL's and CAA's figures can be found in Appendix A.

[37] The figures in this column exclude the impact of elasticity and RPE (except for Distribution contract). We adjust for those effects in the subsequent table.

7. Commercial Revenues

BA strongly supports the CAA's base step trend framework for assessing commercial revenues, including the use of bottom-up analysis as the primary tool complemented by top-down benchmarking. This represents a clear improvement on previous price controls and aligns with the CAA's H8 commitments. However, **persistent deficiencies in HAL's transparency, data provision and engagement** – mirroring those observed in opex – have materially constrained effective scrutiny and led to reliance on assumptions that risk understating the scope for revenue outperformance. Indeed, **the CAA has adopted a cautious approach in setting the efficient baseline, although evidence indicates materially larger efficiency gaps** than reflected in the Initial Proposals, notably in retail, catering, advertising, Fast Track and property revenues. This in turn suggests higher charges for the consumer and inefficient costs.

Similarly, certain modelling choices (including TDOC methodology, Pod revenues and cargo) lead to a baseline that does not fully reflect outturn performance. In addition, there are areas where revenue upside has not been captured, including the pass-through by HAL of Business Rates increases into commercial rents and the interaction between surface access products (such as the interaction of MSCP4 closure and higher surface access revenues elsewhere). Indeed, the MSCP4 overlay must reflect the most likely operational scenario being discussed with airlines, including partial operation and continued revenues.

Without **a materially strengthened efficiency challenge and more accurate baseline calibration**, the cumulative effect would be a commercial revenue allowance that is too conservative and does not reflect HAL's true revenue potential.

Our recommendation is for a revised commercial revenue forecast of £5,905 million, implying an increase of £412 million relative to the CAA's current proposals (2024 CPIH).

7.1. In a similar vein to our position on opex, we welcome the approach carried out by the CAA with respect to the calculation of Commercial Revenues. We welcome the CAA's application of the base-step trend approach to calculate the efficient level of commercial revenues. We agree with the CAA's use of a systematic bottom-up analysis as a tool for assessing inefficiency for the baseline year, while using a top-down econometric benchmarking to cross check the results.

7.2. We further highlight the lack of transparency by HAL both during Constructive Engagement and in its Business Plan on critical issues concerning its commercial revenue proposals, including HAL's refusal to provide a bottom-up approach to opex and commercial revenues forecasting and a lack of transparency in its underlying calculations. This has precluded our effective engagement in the Constructive Engagement process to interrogate whether HAL's proposed allowances represent efficient costs for the consumer.

7.3. However, we believe that the CAA should reconsider some of the assumptions used to set the efficient baseline, scope adjustments, roll forward and the overlays. These are explained in this section.

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Setting the efficient baseline – Scope adjustments

7.4. In order to set the efficient baseline, the CAA removes £9.8 million of revenue attributed to income from Pod parking in 2024 CPI. While we understand the logic behind the removal of revenues and costs associated with the Pod service (as this was an off-RAB investment), we have concerns with regards to the level of revenue being attributed to the Pod.

7.5. In the H7 CMA remittals consultation and final decision, the CAA assessed the costs and revenues related to Pod parking for H7. The CAA indicated that it had calculated an overall revenue of £14.5 million (2020 CPI) over the entire H7 period (which was lower than HAL's proposed £20.2 million for the period)[38]. On a yearly basis, this was equivalent to £2.9 million per annum[39].

7.6. After adjusting the CAA H7 figure to a 2024 price base, we obtain a revenue of £3.6 million which is materially lower HAL's proposal for H8. We therefore consider that the CAA's acceptance of a much higher £9.8 million figure for POD revenue in H8 (equivalent to a 170% increase to H7) is justified. For instance, the CAA has not explained why there is such a significant increase in Pod revenues but not in equivalent opex which remains relatively stable to H7 levels.

7.7. For avoidance of doubt, our position regarding Pod parking revenues is that the Pod service itself does not generate any additional value to customers. It is rather the proximity of the parking area to the terminal that provides such value. This is why the CAA should not be attributing any premium to the Pod service over other parking services considered within the RAB.

7.8. If the CAA considers that Pod revenues must be excluded from commercial revenues, it should do so by aligning to the approach and calculations it has previously. Considering both the CAA's previous decisions and available information from previous periods, we believe that a more appropriate Pod revenue figure to be used for the 2024 scope adjustment would be £3.6 million (instead of £9.8 million). This would be premised on the £2.9 million in 2020 CPI prices established by the CAA in the H7 remittals adjusted for 2024 CPI. This would align with the opex cost attributable to opex costs that the CAA has estimated in line with historical information. Therefore, £6.2 million p.a. (2024 CPI) initially excluded ought to be returned to commercial revenues.

7.9. We urge the CAA to review the revenues assigned for Pod parking and make the necessary amendments to determine the efficient revenue baseline.

[38] See CAP2980 & CAP3001. The CAA also stated that while HAL proposed a premium of 73%, it concluded that the premium was closer to 50%, and that when the effects of occupancy were striped out, the premium reduces to 8.2%.
[39] It is also worth noting that back in Q6, HAL had forecast POD related revenues to be £1.6m per annum.

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Setting the efficient baseline – bottom up analysis

a. Retail, catering and advertising

7.10. We support the CAA's decision to conduct an in-depth assessment of the efficiency of HAL's retail and catering revenues, and adjusting the retail revenue baseline to account for the improvements what would be expected of HAL to its service offering. Indeed, EE/YA's analysis demonstrates that HAL's reaction has been much slower than other airports to changes in its passenger mix and that HAL compares unfavourably to Gatwick on duty free and catering per passenger

7.11. However, the level of the efficiency challenge applied by EE/YA is less clear. EE/YA apply a 5.5% and 9.5% efficiency challenge to retail and catering respectively. However, the actual difference between HAL and Gatwick is much higher, at 11% and 42% respectively. EE/YA use Gatwick's 2019 catering revenue as the benchmark (instead of 2024) which reduces the efficiency gap to 19% and then halves the rate to set the efficiency challenge, which results in an understated challenge. On retail, the consultants halved the gap calculated for 2024.

7.12. In both cases, EE/YA adopt an unjustifiably conservative target that unduly advantages HAL despite its underperformance. Additionally, EE/YA are not forecasting any improvement in the efficiency gap during H8. The adjustment is solely done to the baseline year, but there are no overlays or management stretch assumptions throughout H8.

7.13. EE/YA indicate that the impact on space due to the implementation of Next Generation Security (NGS) would be higher than Gatwick's but do not explain why this effect would lead to the halving of the gap between HAL and Gatwick. This risks an unjustifiably low target unless there is analysis of the extent to which NGS would affect the ability for HAL to fully reach Gatwick's levels.

7.14. Using a conservative approach, we propose that the H8 baseline is adjusted by 75% of the observed gap in retail and catering in 2024 (i.e. 8.25% and 31% respectively), or alternatively to 100% of the observed gap in 2019 for catering (i.e. 19%) recognising EE/YA's concerns on the significant reconfiguration of Gatwick's food offering in recent years.

7.15. With regards to "Other retail/advertising" revenue, we note that EE/YA are suggesting closing 50% of the advertising gap against Schiphol. We believe that closing half the gap to be too low for an efficiency challenge. Similarly to the approach for retail catering, we propose to close 75% of the observed gap.

b. Car Parking

7.16. We are in broad agreement with the analysis carried out by EE/YA. We also support the implementation of a management stretch on all car parking revenues rather than the specific ones that HAL applied. We also agree that parking revenues are a function of yield management and passenger numbers, not just the latter.

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7.17. Nevertheless, it is important that the CAA analyses surface access as a whole, including the interactions of parking, car rental, rail, TDOC, and others. This is of particular importance with the replacement of MSCP4. Since the CAA is proposing to allow a reduction in revenue due to this project it must assess whether additional revenues need to be assumed due to higher usage of other products elsewhere. We encourage the CAA to conduct this assessment for Final Proposals. We elaborate on the impact of the MSCP4 project further in this section.

c. Terminal Drop-Off Charge (TDOC)

7.18. We set out our observations on the CAA's estimation of TDOC revenues below:

7.19. Methodology: Firstly, we note that the CAA has applied a similar methodology as HAL, but updated it with the CAA's passenger numbers and corrected for an issue with the usage of VAT. While the methodology appears to be sensible, we believe that it is incomplete and requires sense-checks. For example, when applying the CAA's methodology to year 2025, the resulting values are significantly lower compared to outturn revenues.

7.20. Applying the CAA's methodology to the actual number of passengers and TDOC tariffs (excl. VAT) applicable in year 2025 (£5.00) yields a revenue £46 million in 2025. However, TDOC revenue for 2025 in HAL's Regulatory Accounts is higher, at £56 million. This means that the CAA's approach yields a revenue that is lower than outturn by £10.5 million before the H8 price control has begun. We show our calculations based on the CAA's methodology below:

TDOC – Revenue estimation for 2025 (using CAA IP methodology) vs. Actual revenue

	Units	**Year 2025**
Outturn passengers	millions	84.5
Originating and departing pax share (CAA assumption IPs)	%	79.2
TDOC tariff per vehicle, excluding VAT (nominal)	£	5.00
TDOC mode share (CAA assumption IP)	%	19.9
Vehicle per pax (CAA assumption IP)	ratio	0.71
On-time payment rate per vehicle (CAA assumption IP)	%	96.5

Calculations

TDOC pax	millions	13.28
"Estimated" TDOC revenue	**£m, nominal**	**45.5**
Actual Revenue (HAL Regulatory accounts)	**£m, nominal**	**56.0**
Difference between Actual & estimated revenues	£m, nominal	10.5
Estimated / Actual	%	81%

Source: BA analysis of CAA IPs, HAL Regulatory accounts

7.21. The difference between the CAA's methodology and outturn passengers is too significant to be disregarded. While some of the difference could be explained by differences in the assumptions behind O&D passengers, TDOC mode share &

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vehicle per pax, we believe that the most relevant difference is due to the lack of inclusion of revenues obtained from penalties paid for late payments.

7.22. The CAA assumes revenues from 96.5% of vehicles that pay on time. However, it does not take into consideration that there are vehicles that pay penalties (i.e. late payments), whereas it had taken these into account when modelling H7 revenues from TDOC[40]. While we do not have the specific information on penalties for 2025, we are using the following assumptions based on the CAA's H7 model to model the revenues from penalties:

- £80 fine, with a £40 discount if paid in less than 14 days.
- 2.5% of the total amount of TDOC vehicles pay the fine in 14 days
- 0.006% of vehicles pay after 14 days.

7.23. Using these assumptions, the estimated penalty-related revenues would be £9.5 million in 2025, which when added to the revenues estimated using the CAA's methodology, would broadly align to the outturn revenues in the 2025 Regulatory Accounts. We recognise that there could be differences in the other variables which would explain why the figures do not perfectly align.

7.24. We urge the CAA review the modelling approach and underlying assumptions above to make the necessary amendments in the Final Proposals. For the purposes of the BA proposed price cap calculation, we use the modelling assumptions highlighted above.

7.25. Tariffs: We note that the CAA has used HAL's proposal of maintaining the current TDOC tariff (£5.83 excluding VAT) for the duration of H8. We are supportive of this assumption and encourage to maintain it for the Final Determinations. Although other airports in the UK may charge higher rates for the same concept, we believe that the public should not be burdened by an ever increasing TDOC tariff.

7.26. However, [REDACTED]. Requiring a "consultation process" for any price rises in H8 will not solve this matter. We therefore consider that the CAA should include a licence condition in which users (and therefore the consumer) would benefit from 100% of the additional TDOC revenues generated from any increases in the TDOC tariff. We discuss this further in our response on commercial revenue incentives.

d. Service Revenue, including Fast Track

7.27. We observe that the CAA includes a revenue line consisting of VIP charges (£32.2 million), Fast Track services (£15.75 million) and Other (£21.63 million) amounting to a total revenue of £70 million in 2024. We also note that the CAA assumes a 1% uplift on Fast Track services (£0.2m) in order to determine the efficient baseline.

[40] See link: https://www.caa.co.uk/media/neyld1by/h7opexcommercialrevenues_redacted.xlsm

7.28. However, we believe that the CAA is significantly underestimating the income from Fast Track services. This is because of two main developments in Fast Track revenue which both occurred on 1 June 2024 (i.e. during the baseline year):

i. Increases of Fast Track charges to airlines: On 1 June 2024, HAL decided to begin treating Fast Track as a commercial product and set a charge to the airlines for the usage of this service (prior to this the service was charged on a cost recovery basis). The implementation of this charge represented, in some cases, up to a [REDACTED] increase of what was being paid by airlines on a cost recovery basis for this service.

ii. The introduction of Fast Track charges to the general public of £12.50 per passenger.

7.29. Since these increases applied only since 1 June 2024, we believe that the 2024 revenue for this service does not fully account for the effects of these changes which were limited to 7 months at the most. This is also evidenced by the fact that Service Revenue in 2025 (as defined in HAL's Regulatory Accounts[41]) increased by £8 million (+12.5%) compared to 2024.

7.30. In view of the above, we believe that the CAA should be increasing Service Revenues for the baseline year. As we do not have access to HAL's monthly revenue figures, it is difficult for us to calculate the precise full year effect of the increases on revenues, though we estimate these to be between £4.14 million and £8 million. For the bottom end of the range, we have assumed that revenues between June and December 2024 are double the revenues between January-May 2024. The upper end of the range is the increase seen in service revenues between 2024 and 2025. We believe our point estimate needs to be at the top end of the range as there were products introduced that did not exist before June 2024 (i.e. Fast Track offered to the public). As such, we consider 2024 revenues need to be increased by £7 million to fully reflect the changes in June 2024. Given that EE/YA has assumed an efficiency target of £0.16 million, an additional £6.8 million uplift to the IP baseline revenue for Fast Track would be required.

7.31. We request that the CAA further analyse this issue and make the necessary amendments to the baseline. In the meantime, for our price cap estimate, we assume a revenue uplift of £6.8 million in the 2024 baseline (as calculated in the previous paragraph). We provide further comments with respect to commercial revenue incentives and Fast Track in the section on commercial revenue incentives.

e. Property

7.32. We note that this is one of the areas where the CAA consultants' analysis has been significantly hampered by the lack of information provided by HAL. We underscore the difficulties in assessing the efficiency of property income as HAL has provided no information on the location and type of the relevant facility, and that the CAA

[41] Service Revenue in HAL's Regulatory accounts: £64m (2024) and £72m (2025)

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should not be led to suboptimal decisions because of this information asymmetry. This information asymmetry needs to be addressed for Final Proposals.

7.33. Based on the information available, EE/YA make an efficiency challenge based on closing 50% of the gap between HAL and Dublin airport (using the measure Property revenues per passenger at benchmark airports) and therefore reducing non-guide price revenue by 2.5%. Given the lack of information, we suggest that the CAA closes 100% of the observed gap and puts the onus on HAL to provide the relevant information to demonstrate why a move away from this assumption is justified.

f. Other Revenues

7.34. We support the CAA's inclusion of a forecast for "Other Revenues", starting from a 2024 baseline of £7.3 million.

g. Cargo

7.35. We support the CAA's disaggregation of 2024 cargo revenues between cargo and the non-passenger flights[42], including the disaggregation of the associated movements, which the CAA then employs for forecasting cargo revenues (Table 5.12 in the Initial Proposals). For Final Proposals, we would ask the CAA to take into account the following:

i. Yield: The CAA assumed a fixed yield (on a real basis) for the entire period. This would not be appropriate if the CAA determines an H8 price cap higher than that the one effective in 2024.

   For instance, the mid-point average charge suggested in the Initial Proposals is £28.8 per pax over H8. Considering that the outturn revenue per passenger for 2024 was £26.3 (2024 is the year used for setting the baseline yield in the CAA calculations), this would suggest that the yields for forecasting cargo/non-passenger revenues should be increased by 9.5% to reflect the growth in the passenger charge.

   Similarly, since cargo flights tend to be operated on aircraft belonging to the noisier categories within HAL's rate card and, given the fact that HAL has been implementing a strategy of increasing the charges differentiation between quieter and noisier aircraft, it is reasonable to expect cargo yields increasing more than the passenger charge.

ii. Movement forecasts: Our cargo and non-passenger movement forecasts align with those proposed by the CAA. If the CAA were to forecast a lower number of passenger movements, there would be scope to increase cargo ones in line with the logic that HAL and airlines will seek to maximise use of the overall 480k movement cap as shown in previous years.

[42] As an aside, the way that HAL has been reporting these revenues over the years in the regulatory accounts has been highly inconsistent.

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7.36. In this submission we are not presenting an amended cargo revenue forecast, but we highly encourage the CAA do so in its Final Proposals. We also recommend the CAA takes into account the points raised in this section when updating the forecast.

h. Taxi feeder park revenues

7.37. We note that HAL proposed to move taxi feeder car park towards commercial revenue. While we acknowledge that previously we opposed this proposal, we have reconsidered this proposal given our views on the low powered incentives of Other Regulated Charges (ORCs). We therefore support this move. Based on the latest information on the cost of this activity as well as the opportunity to commercialise it, we are assuming a forecast revenue of [REDACTED] per annum (2024 CPI)

Setting the efficient baseline – Effect of Business Rates on Commercial Revenues

7.38. While Business rates are dealt with under opex, we consider that changes in Business Rates will have a direct impact on commercial revenues. This is because some of the businesses that operating within Heathrow's perimeter do not pay Business Rates directly. This applies at least in the case of retail and catering businesses within the terminals.

7.39. In this case, these rates are included in HAL's Business Rates bill, with the retailers assumed to pay their allocated share of Business Rates through the rents that HAL collects from them. As such, it is reasonable to assume that HAL will pass on to retailers a portion of the Business Rate increases and therefore it is expected for the retail revenue to increase by the corresponding amount. This amount would be on top of the efficiency targets assumed for retail revenue.

7.40. The question would then be how to calculate the amount to be apportioned to retailers. Since Business Rates are linked to the level of revenues and expenses, we propose to use the share of retail income (as a percentage of HAL's overall revenue) as the coefficient for the revenue share. Based on the 2024 revenue figures, £437 million of HAL's overall revenues (£3,549 million) were related to Retail & Catering[43]. In other words, 12.3% of the Business Rates increases should be allocated as increased rents from retailers. Based on the CAA's Business Rates estimates for H8, we believe that around £55.8 million should be allocated to increased revenues from commercial activities as a consequence of HAL passing on a portion of the increases of Business Rates to the "Retail & Catering" segment:

[43] Sub-categories included in the calculation: Retail, Catering, Bureaux, Other Retail and Other Services.

Estimation of Business rates increases to be allocated to Retail

2024 CPI	2024	2027	2028	2029	2030	2031	Total
Business Rates* ** (£m)	[...]***	180.0	223.0	223.0	223.0	223.0	1072.0
Difference (vs. 2024) (£m)		56.3	99.3	99.3	99.3	99.3	453.5
Percentage allocated to Retail (%)		12.3%	12.3%	12.3%	12.3%	12.3%	
Amount allocated to retail revenues (£m)		**6.9**	**12.2**	**12.2**	**12.2**	**12.2**	**55.8**

Source: BA analysis
**Actual 2024 business rate value excluding capitalized "Rents and rates". The latter is being treated separately in our submission*

*** 2027-2031 exclude the elimination of the "logged up" amount, as that is a regulatory adjustment from H7*
**** Based on HAL Business Plan*

7.41. We request the CAA to review the evidence provided above and make the necessary adjustments when calculating the commercial revenues and H8 price cap in the Final Proposals.

Overlays

a. MSCP4

7.42. The CAA has maintained HAL's assumptions in relation to the revenue reduction from the closure of MSCP4 – from -£17.9 million in 2027 up to -£19.4 million in 2029, and then assuming a positive revenue of £3.1 million from 2030 (all in 2024 CPI prices). We also note that the EE/YA report indicates that the project was "accepted by airlines through the capex governance process".

7.43. It is important to clarify that while airlines have agreed that action is needed in relation to MSCP4, this does not imply that there has been agreement on the scope and associated financial projections.

7.44. [REDACTED]

7.45. [REDACTED]

7.46. Based on the above, we request the CAA to:

i. Enquire as to the current status of the project.

ii. Review the latest information regarding options and associated financials presented by HAL to airlines.

iii. Assess whether there would be an impact in other transport modes at the airport from the [REDACTED] closure of MSCP4.

iv. Adjust the expected level of revenues and costs in the Final Proposals based on the most likely option.

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7.47. For the purpose of the adjusted airline price cap proposals, we are assuming that the MSCP4 will remain partially open and that TDOC continues to bring in revenue (so the overlay would assume that only parking revenues are reduced, not TDOC).

Commercial Revenue – Summary and our recommendations

7.48. Based on our analysis above, we recommend that the CAA:

i. Maintain the base-step-trend methodology, including the use of bottom-up analysis to set the baseline and top-down econometric benchmarking as a cross-check.

ii. Ensure that HAL does not benefit from information asymmetries by requiring full transparency and placing the burden of proof on HAL where data is incomplete or unavailable.

iii. Review and reduce the Pod parking revenue adjustment to align with prior CAA determinations and ensure consistency with observed value drivers.

iv. Increase the efficiency challenge applied to retail, catering and advertising revenues by closing a substantially higher proportion of the observed gap to comparators. In particular, implement more challenging targets for Retail, Catering, Advertising, and Property by closing the gap to 75%-100% to more efficient comparators, rather than just assuming a conservative 50%.

v. Apply a stronger efficiency assumption to property revenues, including closing the full observed gap where insufficient evidence has been provided by HAL.

vi. Review and update the modelling of TDOC revenues to incorporate penalty income and ensure consistency with 2025 outturn revenues.

vii. Introduce a licence condition to ensure that any increase in TDOC tariffs during H8 is fully passed through to users.

viii. Increase the baseline for service revenues, including Fast Track, to reflect the full-year effect of pricing changes introduced during 2024.

ix. Review the interaction across surface access revenues, including parking, TDOC and alternative transport modes, particularly in light of the MSCP4 closure.

x. Ensure consistency between cargo revenue forecasts and the CAA's proposed changes to airport charges and reflect differentiation across cargo aircraft noise categories.

xi. Incorporate the impact of Business Rates increases into commercial revenues, including passing through the share of the increase paid by retail and catering in rents (this could be modelled as addition commercial revenue or reduced opex).

xii. Review and update the MSCP4 overlay to reflect the most likely operational scenario, including partial operation and associated revenue impacts (such as on

TDOC). In addition, decide whether specific provisions are necessary in the settlement to deal with changes in scope.

7.49. Based on our analysis, the implementation of the above should lead to the following changes in commercial revenues.

Summary of recommended changes to commercial revenues (vs. IPs)

Commercial Revenues BA recommended changes (vs. IPs)	CPI 2024 £m	2024	2027	2028	2029	2030	2031	Total[44]
Pod parking	Baseline	6.2						31.1
Catering	Baseline	8.4						42.1
Retail	Baseline	7.5						37.5
Other Retail	Baseline	1.2						6.1
TDOC	Forecast		9.5	9.8	9.9	10.1	10.3	49.7
Property	Baseline	1.4						7.0
Business rates on retail	Overlay		7.0	12.2	12.2	12.2	12.2	55.7
Fast track	Baseline	6.8						34.2
MSCP4	Overlay		[...]	[...]	[...]	[...]	[...]	[...]
Taxi feeder	Baseline	[...]						[...]
								[...]

Source: BA analysis

7.50. Applying the above changes to the CAA's opex and commercial revenues model, and after adjusting for volume and price effects, our recommendation is for a revised commercial revenue allowance of £5,960 million, representing an additional efficiency of £416 million compared to the CAA's forecast (2024 CPI). We subsequently rebase to 2024 CPIH, which revises our proposed opex allowance to £5,905 million, representing an additional efficiency of £412 million.

Commercial Revenues - Comparisons between BA proposals and CAA IPs (CPI 2024)

Commercial Revenue (£m)	Index	2024*	2027	2028	2029	2030	2031	Total
CAA IP	2024 CPI	1,085	1,080	1,089	1,099	1,133	1,142	5,544
BA proposals	2024 CPI	1,120	1,151	1,171	1,186	1,218	1,234	5,960
Difference	2024 CPI	35	71	82	87	85	91	416

* 2024 Efficient baseline

Source: BA analysis, CAA Initial Proposals

[44] The figures in this column exclude the impact of elasticity and RPE. We adjust for those effects in the subsequent tables.

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Commercial Revenues - Comparisons between BA proposals and CAA IPs (CPIH 2024)

Commercial Revenue (£m)	Index	2024*	2027	2028	2029	2030	2031	Total
CAA IP	2024 CPIH	1,085	1,072	1,080	1,090	1,121	1,129	5,493
BA proposals	2024 CPIH	1,120	1,142	1,162	1,176	1,205	1,220	5,905
Difference	2024 CPIH	35	70	82	86	84	90	412

* 2024 Efficient baseline

Source: BA analysis, CAA Initial Proposals

7.51. Comparisons against HAL's and CAA's figures can be found in Appendix B.

8. Other Regulated Revenues (ORCs)

BA considers that the current ORC framework is no longer effective, with governance having materially deteriorated into a pass-through mechanism that fails to deliver meaningful cost control, transparency or airline engagement. This is to the detriment of consumers. Airlines lack visibility and influence over key cost drivers, while the intended collaborative governance model has not materialised in practice, as evidenced by significant cost increases in areas such as PRM without adequate scrutiny or involvement. While BA supports the CAA's decision not to expand the scope of ORCs by including further aeronautical costs, it considers that this does not go far enough, as the continued inclusion of material services such as baggage/HBS undermines effective cost discipline and creates a risk of perverse incentives, including the pass-through of costs linked to HAL's own performance failures.

More broadly, the current framework – including **the proposed licence condition** and simplified modelling approach adopt uniform efficiency assumptions and provide for ex-post controls that are **unlikely to deliver meaningful cost discipline** given the low-powered incentive regime. There are also **material concerns regarding cost allocation and cross-subsidisation** in relation to non-airline costs and Business Rates. Without **structural reform of the ORC framework, including a reduction in scope, reclassification of material services into aeronautical charges and stronger ex-ante scrutiny**, the cumulative effect would be an ORC regime that continues to allow inefficient cost pass-through and does not adequately protect consumers.

Based on the above adjustments, we propose ORC revenues of £614 million in 2024 CPIH in H8.

Scope of services and concerns over ORC framework deterioration

8.1. BA considers that the current ORC framework is no longer effective, with governance having materially deteriorated over time and failing to deliver meaningful cost control or stakeholder engagement. In practice, ORCs have become a pass-through mechanism with limited incentives on HAL to manage costs efficiently, as airlines have neither visibility nor influence over underlying cost drivers, including contract negotiations.

8.2. The collaborative governance model originally envisaged has not been realised in practice, with ORC forums functioning largely as one-way communication rather than genuine scrutiny or challenge, and this has persisted despite expectations of improvement following H7. For instance, this is evident in areas such as PRM, where costs have trebled since 2019 without adequate justification or airline involvement, including no meaningful involvement in HAL's latest PRM contract renegotiation.

8.3. Given the materiality of ORCs and the resource required to engage with them, BA considers that the current framework lacks proportionality and delivers limited value for consumers, with stronger incentives more appropriately delivered through airport charges and MTIs (where relevant). As a result, BA believes the scope of ORCs should be reduced wherever possible and that the framework itself should be fundamentally reconsidered.

8.4. BA therefore supports the CAA's decision to reject HAL's proposals to expand the scope of ORCs, recognising that doing so would have shifted material cost categories away from high-powered opex efficiency incentives and further weakened cost discipline. Given the scale of these costs and the likelihood of upward pressure, most notably in areas such as Business Rates (see our response on opex), BA considers that maintaining these activities within the aeronautical charges is essential to ensure effective regulatory scrutiny and protect consumers.

8.5. While BA supports the CAA's decision not to expand the scope of ORCs, we consider that this does not go far enough, as the current framework fails to apply effective cost discipline to material services such as baggage/HBS. Given the low-powered incentives inherent in ORCs, BA believes that retaining such costs within this framework is not in the consumer interest and that they should be reclassified into aeronautical charges, where stronger efficiency incentives and accountability would apply. This is particularly important in the context of the repeated and significant baggage system outages by HAL. If baggage remains within ORCs, the proposed introduction of an MTI would create perverse incentives for HAL to pass through the costs of meeting performance targets driven by its own failures onto consumers (see our response on MTIs for further information on baggage performance).

8.6. In line with our comments in the commercial revenue section, we have reconsidered HAL's proposal to move the taxi feeder car park from ORCs towards commercial revenue activities. Moving these activities out of the ORC framework would better align incentives for HAL to deliver measurable benefits and adopt a more efficient, commercially driven pricing structure for the service.

8.7. BA does not accept HAL's argument that reclassifying these costs into aeronautical charges would conflict with the "user pays" or fairness principles, considering that this outcome can be proportionately managed through the regulatory framework. In particular, such costs could be incorporated into the rate card following a robust consultation with users, with existing safeguards allowing airlines to challenge any charges that do not comply with regulatory principles, including through recourse to the CAA under the Airport Charges Regulations 2011.

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8.8. BA reiterates its concern with the application of financial MTIs to activities within the ORC framework, as the low-powered incentive nature of ORCs creates a risk that HAL could increase costs in order to meet performance targets, with those costs then passed through to users. This is already evident in the CAA's proposal to introduce a financial incentive for PRM, where inefficient cost increases could be passed through with minimal scrutiny. For clarity, BA does not in any way argue against introducing a financial rebate for the MTI on the timely delivery of departing baggage; indeed, such a rebate is entirely warranted given HAL's underperformance and needs to be further tightened in view of the significant outages (see our response on MTIs above). BA's view is that baggage costs ought to be reclassified into aeronautical charges, in addition to the introduction of the financial MTI.

Proposed licence modification

8.9. BA notes the CAA's proposal to introduce a licence condition requiring HAL to notify the CAA and users in writing where ORC unit rates (or any cost components) increase in real terms but considers that this measure is insufficient to address the underlying governance and incentive issues within the framework.

8.10. As an ex-post mechanism, it limits the ability to intervene effectively, focuses only on cost increases without recognising potential inefficiencies in the broader cost base, and does not enhance airlines' ability to influence outcomes or engage meaningfully in cost drivers such as contract negotiations. As such, BA considers that the proposal does not adequately strengthen accountability or deliver cost discipline.

8.11. BA therefore maintains its position that the ORC framework requires a structural reform, as its current design embeds low-powered efficiency incentives that fail to deliver effective cost discipline or accountability. In particular, BA considers that services – including key aeronautical services for the consumer such as baggage/HBS – should be reclassified into aeronautical charges, where stronger incentive mechanisms apply as part of the opex allowance. This would ensure that HAL is subject to appropriate regulatory scrutiny and that consumers are protected from inefficient cost pass-through.

Modelling ORC costs & revenues

8.12. BA notes the CAA's proposed methodology for calculating ORCs, in paragraphs 7.28-7.29 of the Initial proposals and the corresponding calculations shown in Table 7.3 which simplifies the approach by avoiding detailed modelling of individual components. However, we consider that this approach raises concerns as to the robustness and accuracy of the resulting allowances and would benefit from further scrutiny by the CAA.

8.13. BA notes that the CAA applies a uniform efficiency challenge to ORCs in line with the overall opex baseline (4.3%). We have two concerns with this approach:

i. The areas where efficiencies were identified for HAL's opex are not necessarily linked to the ORC activities. For example, one of the major efficiency challenges

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is in relation to security staff costs (which have no link to ORCs). Assuming a level of efficiency for ORCs that in practice may not materialise could lead to outturn ORC revenues being much higher than forecast (since these are passed through under the current arrangements). We request the CAA to focus its efficiency challenges on areas that could affect ORCs.

ii. More generally, we are concerned about assigning efficiencies to ORCs. In the CAA's methodology, the overall efficiency challenge on opex is being explicitly split between aeronautical charges and ORCs. Given the low powered incentives on ORC costs, we are concerned that HAL may not deliver its efficiency target and passing on its underperformance to users. It is important to set a framework within ORC that would ensure that such efficiency challenge is maintained throughout H8.

8.14. Consistent with our proposals in the Alternative Business Plan, we propose to **remove baggage/HBS ORC** and recover these costs from aeronautical charges (c. £134.4 million in 2024 CPI prices). This proposal has been included in our modelling for the BA price cap proposals (reduction of our ORC revenue baseline of £134.4 million).

8.15. Based on our revised proposal on **taxi feeder car park**, we propose to remove from ORCs £2.1 million in costs (of which £1.1 million are direct costs). The revenue from this activity is therefore treated as a commercial revenue.

8.16. We propose that **PRM** revenues to be modelled as a separate bespoke item, rather than being subject to the same top-down methodology as proposed by the CAA for all ORCs. The reasoning for this is as follows:

i. PRM costs have already been modelled by the CAA which enables to match costs and revenues.

ii. Since the CAA has made important efficiency assumptions on PRM costs, by reducing its PRM baseline by £13 million (-20%) it is important to ensure that there is no misalignment between the expected costs, cost efficiencies, and revenues.

8.17. In addition, we re-iterate our request to the CAA set out in the MTI section of our response to obtain and review the new PRM contract concluded between HAL and the new supplier to inform its efficiency assessment for Final Proposals.

8.18. We note that an overlay for **Business Rates** of £1.35 million has been added to the CAA's ORC calculations. We are not aware as to how Business Rates have been allocated to ORCs, but considering that overall Business Rates are set to be around £100 million higher in 2027 compared to 2024, we would request the CAA to explain why it has only allocated 1.3% of those costs to ORCs.

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Treatment of non-airline fixed costs

8.19. We agree with the CAA's decision to reject HAL's proposal to move all fixed costs (including non-airline costs) to aeronautical charges. We firmly support the principle that non-airline costs should be recovered from non-airlines, rather than being subsidised by airlines, in line with the user pays principle.

8.20. However, we are concerned about the capping of ORC water and wastewater charges (reducing the non-airline share of the of bill for specified activities from £9.91 million to £6.5 million). While we note the CAA's view that the resulting charge should not be much higher than at other major airports, we are concerned that airlines will be asked to cross-subsidise non-airlines to cover this gap.

8.21. We note that the CAA's approach in Table 7.3 retains an overlay of £9.91 million for non-airline fixed costs, but we consider that this raises concerns regarding the source and allocation of funding under the proposed cap. In particular, BA emphasises that the principle of non-subsidisation must be maintained to ensure that costs are not inappropriately shifted between users or activities, and that cross-subsidisations are avoided.

ORCs – Summary and our recommendations

8.22. Based on our analysis above, we recommend that the CAA it:

i. Maintain its proposal not to expand the scope of ORCs to cover the aeronautical charges proposed by HAL and ensure that those costs remain subject to high-powered efficiency incentives within opex.

ii. Implement a structural reform of the ORC framework to address the low-powered incentive regime and restore effective cost discipline and accountability. This could proportionately be done by reducing the scope of ORCs and reclassifying services, such as baggage/HBS and taxi feeder park, into aeronautical charges where stronger incentives apply.

iii. Ensure that any arguments by HAL on fairness are justified appropriately and investigate whether these could be addressed through more proportionate means, such as the charging structure within the rate card.

iv. Reconsider the adequacy of the proposed licence condition on ORC cost increases and assess whether this is more proportionate than the structure solution of including costs into the high-powered incentives of the opex allowances.

v. Reviews its ORC revenue modelling taking the below into account:

- Exclude £134.4m of Baggage/HBS ORC costs (as we assume those costs will be recovered through Aeronautical charges)
- Exclude Taxi feeder costs (£1.1m in direct costs)

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- Allocate only those opex efficiencies that would impact ORCs
- Treat PRM as a bespoke revenue line
- Review the size of the Business Rates overlay
- Refrain from requesting airlines to cross subsidise £3.4 million p.a. to non-airlines due to capping of water charges.

8.23. Based on our analysis, the implementation of the above recommendations should lead to ORC revenues of £620 million in 2024 CPI, or £614 in 2024 CPIH over H8.

Calculation of ORCs for H8 – BA proposal

Figures in CPI 2024 (£m, unless stated)	**2024**	**2027**	**2028**	**2029**	**2030**	**2031**
ORC revenues	285.7					
less H7 fixed costs and business rates	-39.9					
plus 2024 under-recovery	3.2					
plus 2023 over-recovery reflected in lower 2024 charges	14.4					
2024 outturn ORC direct costs	263.3					
Remove Baggage/HBS direct costs	-134.4					
Remove PRM costs (to be treated as bespoke)	-65.7					
Remove Taxi feeder park direct costs	-1.1					
Direct costs after removing Baggage/HBS & PRM & Taxi feeder	62.0					
Baseline efficiency adjustments (excluding. Business Rates) %	95%					
Efficient ORC direct cost baseline	59.0					
Total efficient opex (excluding. Business rates and PRM)	1,288.7	1,289.0	1,278.1	1,267.7	1,250.6	1,245.0
Share of 2024 direct ORC costs as a proportion of total opex (excluding Business rates), %	4.57%	4.57%	4.57%	4.57%	4.57%	4.57%
Forecast H8 direct costs		59.0	58.5	58.0	57.2	57.0
plus H8 non-airline fixed costs		9.91	9.91	9.91	9.91	9.91
plus Allocation of rates to ORCs		1.35	1.35	1.35	1.35	1.35
ORC revenue (Excluding PRM, Baggage/HBS & Taxi feeder)	**59.0**	**70.2**	**69.7**	**69.3**	**68.5**	**68.2**
PRM (efficient baseline costs + overlays)	**52.2**	**54.1**	**54.7**	**54.7**	**55.3**	**55.3**
Efficient 2024 ORC revenue (excluding Baggage/HBS & Taxi feeder)	**111.1**					
H8 ORC revenues (CPI 2024)		**124.4**	**124.4**	**124.0**	**123.8**	**123.5**
H8 ORC revenues (CPIH 2024)		123.4	123.4	122.9	122.5	122.1

Source: BA Analysis

8.24. The ORC forecasts amount to £620 million (2024 CPI) and £614 million (2024 CPIH). This compares to the CAA IP's £1,307 million (2024 CPI) and £1,289 million (2024 CPIH). This shown below and represents a difference of £674 million (2024 CPIH) against the

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CAA's proposal of £1,289 million mainly driven by the removal of baggage/HBS costs and the taxi feeder park to aeronautical charges.

ORC - Comparisons between BA proposals and CAA IPs (CPI 2024)

ORC	Index	2024**	2027	2028	2029	2030	2031	Total
CAA IPs	2024 CPI	252	264	263	262	260	259	1,307
BA proposals*	2024 CPI	111	124	124	124	124	124	620
Difference	2024 CPI	-141	-140	-139	-138	-136	-135	-687

*BA proposals include the following changes: Baggage/HBS moved to Aero charges, Taxi feeder park moved to Commercial Revenues ** Efficient baseline

Source: BA Analysis, CAA IPs

ORC - Comparisons between BA proposals and CAA IPs (CPIH 2024)

ORC	Index	2024**	2027	2028	2029	2030	2031	Total
CAA IPs	2024 CPIH	252	262	260	258	255	254	1,289
BA proposals*	2024 CPIH	111	123	123	123	123	122	614
Difference	2024 CPIH	-141	-139	-137	-135	-133	-131	-674

*BA proposals include the following changes: Baggage/HBS moved to Aero charges, Taxi feeder park moved to Commercial Revenues ** Efficient baseline

Source: BA Analysis, CAA IPs

9. Commercial revenue incentives

We support the CAA's overall approach to commercial revenue incentives, in particular its **rejection of HAL's proposals to depart from the single till framework**, which we consider remains firmly in the interests of consumers. However, we are concerned that the CAA has not definitively excluded alternative approaches to commercial property investment despite a clear absence of evidence to justify change, and we set out why maintaining a clear and unambiguous single till is essential to avoid consumer harm and regulatory uncertainty. We also highlight **risks associated with HAL's incentives to increase charges on directly or indirectly consumer-facing services, including TDOC and Fast Track, and propose targeted safeguards** to ensure that any upside revenues are fully returned to users and guarantee that the price control framework is not circumvented.

9.1. The CAA dedicates a chapter in its Initial Proposals to regulatory incentives (capex and commercial revenue). In this section we set out our views on commercial revenue incentives, while our assessment of capex incentives is addressed separately in this response.

Commercial property investment incentives

9.2. We agree with the CAA's view that HAL's proposals to introduce a different treatment of commercial property investment have not demonstrated benefits for consumers. We fully support the CAA's proposal to retain the single till approach. The single till model continues to best serve consumer interests by lowering charges

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and airfares, supporting connectivity and economic growth, and enabling efficient planning of airport expansion.

9.3. However, we are concerned that the CAA has not fully ruled out HAL's proposals and states that it remains open to consider a different treatment should there be a special case in which doing so would be interest of users.

9.4. In our view the CAA should unambiguously reaffirm the single till for H8 and decline to pursue any further work on alternative till structures or boundary adjustments for commercial property investment that would harm consumers. The case for change has not been made, with HAL presenting poorly considered theoretical arguments for developing an alternative till structure and failing to demonstrate a practical constraint to the development of property projects. We continue to stand by the findings of the CEPA report assessing HAL's proposals that was commissioned by BA and shared with the CAA.

9.5. There is limited theoretical or empirical evidence to suggest that either the CAA or airlines act as a constraint on commercial property development. The CAA's approach in H7 has been facilitative, enabling projects supported by robust business cases. Airlines similarly have a clear incentive to support viable developments, given the associated benefits, as demonstrated by their approval of over [REDACTED] of investment [REDACTED].

9.6. The existing regulatory regime materially reduces the risk profile of commercial property investment by distributing costs and periodically recalibrating revenue expectations across control periods. Construction costs enter the RAB, providing a guaranteed return on efficient investment regardless of revenue performance. In-period revenue risk is limited and is reset at each price control review.

9.7. The claim that the allowed WACC is insufficient to motivate property investment fails to account for this de-risking effect: HAL's property investments are structurally less risky than equivalent investments in the wider commercial property market, and the allowed WACC should already reflect the blended risk profile of HAL's activities. We present independent academic advice by Professor Robin Mason in our response on the WACC on how HAL's asset beta ought to be adjusted downwards to reflect this systematic de-risking effect.

9.8. Indeed, regulators and credit rating agencies have consistently acknowledged that the single till framework stabilises risk, notably by dampening volatility, and there is little empirical support for the claim that it weakens airports' incentives to invest in commercial assets. At Heathrow, the scale of capital investment delivered since privatisation clearly indicates that HAL faces strong and effective incentives to undertake capex at the allowed WACC.

9.9. Any adjustment to the boundary of the single till is likely to cause significant consumer harm.

i. Introducing a separate regulatory treatment for commercial property would create perverse incentives. HAL could be encouraged to understate expected

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returns or inflate costs on proposed developments to shift them outside the regulated till. It would also incentivise prioritisation of off-till assets and the design of infrastructure that maximises non-aeronautical returns even where this compromises aeronautical efficiency. Such distortions will ultimately work against the interests of consumers.

ii. Any adjustment to the boundary of the single till would, in practice, introduce hybrid till characteristics without the transparency and discipline of a properly constituted dual till. The regulatory and monitoring burden this would impose on the CAA is not proportionate to the hypothetical problem it purports to solve and would create a high risk of legal challenge as evidenced in other jurisdictions.

iii. The CAA should recognise the substantial body of regulatory precedent demonstrating the consumer harm associated with modifying the single till framework, as evidenced in the CEPA report, including findings from airport charges regulators in France, Switzerland, Spain and Ireland.

9.10. The CAA should therefore confirm clearly in its Final Proposals that the single till will be maintained unchanged for H8 and that no further work will be undertaken on adjustments to the till boundary for commercial property investment during this price control period. Leaving open the possibility of such an approach, in the absence of any evidenced need, risks harming the consumer, creating unnecessary regulatory uncertainty and diverting time and resources across stakeholders.

Terminal Drop-Off Charge (TDOC)

9.11. In the previous section on commercial revenues, we set out areas where the CAA could strengthen its forecasting of TDOC revenues, including the need to incorporate a specific revenue line for late payments. We also highlighted that certain assumptions underpinning HAL's projections, in particular mode share calculations, may require further scrutiny.

9.12. We also support the CAA's proposal, consistent with HAL's commitment and assumptions in its Business Plan, to maintain the TDOC charge flat in nominal terms over H8.

9.13. However, we are concerned about HAL's incentive to increase the TDOC tariff during H8. The EE/YA study on opex and commercial revenues indicates that a revenue-maximising entity would have a clear incentive to raise such tariffs, particularly given that comparator UK airports already apply higher charges. [REDACTED].

9.14. Given this inherent incentive, we consider that the only basis on which we can support an assumption of a flat charge over H8 is through a licence condition requiring that any revenues collected by HAL from a tariff above the current £7 level are returned to users. We do not consider that the current H7 revenue sharing arrangements are sufficient, as they do not remove HAL's incentive to increase tariffs, given that it would continue to retain a proportion of the resulting revenue uplift.

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9.15. If the CAA were to maintain the current 65%/35% risk sharing arrangement, or any model under which HAL retains a share of incremental revenues from higher charges, we would request the following safeguards to protect the consumer:

- The CAA should forecast TDOC revenues throughout H8 assuming HAL would progressively increase the tariff in line with other airports.
- It should be made explicit that the sharing mechanism applies only where revenues exceed expectations, consistent with the CAA's intent at the time of its introduction in H7[45].

9.16. We address the estimates for the TDOC revenues in the commercial revenues section of our response.

Fast Track

9.17. We fully agree with the CAA's concerns regarding Fast Track tariffs levied on consumers following a significant increase on 1 June 2024 after the H7 settlement was concluded. Indeed, HAL began treating Fast Track as a commercial product and set a charge to the airlines for the usage of this service (prior to this the service was charged on a cost recovery basis). The implementation of this charge represented, in some cases, up to a [REDACTED] increase of what was being paid by airlines on a cost recovery basis for this service.

9.18. As HAL failed to demonstrate that these revised charges were cost reflective, or that they were justified due to similar increases in underlying costs, we are concerned that the H7 price control and single till have been circumvented and HAL benefitted from windfall gains.

9.19. We therefore do not consider that an obligation to consult would be sufficient, as consultation alone would not prevent such price increases or contain the associated perverse incentives, as the CAA itself recognises.

9.20. Consistent with our position on TDOC, we consider that a true-up mechanism should be implemented whereby any revenues generated from increases in fast-track charges are returned to users.

9.21. We address the estimates for the Fast Track revenues in the commercial revenues section of our response.

[45] CAA's CAP3001, paragraph 7.30

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10. Capital expenditure assessment: envelope and prioritisation

BA strongly supports the CAA's methodology in setting the H8 capex envelope, including the use of a transparent, evidence-based needs assessment and prioritisation framework to determine an appropriate level of investment. **The proposed envelope of £5.8 billion – while significant in size - is consistent with Heathrow's delivery capability**, broadly aligned with the airline community's Alternative Business Plan, and appropriately constrains spend to what is deliverable and affordable within a live, capacity-constrained environment. The CAA's methodology, including the requirement for a clear "golden thread" linking investment to consumer outcomes and the rejection of projects lacking robust business cases, represents a clear improvement on H7 and ensures that capital expenditure is contingent on efficiency and demonstrable consumer value.

Indeed, **we support the CAA's acknowledgement of the persistent deficiencies in HAL's Business Plan** – notably the absence of a clear golden thread and insufficient detail in business cases – which have materially constrained effective scrutiny and prioritisation by airlines and have undermined the Constructive Engagement process.

BA supports the CAA's decision to set an overall envelope without mandating specific investments, preserving flexibility for HAL and airlines to prioritise (and reprioritise) the portfolio throughout H8. However, this approach is only effective if supported by robust governance, including continuous airline involvement from early-stage project identification through to delivery. In the absence of this, there is a risk of inefficient spend and late-stage changes.

BA supports the prioritisation of T5 Optimisation, which is now consolidated into a single phase, within the envelope and the removal of expansion-related projects. At the same time, **delays to critical capacity programmes such as Terminal Occupancy risk constraining growth, harming consumers and creating perverse incentives under the TRS mechanism**, whereby HAL could benefit financially from non-delivery. These risks must be addressed to ensure that incentives remain aligned and that consumers are protected from the consequences of under-delivery.

We further **support the CAA's prioritisation of Asset Management and Compliance** and highlight the need that to the proposed envelope covers clearly defined safety-critical, mandatory compliance needs and that discretionary scope is subject to robust scrutiny and prioritisation.

Finally, **BA firmly supports the CAA's deliverability assessment**, which is critical in ensuring that investment is feasible, deliverable and reflects real operational constraints. **The CAA must avoid increasing the overall capex envelope** and consider any requests for further spend against constraints on deliverability, affordability, as well as the additional constraints resulting from the simultaneous expenditure being proposed by HAL outside H8 such as enabling work for expansion and commercial property projects.

A very high bar needs to be applied to late submissions by HAL seeking to relitigate the business cases as this would create significant regulatory risk, undermine the integrity of the Constructive Engagement process and bypass structured scrutiny by airlines It could equally

create perverse incentives and confusing narratives on issues such as asset management, to the detriment of consumers.

Our support of the CAA's proposed envelope

10.1. BA agrees with the methodology used by the CAA to determine a capital investment envelope of £5.8 billion (2024 CPIH) for 2027 to 2031. This aligns with Heathrow's historical delivery capacity and protects consumers from funding an undeliverable plan.

10.2. In this vein, we support the requirement to transparently define project benefits and outcomes, creating a "golden thread" linking capex to service and value improvements.

10.3. We also endorse the assessment by the CAA and its consultants that a need in itself is not an investment demand, confirming that no capex should proceed without a robust business case and options analysis following prioritisation.

10.4. We support the CAA's approach to deriving this envelope through project prioritisation (with the highest category focusing on safety, operational resilience, and compliance, followed by customer experience, operational performance and efficient growth) using an approach requiring HAL to justify each project's need and consumer benefits.

10.5. We firmly support the CAA's concerns on HAL's Business Plan, including the lack of the "golden thread" demonstrating clear benefits between several business cases and the consumer, and questioning numerous discretionary projects.

10.6. The CAA has confirmed our view that capex must be limited to what can be efficiently delivered, reflect its run-rate and genuine needs. By proposing an envelope smaller than that proposed by HAL and requiring optioneering and benefit quantification, the CAA is making capex allowances contingent on efficiency and consumer value. BA welcomes this approach.

10.7. During H8 Constructive Engagement, airlines submitted an alternative capex plan with their Alternative Business Plan (ABP) amounting to £5.5 billion and repeatedly stressed the need to assess against affordability and deliverability. The CAA's £5.8 billion proposal largely aligns with our input, and we commend the CAA for prioritising safety, resilience, and growth-critical projects while deferring or rejecting low-value schemes.

10.8. **BA therefore firmly supports the capex envelope set by the CAA, conditional on robust governance, prioritisation to ensure efficient spend, and the inclusion of the entirety of the T5 Optimisation Programme.**

Review of the process followed and potential late submissions by HAL

10.9. The H8 Method Statement set out a single Business Plan process intended to address the shortcomings of the H7 Constructive Engagement identified in the

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CAA's Lessons Learned exercise. The expectations of this process were clear to both HAL and the airlines from the outset, including the need for a materially different approach to engagement for H8 to be effective.

10.10. However, throughout Constructive Engagement, BA and the airline community consistently raised concerns regarding the absence of a clear "golden thread" in advance of HAL's Business Plan linking consumer research, proposed capital investment, and the resulting consumer benefits. This materially constrained meaningful prioritisation with HAL to maximise outcomes for consumers, as key elements of the plan such as business cases lacked sufficient scope definition, clarity and a link to overall consumer benefits. These concerns were reflected in the Independent Reporter's reports of the CE process and in airline community correspondence to the CAA dated 27 May 2025, 13 October 2025, 30 January 2026 and 5 March 2026. These issues have subsequently recognised by the CAA in its Initial Proposals, which identified significant weaknesses in HAL's Business Plan rating it as "low quality".

10.11. The lack of sufficient detail required the CAA to request substantial additional information from HAL through its Q&A process to complete its needs assessment. Despite this, material information gaps remained, with some projects lacking sufficient evidence to be fully assessed. Airlines have not had visibility of this additional information.

10.12. As part of its response to the Initial Proposals, BA expects HAL to submit additional information and potentially material revisions to its July 2025 Business Plan. Clear guidance from the CAA is therefore required on how such information will be treated. **The CAA should apply a very high threshold for the acceptance of any new material**, ensuring that it is proportionate, subject to full scrutiny by airlines, and demonstrably in the interest of consumers, including in terms of affordability.

10.13. HAL should not be allowed to benefit from prior shortcomings in transparency or from any form of regulatory gaming. Acceptance of substantive late submissions would risk undermining the integrity of the process, bypass structured scrutiny and reintroduce projects previously rejected due to insufficient evidence (for instance, through a confusing narrative on asset maintenance) to the detriment of consumers. Accordingly, any late submissions should be limited to narrow clarifications with clear consumer benefit that airlines can meaningfully assess and respond to. The airline community set out these concerns in its letter to the CAA dated 20 May 2026. We have set out our concerns and proposed safeguards in the section on Constructive Engagement and H8 Business Plan above.

10.14. **The CAA should therefore be cautious in increasing the size of the envelope in its Final Proposals.** The application of other assessment criteria, including its approach on Deliverability and Efficiency, must continue to act as constraints to ensure that the overall envelope remains proportionate and reflects an efficient level of costs.

10.15. Regardless of any additional project-specific information, the CAA sets an overall envelope within which HAL and the airlines agree a prioritised portfolio of projects for assessment and delivery. We support the CAA's decision not to mandate a

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project list, preserving flexibility for stakeholder-led prioritisation within the established envelope during the price control.

10.16. A constrained capital envelope must require HAL to engage continuously with airlines to prioritise which projects are progressed, while ensuring sufficient headroom across all years for safety, compliance and asset maintenance to protect consumers.

Our support to the CAA's approach to setting the capital envelope

10.17. **BA firmly supports the process employed by the CAA to set the capital envelope for H8**. We recognise that H7 was the first quinquennial period with a fixed cap, and this has been useful throughout H7 to focus the prioritisation of capital spend. We therefore support the concept of a capex envelope with a fixed cap continuing into H8.

10.18. We also support the CAA in setting the envelope **but not mandating the projects** that should be delivered within that envelope. This enables the airlines and HAL to work together through the regulatory period to continuously prioritise the projects to be delivered within the portfolio, maintaining flexibility to respond to changing circumstances, needs and technology advances. Mandating a list of projects at this stage (based on a HAL Business Plan from July 2025) would not be beneficial nor in the interests of the consumers.

10.19. However, **this process is only effective if HAL works with the airlines to initially agree the portfolio, and then to regularly review and reprioritise it.** The airlines today, do not get visibility of the projects that HAL are initiating internally, and are often unaware of work in progress until a P2T gateway. The programmatic approach was supposed to provide this portfolio overview and visibility and enable richer conversations. However, over time the portfolios across the programmes have deviated from that originally agreed at the P2 gateway and hence the airlines are not aware of projects in the early stages of discussion and development. Conversely, other projects that the airlines had understood to be progressing, have been deprioritised with no work planned. If the project list is not to be mandated and controlled by the CAA, the scope must be agreed between HAL and the airlines from initial identification of a business need through to delivery. The Q6 G0 and G1 gateways in the Heathrow Gateway Lifecycle used to do this effectively and the airlines request that these be re-introduced.

10.20. It is critical that the airlines are part of the prioritisation of the complete project portfolio, ensuring the business need is understood before any work commences. This is particularly important under a constrained capital envelope. If the airlines do not have visibility of a project until later in its development, any challenge will result in rework and hence inefficient spend.

10.21. BA recognise that the CAA's proposed capital envelope is similar in size to that proposed in the airline Alternative Business Plan. At an overall level, the airlines followed a similar approach to the CAA in setting the envelope. Specifically, the airlines categorised at a project level, prioritised the categories and applied a

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constraint based on an assessment against historical capability and capacity. The airlines sense-checked that its proposed £5.5 billion envelope enabled Asset Maintenance and Compliance delivery at an equivalent rate to H7, enabled large projects to be delivered, as well as delivering multiple initiatives for customer and operational performance.

10.22. We nevertheless note that the CAA's approach is more granular, as would be expected given that the CAA benefitted from significant further follow up clarifications with HAL.

10.23. A capital envelope range of £5.5 billion to £6.1 billion proposed by the CAA is not a modest cap on capex. In a two-runway environment it enables significant annual expenditure on safety, compliance, asset maintenance, resilience and capacity initiatives, and enables the delivery of benefits to both the consumer and the efficiency and resilience of the operation.

10.24. HAL has suggested that airlines are seeking to deliver its £10 billion envelope proposed in its Business Plan within a £5.5 billion envelope. This is not the case. Airlines recognise that within a constrained capital envelope, and within the physical constraints of the airport, difficult prioritisation decisions are required. This inevitably means that some projects, despite delivering benefits to consumers or operations, cannot be progressed within H8, as would be the case in any commercial environment.

10.25. Similarly, the CAA's methodology for defining the capital envelope was transparent, predictable and appropriately consulted on with both airlines and HAL. This reflects the requirements of any capital planning process, where investment must be prioritised on the basis of deliverability and affordability. The CAA has provided clarity on its approach and delivered it in a consistent and predictable manner.

10.26. **BA therefore supports the proposed size of the capex envelope (mid-point of £5.8 billion 2024 CPIH) and the process followed by the CAA to determine it.**

Scope adjustments

10.27. The CAA has clearly set out the investments proposed in HAL's Business Plan that it has excluded from its Needs Assessment. We have the following comments on the specific scope adjustments.

a. Terminal 5 (T5) Capacity Optimisation

10.28. In contrast to the CAA's view, BA does not consider T5 Capacity Optimisation "Phase 2" to be an expansion-related project, but rather part of the two-runway Masterplan. The programme is no longer proposed to be delivered as set out in HAL's Business Plan and is instead being consolidated into a single phase with Phase 1, which has been prioritised within the H8 envelope, to enable more efficient delivery of the required infrastructure changes.

10.29. The programme is intended to deliver key improvements to the resilience, customer experience and operational performance of Terminal 5, through enhanced utilisation of existing assets and targeted developments to improve capacity and system robustness.

10.30. BA therefore supports the prioritisation of (the scope previously defined as) Phase 1 and Phase 2 of T5 Optimisation within the capex envelope.

10.31. In the first instance, this program should be included within the capex envelope, but If the CAA decides to increase the envelope at Final Proposals, and without prejudice to our comments about maintaining the capital envelope of £5.8 billion defined in the Initial Proposals, BA considers that any such adjustment should be tightly targeted and justified, with priority given to T5 Optimisation.

b. Modernising Heathrow DCO, Enabling Works and Ancillary Projects

10.32. In contrast, BA supports the removal of these elements of the Modernising Heathrow programme from the H8 portfolio, as they are directly related to the expansion of Terminal 2, including the construction of a new satellite building.

c. Noise and Vortex

10.33. As set out in the operating costs section, BA supports the removal of noise and vortex costs from capex to opex, provided this is accompanied by robust safeguards. In particular, allowances should be linked to clearly defined outputs with appropriate mechanisms to address under-delivery, and further work is required to establish a governance framework ensuring effective oversight, cost control and delivery discipline.

Needs assessment

10.34. BA strongly supports the CAA's requirement for a clearly defined needs assessment and a quantified benefits case for each project, to ensure that only those projects with a robust and evidenced case are included within the H8 portfolio.

10.35. This approach provides a clear and structured methodology for airlines to adapt to assess HAL's projects during H8. We propose that a consistent set of evaluation criteria and standards be developed and agreed with HAL to support this assessment.

10.36. We recognise that the airlines did not provide the CAA with any pre-G3 supported projects. This was the result of insufficient information in HAL's Business Plan which did not enable airlines to assess key elements such as scope, options, costs and quantified benefits with confidence.

10.37. As discussed in Constructive Engagement there are a number of objectives or principles on which we will find alignment with HAL, however, we are unable to firmly state our support for specific projects at this stage. We also note that the CAA has been able to reach a more developed assessment on some projects even after

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having access to additional Q&A information from HAL that was not made available to airlines.

10.38. The inability of airlines to support specific projects at this stage reinforces the need for a structured and ongoing governance process, whereby HAL is required to review, consult and agree the overall portfolio with airlines at the outset of, and throughout, H8, including any additions or removals.

10.39. As outlined in the Round 1 of Constructive Engagement and again in the Airline Alternative Business Plan, our priority themes for investment are:

i. Consumer: A high-quality and well-functioning airport experience throughout the passenger journey: a predictable, punctual and reliable journey while ensuring value for money.

ii. Affordability: Provide services to passengers at an efficient cost. Create headroom in charges to support priorities while reducing cost of operating at Heathrow.

iii. Resilience: Stable platform with problem areas proactively mitigated, impacts minimised and prompt recovery. Agreed resilience levels by design.

iv. Infrastructure & Capacity: Ensure infrastructure is fit for purpose. Unlock capacity by balancing growth and operational robustness.

v. Sustainability: Enable targeted initiatives within HAL's control to bolster decarbonisation: cost and waste reductions, airline operational improvements and net zero targets.

Asset Management & Compliance

10.40. We are supportive of the CAA's prioritisation of safety, mandatory, critical compliance projects, and agree with the CAA that these should be prioritised in the highest category.

10.41. We note that the CAA's consultants, Steer, were unable to clearly prioritise and score all of the Asset Management and Compliance projects. HAL did not provide a Corporate Risk Factor (CRF) score for all projects which is the mechanism by which HAL prioritise the need. We note for instance:

i. BC03.01 – *"Out of the 107 projects which have not passed G3 [...] HAL provides CRF scores for 44 of them and doesn't provide CRF scores for 63 of them"*[46].

ii. BC04.00 – *"For technology assets, no CRF score or similar measure have been provided [...] technology assets are not prioritised based on the CRF score but on asset life [this] has not been provided"*.[47]

[46] See Steer report for the CAA on H8 capital prioritisation, paragraph 2.41.
[47] See Steer report, paragraph 2.78.

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10.42. BA sought to understand from HAL the breakdown of its Asset Maintenance and Compliance portfolio between safety-critical or mandatory scope and more discretionary, risk-based projects. This split was not provided during Constructive Engagement for discussion. While HAL shared a project-level dataset on 18 May 2026, this constituted a reissue of its July 2025 Business Plan and was submitted too late to allow for meaningful review or consideration within this response.

10.43. We are nevertheless concerned over HAL's perverse incentive to create a confusing narrative on asset maintenance in an attempt to request an increase of the capital envelope without proper consultation – for instance by providing a confusing narrative between safety critical and discretionary risk-assessed asset replacements.

10.44. We recognise and support that the Asset Management and Compliance portfolio requires continuous prioritisation throughout the period, to ensure that the highest priority assets are worked. We therefore support HAL focussing on the highest priority assets in need of repair, replacement or upgrade. However, this process is managed by HAL and should operate within a defined allocated budget, subject to assurance and scrutiny, for which targets and prioritisation are key.

10.45. BA notes that the CAA's proposed annual spend on Asset Management and Compliance is broadly aligned with the forecast outturn for this category for 2026.

Terminal occupancy

10.46. The Occupancy Infrastructure business case (BC11.00) received a sufficiently high needs score to be included within the CAA's capital envelope. While we recognise that the CAA is not mandating specific projects within that envelope, BA considers that there is a risk of consumer harm and perverse incentives if HAL were not to proceed with this initiative.

10.47. HAL has stated during Constructive Engagement that the terminal occupancy programme is expected to increase Heathrow capacity by [REDACTED] passengers per annum over H8. Indeed, BA strongly supports this initiative, although we consider that it could be delivered through a simpler and more cost-efficient solution than that proposed by HAL in its consultation last year.

10.48. [REDACTED]

10.49. Failure to deliver this investment would constrain growth and could trigger the Traffic Risk Sharing (TRS) mechanism due to lower outturn passengers, creating a perverse incentive whereby HAL could benefit financially from a decision that restricts airline growth at the consumer's expense.

10.50. It is therefore critical that HAL does not benefit from delaying high-priority capacity improvement projects, as identified by the CAA, including through passenger forecast adjustments or TRS protections. Such an outcome would undermine the integrity of the regulatory framework, allowing HAL to pass through

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the consequences of its own non-delivery to consumers, resulting in reduced capacity, weaker operational performance and a deterioration in customer experience. We address these risks, including appropriate remedies, further in our response on the TRS mechanism in the financial framework and WACC chapters of our response.

Deliverability assessment

10.51. We are firmly supportive of the CAA conducting a deliverability assessment to create realistic boundaries within which to set the cap. The methodology was transparent and clear even if at a high-level. The CAA have set a range within which it is deemed that the deliverability risk to be both manageable and acceptable to the consumer.

10.52. This is a key consideration when delivering significant investment within a live, capacity-constrained operational environment. While initiatives such as off-site construction can help mitigate disruption, the impacts on consumers, operational resilience, the supply chain and wider facilities must be carefully assessed and managed to ensure any adverse effects are justified.

10.53. It is therefore critical that this forms part of the overall evaluation, to protect consumers from the cumulative disruption arising from multiple parallel projects impacting service levels and operational performance.

10.54. BA recognises that H8 will likely run in parallel with early enabling works for expansion, which will introduce additional constraints not only in terms of site access and geography, but also across critical resources such as materials, HAL capability and its supply chain. The CAA should take these cumulative pressures into account in its assessment of deliverability and disruption.

10.55. In addition, HAL's Business Plan does not include certain extensive commercial property projects, which, if subsequently brought into the portfolio, would place further pressure on supply chain capacity, resourcing and materials. This reinforces the need for a holistic deliverability assessment in defining an appropriate capex envelope.

10.56. If, at Final Proposals, the H8 envelope is set at the upper end of the deliverability threshold, BA will require clarity on how the CAA has assessed the resulting risks to the consumer experience across the Heathrow campus, including the cumulative impacts of H8 investments, potential commercial property developments and early enabling works for expansion.

10.57. BA further supports the CAA's assessment recognising the proposed step-up in capital expenditure in Year 1 of H8 and agrees that such a profile is not deliverable. A sharp increase in spend over a single year risks inefficiencies, as multiple projects would need to be initiated in parallel, placing pressure on resources, supply chains and operational delivery.

Efficiency assessment

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10.58. We note that the CAA's assessment of the efficiency of the proposed projects through its consultants' benchmarking assessment resulted in alignment with HAL's forecasts after the assumed efficiency percentage had been applied. However, the efficiency percentage proposed in HAL's Business Plan will not be traceable through the project lifecycle in the absence of a mandated project portfolio. As stated above, we do not support the CAA mandating specific capital projects.

10.59. The assessment does not consider how HAL's cost estimates have historically evolved from initial forecasting through to G3 approval and eventual outturn. This cost evolution is critical to assessing the credibility and efficiency of HAL's estimates at this stage.

10.60. BA considers that further assurance is required on the suitability and robustness of risk allowances applied across the H8 portfolio. As highlighted in Steer's report "*[f]or H7, HAL's approach to risk management was reviewed by the Independent Fund Surveyor (IFS), which concluded very positively on the approach. However, the review did not seem to cover whether the risk allowances in HAL's cost estimates when projects are still in design development were appropriate or not.*"[48]

10.61. The benchmarking activity undertaken by Steer is an example of the detailed independent assessment that should be undertaken at G3 for each project, to provide guidance as to whether the proposed cost plan is appropriate.

Capex – Summary and recommendations

10.62. **BA supports the proposed size of the capex envelope (mid-point £5.8 billion in 2024 CPIH) and the approach followed by the CAA in determining it.** The CAA's methodology, including the needs assessment, was transparent, predictable and appropriately consulted on, with a clear focus on consumer benefit. It is also set within the context of deliverability to ensure that the scale of investment is feasible within a live, capacity-constrained environment, including alongside early expansion works. The resulting framework appropriately drives prioritisation within an envelope that is affordable and deliverable.

10.63. Based on our analysis above, we recommend that the CAA:

i. Maintain the proposed capex envelope (mid-point of £5.8 billion in 2024 CPIH), ensuring it remains aligned with deliverability constraints, historical run-rate and consumer affordability.

ii. Retain the base framework for capex assessment, including robust needs assessment, quantified benefits and a clear "golden thread" linking investment to consumer outcomes. A strict approach must apply to business case quality, ensuring that no project is included without sufficient evidence on scope, options, costs and benefits.

[48] See paragraph 4.41 of Steer report.

iii. Ensure that HAL does not benefit from information asymmetries by requiring full transparency and limiting the weight given to new information submitted late and not subject to airline scrutiny. The CAA must apply a very high threshold to any late submissions by HAL, limited to narrow clarifications with clear and demonstrable consumer benefit.

iv. Avoid increasing the overall capex envelope unless strictly justified and tightly targeted, with any adjustment constrained by deliverability and affordability considerations.

v. Maintain the principle of setting an overall envelope without mandating specific projects, preserving flexibility for joint airline-HAL prioritisation.

vi. Strengthen arrangements to ensure continuous airline involvement in portfolio prioritisation, including early-stage visibility and ongoing reprioritisation of projects, from initial identification through to delivery.

vii. Reintroduce G0 and G1 gateways to ensure visibility and airline engagement early in scope definition phase of the project lifecycle.

viii. Prioritise investment in safety, compliance, asset maintenance and resilience, ensuring sufficient headroom is maintained across the H8 period, recognising the continued allowance of similar run-rate allowed in H7 and ensuring a clear distinction between safety-critical and discretionary scope.

ix. Prioritise T5 Optimisation (previously called Phases 1 and 2) within the capex envelope to deliver efficiency, customer, resilience and capacity benefits.

x. Maintain the exclusion of expansion-related projects (including T2 satellite works) from the H8 portfolio.

xi. Reclassify Noise and Vortex costs from capex to opex, subject to robust output-based safeguards and strengthened governance arrangements.

xii. Ensure that high-priority capacity projects, such as Terminal Occupancy, are progressed and not delayed, to avoid creating perverse incentives under the TRS mechanism.

xiii. Prevent HAL from benefiting financially from non-delivery of capacity-enhancing projects, including through adjustments to passenger forecasts or TRS protections.

xiv. Maintain and strengthen the deliverability assessment framework, taking into account cumulative disruption, operational constraints and supply chain capacity.

xv. Ensure that the envelope appropriately reflects the cumulative impact of H8 investment, expansion enabling works and potential additional projects.

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xvi. Strengthen efficiency assessment by reviewing historical cost evolution (from initial estimates through G3 to outturn) and improving the traceability of efficiency assumptions.

xvii. Provide further assurance on the appropriateness and robustness of risk allowances embedded in project cost estimates.

xviii. Ensure that independent benchmarking is consistently applied at key project approval stages to validate cost assumptions.

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11. Capital expenditure: Incentives & Governance

BA considers that **the current capital governance framework is not fit for purpose and that the CAA's Initial Proposals lack ambition**, and do not adequately address its structural weaknesses, **relying too heavily on the existing H7 model despite clear evidence of its shortcomings**.

While BA supports the principle of ex-ante scrutiny and the continuation of stage-gated processes, the current framework is undermined by **late airline involvement, persistent information asymmetry, weak delivery incentives and insufficient independent assurance**, which together limit effective challenge and allow inefficient or poorly justified projects to progress.

We remind the CAA that **our advocacy for regulatory reform predates the renewed focus on Heathrow expansion**, and we call for a **comprehensive approach instead of restricting reforms to expansion-related matters only**.

BA emphasises that these deficiencies are compounded by **weaknesses at the portfolio level**, including the **absence of a transparent and airline-endorsed prioritisation framework, insufficient visibility over the full programme of investment, and limited ability for airlines to influence which projects are initiated or progressed**.

The programmatic approach adopted in H7 has further **reduced transparency and control**, with **governance processes not consistently applied in practice**, including instances of projects progressing ahead of formal approvals or being reshaped through change mechanisms.

Without fundamental reform within the H8 settlement, there is a **material risk that the significantly larger capital programme will be delivered inefficiently**, with inadequate cost discipline and misaligned incentives ultimately borne by consumers. BA therefore calls for a step change in governance. The CAA must not let the opportunity to implement significant reform H8 pass us by. To do so would be a clear failing by the regulator to the detriment of consumers.

We set out our proposals **for earlier and structured airline engagement, full portfolio transparency and dynamic prioritisation, genuinely independent and decision-grade assurance, stronger delivery incentives focused on outcomes, and formal pause and escalation mechanisms** to deal with disputes or major concerns at project lifecycle stage gates.

Our objective is for the capital governance process to guarantee that capital investment is efficient, justified and aligned with the interests of users, ahead of **potential bolder reforms for expansion such as the airlines' request for a Capital Investment Committee** to oversee and approve major capital investment at Heathrow.

Issues with the current capital governance processes

11.1. BA supports the continuation of the ex-ante assessment of capital introduced in H7 as a proportionate mechanism to scrutinise investment and protect consumers.

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11.2. However, there are fundamental weaknesses in the current capital governance framework, as highlighted consistently through Constructive Engagement and in responses from BA, IAG, Heathrow Reimagined, and the wider airline community to the CAA's consultations on the reform of Heathrow's regulatory framework. These issues risk undermining effective cost discipline and the credibility of the existing capital governance process.

11.3. Given our position, it is not realistic to expect airlines to agree improvements to existing governance processes with HAL. There is a fundamental divergence in views on the nature and extent of required reforms, compounded by a clear power asymmetry, meaning that engagement alone will not deliver meaningful change. The CAA should therefore set these requirements directly, rather than relying on airlines to influence outcomes through bilateral processes.

11.4. While the development of the ex-ante capital governance handbook for H7 was undertaken jointly with HAL, the agreed processes have not been delivered as intended and the expected benefits have not been demonstrated.

a. Portfolio oversight

11.5. Airlines do not have access to a comprehensive live portfolio view or sufficient supporting data to influence decisions early, limiting effective oversight and prioritisation. Airlines only received a list of the full portfolio on 25 April 2026 after months of requests and challenge and only in the final year of H7. Previous disclosures have been limited to partial and selective subsets of the overall scope. For the first time, this portfolio includes the full scope of investment from early-stage P2 concepts through to projects already in-flight.

11.6. This is not acceptable – the full portfolio should be maintained as a live, transparent document, regularly shared and discussed with airlines to enable the prioritisation of the portfolio as well as assess new and emerging requests and requirements for inclusion. It should include potential, paused and stopped scope alongside live in-flight projects.

11.7. The visibility gained from the full portfolio list has highlighted:

i. Projects that were identified at P2 that have not been progressed and subsequently removed from the portfolio with no rationale or engagement e.g. [REDACTED].

ii. New scope that has been initiated, that was not in the baselined P2, which we may or may not support, but were not part of the prioritisation process.

iii. Projects where a unilateral decision was taken to stop the project, e.g. [REDACTED].

iv. Other projects that continued, even after airlines stated their non-support (e.g. [REDACTED]).

This lack of transparency undermines airlines' ability to influence the portfolio as a whole, how projects are delivered or sequenced, identify synergies, but also to ensure robust need and benefits cases are in place before costs are incurred.

11.8. There is no current process by which HAL must engage airlines on the content of the entire portfolio, or the prioritisation through which new projects are added to this portfolio and work started. This needs to be strengthened in Final Proposals – mandating visibility, recognising that a limited look-ahead to upcoming G3 decisions is insufficient as it comes too late in the process to meaningfully influence outcomes for the consumer. The lack of a comprehensive list of projects or scope in the pipeline or in-work, limits our ability to challenge and influence in a timely manner, reducing unnecessary work and cost.

11.9. As noted above, we support the CAA setting the overall capital envelope. However, there needs to be a licence modification to mandate Heathrow to review the entire portfolio with the airlines on a monthly basis, including visibility of all scope in work, new requests to be prioritised and proposals for projects to be paused or stopped.

11.10. The programmatic approach in H7 has compounded this lack of visibility. Scope is only proposed at P2 stage, after which HAL retains full discretion to determine whether packages are progressed into future tranches, paused, or replaced with new initiatives.

11.11. Airlines have little influence over this process and what projects are prioritised and this needs to change for H8. The governance framework should require agreement on the portfolio of projects to be taken forward, with structured and earlier engagement so that airlines can meaningfully influence which initiatives are started, developed and advanced. This would improve prioritisation and minimise the risk of time and resources being spent on projects that will not have airline support.

b. Programmatic approach

11.12. The programmatic approach adopted by HAL for H7 has not enabled greater visibility of the entire portfolio but has instead reduced it. It has reduced transparency and effectiveness, has not improved stakeholder engagement, and has provided little clarity of benefit delivery. The removal of earlier lifecycle gateways has shifted decision points too late in the process, often after substantial spend, reducing the ability to challenge scope, need, or cost.

11.13. In particular:

i. P2 Business Cases have not been refreshed at every P2T gateway as initially intended. The substitute process of fixed P2 Refreshes was delayed and has proved to be ineffective in providing visibility of the evolution of the scope of the programme, its overall business case and the rational for scope decisions that had been made since P2.

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ii. Individual tranches have been set to extend beyond the end of H7, with only a few P3Ts planned to occur within H7. This weakens the opportunity for benefit realisation and lessons learned reviews.

iii. Projects named in the P2 stage have not always been progressed as expected: they may have been assessed and stopped, and other scope has been introduced to the programme without airline knowledge or engagement.

iv. Even when portfolio reviews have been conducted, airline feedback is not incorporated, and HAL continue to work on projects regardless of airline views.

11.14. The programmatic approach that HAL is looking to continue and expand into H8 does not therefore work for the airlines. It reduces visibility and governance at a project level, particularly where programmes are in reality portfolios of related projects. While there are exceptions, [REDACTED], others are a portfolio of related projects, either connected through benefit theme, geography, facility-type or solution type. Applying programme-level governance to a portfolio removes flexibility, transparency and control from an airline perspective.

11.15. We have requested to HAL that governance reverts back to the full Heathrow Gateway Lifecycle (G0 to G7) for these portfolios and that the programme gateways be only be maintained for true programmes ([REDACTED]). This does not prevent HAL from managing the delivery of their portfolio as programmes where efficient, but the application of the programmatic approach for effective governance of portfolios is unworkable.

c. Timely adherence to governance gateway approvals

11.16. Formal governance processes are being side-lined and will be applied retrospectively in some instances, undermining the integrity and validity of the approval process. A lack of adherence to the agreed governance framework undermines the ability for projects to be fully assessed and assured as value for money and beneficial to the consumer.

11.17. Significant projects such as [REDACTED] are being progressed ahead of formal gateway approval including visibility of the latest cost estimates. [REDACTED].

11.18. The governance approval gateways are there to ensure the need has been properly articulated, options assessed, proposed solution fully designed and costs and delivery assured. Treating the governance process as an add-on rather than integral to the delivery of capital projects prevents robust assessment on behalf of the consumer.

d. Project and financial commitment before governance approval

11.19. Significant financial commitments should only be made once governance approval (G3 DEV to CORE) has been secured. Governance approvals should not be driven by pre-committed contract signature dates.

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11.20. This was experienced with [REDACTED].

11.21. It is assumed that this is not a one-off; however, this change in process has not been discussed or agreed with the community.

11.22. In principle, no significant financial commitment or contract must be made before G3 approval. Enhanced assurance from project initiation through to delivery would provide visibility and ensure governance was properly followed.

e. Additional major scope being classified as change control

11.23. HAL are seeking to add new (albeit related) scope as change requests to existing projects rather than raise as new projects. [REDACTED]. This reduces governance scrutiny, avoids IFS assurance, extends the original project delivery dates and scope and hence resets the agreed Delivery Obligation for the original scope.

11.24. These requests are outside the remit of what is reasonably classified as changes to the scope of an approved project.

11.25. All major scope additions and changes must require a new project to be raised, that can be fully assured and with an associated Delivery Obligation. Project Governance must be independent of contracting processes and approvals.

f. Independent Assurance and Delivery Obligations

11.26. While we agree with the principle of the ex-ante process, in the absence of stronger independent assurance airlines are unable to validate the robustness of the business case presented.

11.27. Any future assurer must be truly independent, and its remit must cover business need, proposed solutions and scope requirements and the ability to challenge and validate value for money, effectively replicating the role of an internal finance function in a competitive organisation.

11.28. Delivery Obligations are not working in the way CAA envisaged. Timelines are not challenging, and HAL is largely insulated from any delivery risk – [REDACTED], with the resulting risk ultimately borne by consumers.

11.29. Issues with the current framework, including the treatment of change requests, the definition of outputs versus outcomes, and the timing of key decisions, collectively raise concerns that the ex-ante regime is not operating in line with the "fair bet" principle, and is being applied in a way that weakens effective challenge and accountability and may be indicative of regulatory gaming.

11.30. Indeed, [REDACTED].

11.31. There remain fundamental challenges in the calibration of Delivery Obligations, particularly in the definition of key outputs and outcomes. HAL further seeks to mitigate its risk exposure by disaggregating output categories into individual

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elements rather than applying a pass/fail assessment, even where all elements are required for successful project delivery.

11.32. Lack of visibility over supplier contract terms, particularly in relation to risk allocation, limits airlines' ability to challenge the overall business case and how the subsequent Delivery Obligations are structured. Our request for a strengthened, multi-layered Independent Assurance function would help address this by supporting more effective validation of proposed Delivery Obligations.

11.33. Given that Delivery Obligations are still relatively new, the airlines request a CAA-mandated review of the process during H8 when more projects have completed the process. Support from the CAA is required to ensure that robust Delivery Obligations are set against an assured business case.

11.34. Similarly, the treatment of outperformance is in our view not justified: it is unclear why the 25% bonus is retained on a permanent basis through additions to the RAB, where it continues to earn a return at the allowed WACC plus inflation indexation without a reset in subsequent periods.

The CAA's proposed minor refinements are insufficient

11.35. While we strongly endorse the overall cost envelope proposed by the CAA, BA disagrees with the lack of meaningful proposals on capital governance reform. The Initial Proposals largely retain the H7 framework, relying on airline scrutiny through Gateway (G) processes supported by an Independent Fund Surveyor (IFS) (for major investments only), alongside Delivery Obligations (DOs) and associated penalties and bonuses. The CAA considers these mechanisms to be broadly adequate, proposing only limited refinements, such as adjustments to DO thresholds and the continuation of ex post reviews based on the Demonstrably Inefficient or Wasteful Expenditure (DIWE) standard, while deferring any substantive reform to a later, separate workstream likely linked to expansion.

11.36. BA strongly refutes that minor refinements are sufficient. The current capex governance framework is not fit for purpose and exhibits fundamental structural weaknesses that are not addressed in Initial Proposals. We set out our concerns below.

11.37. **Late airline involvement:** The current model, and specifically the programmatic approach adopted by HAL in the H7 period, does not provide airlines with comprehensive oversight of how the capex portfolio is being managed, and specifically, visibility of new projects being initiated or actively been worked on by the HAL teams. Project scope is proposed by HAL at the Phase 2 Tranche stage and then formulated into projects with no early engagement with airlines. As a result, significant time and indeed cost has already been invested before any meaningful engagement with airlines on the need, potential solutions and/or proposed scope. Later in the process at the G3 stage (business case approval), this issue is compounded because of insufficient engagement, and pre-commitments to suppliers ([REDACTED]). This situation effectively creates a "take it or leave it" decision point. This is too late for meaningful challenge: by G3, HAL has typically

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have locked in scope, design and procurement, leaving airlines faced with approving projects or risking delay and cost escalation. The Initial Proposals do not address this deficiency. BA's position is that H8 must provide for earlier and substantive airline engagement, throughout the lifecycle, on project scope and option selection to avoid fait accompli outcomes.

11.38. **Information asymmetry and transparency:** H7 experience demonstrates that HAL retains control of information. Airlines continue to receive large volumes of material that are incomplete, poor quality, often lacking sufficient cost breakdowns, credible alternatives assessment and robust benefit analysis, materially constraining informed scrutiny and decision-making. The Initial Proposals' reliance on HAL's discretion to share information is not sufficient to address this imbalance. BA's position is that H8 must embed stronger transparency requirements, including the early provision of full project-level information and clear portfolio-level visibility linking capex decisions to the RAB and the resulting impact on charges.

11.39. **Delivery Obligations (DO) weaknesses:** The H7 DO framework, intended to ensure timely delivery and accountability for outputs, has not operated as intended. In practice, HAL can (and has done so in H7) reset DO baselines through change control, weakening their effectiveness, while the framework remains focused on outputs rather than outcomes, providing no assurance that consumer benefits are delivered even where DOs are met. The Initial Proposals propose only limited refinements (for example, adjustments to materiality thresholds), which do not address these underlying deficiencies. BA's position is that H8 must refocus incentives on the delivery of outcomes — including demonstrable service improvements and cost efficiencies — truly independent assurance would provide enhanced confidence in the DO process for the airline community.

11.40. **Independent assurance and CAA role:** The Independent Fund Surveyor (IFS) does not provide genuinely independent assurance, given it is appointed jointly by, and accountable to, HAL and the airlines, and its remit is focused primarily on procedural compliance rather than value for money. The Initial Proposals largely retain this approach. BA's position is that the CAA should take a more direct and active oversight role in H8, including through the appointment of independent experts reporting to the CAA to scrutinise in a broader sense high-value projects, and/or the introduction of CAA observer roles within governance processes to intervene where there is disagreement between HAL and airlines.

11.41. Absent more substantive reform, the H8 capex envelope risks being delivered inefficiently under the current governance framework. BA's position is that capital governance reform must be embedded within the H8 settlement, rather than deferred to a separate workstream. We reiterate to the CAA that our calls for regulatory reform were made before the re-emergence of Heathrow expansion, and we therefore urge the CAA to adopt a holistic approach rather than confining improvements solely to expansion.

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Capital Investment Committee and "bridging" practical improvements for H8

11.42. The CAA's primary statutory duty under Section 1 of the Civil Aviation Act 2012 is to further the interests of users of air transport services, including in relation to the cost, quality, continuity and range of airport services. This duty directly underscores the need for robust capital governance at Heathrow. Where the investment framework permits inefficient or misdirected expenditure, consumers ultimately bear the cost through higher airport charges (and, in turn, airfares) or through weaker service quality and resilience. Conversely, rigorous capital governance is essential to ensuring that investment is necessary, well-spent, efficiently delivered and aligned with the consumer interest.

11.43. BA remains committed to the urgent transformation and reform of the regulatory framework at Heathrow. In our response to CAP3195 *Working Paper on Regulatory Models*, and in submissions from IAG (including through the Heathrow Reimagined campaign), we set out a comprehensive reform proposal centred on the establishment of an independent Capital Investment Committee ("CIC") to oversee and approve major capital investment at Heathrow.

11.44. This remains BA's firm position and long-term ambition. A CIC, comprising the CAA, airlines, independent experts and other stakeholders, would introduce robust external challenge and ensure that capital investment decisions are demonstrably aligned with consumer interests. By giving those who ultimately fund and depend on the infrastructure a meaningful role in decision-making, a CIC would materially reduce the risk of unnecessary cost burdens, suboptimal service outcomes and inefficient investment being imposed on consumers.

11.45. Our view is that much of the CIC model can be established through modifications to HAL's license without requiring new primary legislation, making it a realistic goal.

11.46. We recognise that H8 will commence in January 2027, leaving insufficient time for the full implementation of our complete reform agenda prior to H8 commencement. That said, this does not absolve the CAA of the obligation to pursue consumer-focused improvements now. As set out in CAA12, if aspects of the status quo risk harming consumers, the CAA must act to mitigate those risks to the extent feasible.

11.47. As such, we agree with the CAA's distinction between "H8 bridging" improvements and more fundamental reforms thereafter. However, we believe that the bridging proposals as set out CAA are a step in the right direction, they lack ambition and do not meaningfully address the challenges within the existing capital governance process as identified. Notwithstanding 11.49 below, our clear ambition is that the CIC should be operational from the start of H8, overseeing the H8 capital portfolio alongside the governance measures proposed below. The measures set out here are the governance enhancements necessary for the substantial capital programme commencing at the beginning of the H8 period in January 2027.

11.48. We also believe that CAA needs to ensure that any more fundamental reforms identified through its work on regulatory models can be implemented for H8. We remind CAA that our calls for regulatory reform pre-dated the re-emergence of

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Heathrow expansion and therefore we call for CAA to take a holistic view of reform as opposed to limiting reform improvements to expansion only.

11.49. While we will continue to champion the CIC and related measures as the best end-state solution, our focus for H8 is on practical, meaningful improvements to the capital governance process that can and should be made for H8. These interim measures will move significantly towards our desired future model, address known weaknesses in the status quo, and deliver more efficient, consumer-focused outcomes in H8.

11.50. We therefore welcome the proposals in the Initial Proposals seeking to improve capital governance, such as continued use of stage-gated approvals and oversight by the Independent Fund Surveyor (IFS). These steps indicate progress in principle. Nevertheless, serious shortcomings in the current system persist and must be remedied if consumers are to benefit from timely, value-for-money investment.

11.51. Under the H7 framework, HAL's incentives are not aligned with efficient delivery. In practice, HAL has been able to progress projects despite unresolved airline concerns and without sufficient scrutiny, reflecting its ability to work around existing governance processes. Airlines do not have effective formal levers to prevent or reshape proposed investments, even where these involve undue cost increases or overlook more efficient alternatives. While HAL may proceed "at risk" beyond stage gates without airline agreement, and such investments cannot enter the RAB without DEV to CORE approval, this occurs too late in the process to provide a meaningful opportunity to halt or redirect inefficient expenditure.

11.52. This imbalance allows projects to be approved despite clear and reasonable objections focused on efficiency or necessity, ultimately exposing consumers to avoidable costs. In one case raised with the CAA, HAL secured final approval for a major baggage programme at G3 stage despite outstanding airline concerns on cost and deliverability. The procurement timeline, and in particular the requirement to commit to contractor contracts, effectively compelled airline agreement on the T2 baggage system, given the disproportionate cost and schedule consequences of withholding approval. This example highlights a material weakness in the current regime, whereby airlines lack effective tools to meaningfully influence outcomes within the existing governance process.

11.53. Moreover, while the IFS has been a valuable source of expert input, the present IFS assurance mechanism is not truly independent. The IFS is effectively a consultant jointly appointed by HAL (the regulated company with a profit incentive in capex) and airlines, and there is limited transparency or accountability in how its recommendations are incorporated. HAL's profit incentive clearly dilutes the independence of the IFS. As a result, there is a risk that inefficient expenditure is not sufficiently challenged, undermining the economy and efficiency duties set out in CAA12. As highlighted in the airline community's May 2026 letter ("Effective Capital Governance and the Independent Fund Surveyor"), continuation of the H7 IFS arrangements into H8 would not be acceptable, and a strengthened assurance framework is required to improve outcomes.

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11.54. A further deficiency has been the lack of any formal requirement for airline consent or regulatory approval at crucial stages beyond the initial capital determination. Where airlines dispute a project's need, scope or cost, there is no mechanism to pause delivery pending resolution, allowing HAL to continue committing expenditure and leaving the CAA to address issues only retrospectively through potential cost disallowance. This reactive approach is not consistent with putting consumers first, as by the time inefficient spending is identified consumers will likely already be exposed to higher costs or delays due to inefficient investment. A more proactive safeguard is needed to ensure contentious projects are resolved or halted before money is spent. Currently, we rely on good will to ensure HAL adjusts plans in response to feedback. This has proven insufficient in practice. As a result, suboptimal investment choices, overly expensive scopes, weak "golden thread", or mis-prioritised projects are too often locked into the plan, with consumers bearing the cost of inefficiency.

11.55. HAL unavoidably holds far more information than airlines or the CAA on project options, cost drivers, and delivery plans. Under current processes, airlines have frequently been unable to receive complete and timely data as required to effectively scrutinise HAL's proposals (e.g. detailed breakdowns of cost, robust options appraisals, evidence of the "golden thread"). This lack of transparency limits effective challenge and risks suboptimal decisions, which can drive up costs or degrade service outcomes, at the consumer's detriment. This is not consistent with the CAA12 requirement for decisions to be evidence-based and targeted, which presupposes a sufficient degree of information symmetry between decision-makers.

11.56. We therefore call on the CAA to ensure that capital governance for H8 is materially strengthened relative to the current proposals. The H8 period encompasses a critical ramp-up in investment, including potential expansion-related expenditure as set out in the CAA's draft decision on CAP3201, and will be delivered against an uncertain macroeconomic backdrop. Robust governance arrangements are therefore essential to ensure that all capital expenditure is fully justified, efficiently delivered, and consistent with the CAA's primary duty to further the interests of consumers.

11.57. We propose four interrelated enhancements to the H8 capital governance framework. These measures are targeted, proportionate and directly address the consumer risks identified, while remaining consistent with the overall regulatory framework. Taken together, they represent a coherent and complementary package of reforms that would strengthen oversight and improve outcomes. For each proposal, we set out how it would support more effective scrutiny, ensure that investment is efficient and justified, and enable the CAA to better discharge its statutory duties to further the interests of consumers.

a. Prioritisation of the capital portfolio – aligning investment with strategy

11.58. In addition to strengthening project-level controls, the H8 capital governance framework should incorporate robust upfront prioritisation of the overall capital portfolio, with explicit airline engagement and endorsement. While the CAA sets the total capital envelope through the price control, further safeguards are required to ensure that capital within that envelope is allocated to projects that most effectively

serve strategic objectives and consumer interests. This requires moving beyond a bottom-up, HAL-determined project list towards a clearly prioritised portfolio, jointly scrutinised and aligned with Heathrow's long-term strategy and evidenced business needs.

11.59. We recommend that HAL be required to provide – and maintain on a rolling basis – a single, integrated project-level portfolio view of all potential and current capital projects. This integrated portfolio should be baselined and updated regularly, giving all stakeholders a shared, transparent view of the status, forecast cost, and schedule of each project, and how they collectively map to strategic objectives (such as safety, asset health, capacity growth, or decarbonisation).

11.60. To guide decisions within the portfolio, the CAA should mandate that HAL adopt a formal prioritisation framework with transparent criteria and standards. This framework would define how projects are assessed and ranked (for example, based on consumer benefit, regulatory compliance need, risk mitigation, and affordability) and how trade-offs are made when funding is limited.

11.61. Transparent criteria and scoring would enable airlines and the CAA to ascertain why one project is accelerated while another is deferred, ensuring that decisions are made in a structured, objective manner that furthers the interests of consumers. Moreover, prioritisation should not be a one-off exercise: it must be continuously applied throughout the project lifecycle. As projects evolve or external conditions change, the prioritised portfolio should be revisited (as business cases change) – including decisions on sequencing, acceleration, deferral or removal of projects – to always reflect what is most important for efficient passenger outcomes.

11.62. This dynamic approach would allow for the swift reallocation of effort and funds if a higher-value project emerges or if a planned scheme becomes less urgent, thereby maximising consumer value from the overall capital budget.

11.63. For these governance improvements to be meaningful, the process must incorporate formal airline endorsement of the prioritised portfolio. We ask that the CAA require HAL to seek and demonstrate airline agreement (or at least broad support) to the initial H8 portfolio prioritisation and any major updates to it. In practice, this could be achieved via the Capital Portfolio Board or a similar forum where airlines formally sign off on the ranked list of projects.

11.64. Such endorsement would confirm that those who use and fund the infrastructure consider the proposed investment plan to be appropriate, thereby providing legitimacy and assurance that consumer interests are being reflected. It also acts as an important safeguard against the risk of HAL unilaterally prioritising projects that serve its own commercial objectives while delivering limited consumer benefit.

11.65. Taken together, a transparent prioritisation framework and a requirement for airline sign-off would ensure that the capital programme is strategically coherent and clearly focused on delivering outcomes that matter most to passengers, consistent with the CAA's duties under CAA12 to promote efficient, demand-led investment and protect consumers from unnecessary costs.

b. Genuinely independent and empowered assurance leading to decision grade information

11.66. The CAA must substantially strengthen the independence and authority of the capital assurance function to ensure that decision-making is supported by robust, transparent, decision-grade information, with clear accountability for outcomes.

11.67. We propose that the assurer (whether continuing under the title of IFS or a new panel of experts) must be appointed, overseen and accountable directly to the CAA, with structured airline input, rather than operating effectively as a contractor to HAL. Governance arrangements must provide robust evidence to enable airlines to make informed decisions at each gateway, with materially greater accountability than today.

11.68. Assurance must operate as a multi-layered function spanning the full lifecycle of capital decision-making, planning, approval and delivery. This should include independent challenge and validation at portfolio level and, for individual projects, rigorous assessment of underlying need and requirements, scope and proposed solution, delivery approach and procurement strategy, design and technical specifications, robust business case, including quantified costs and benefits as a default and external benchmarking to test efficiency and value.

11.69. Governance and assurance outputs must be decision-grade, financially rigorous and directly usable in both regulatory and airline decision-making, underpinned by transparent, timely and consistently high-quality information to support informed choices at each gateway. Standalone business cases should demonstrate clear financial discipline, with quantified benefits and explicit assumptions as a default, while establishing a clear and traceable linkage between outputs, outcomes and benefits across the full project and asset lifecycle. Where material concerns are identified—such as costs being disproportionate to benefits, weak evidence of underlying need, or failure to adequately consider alternatives—projects must not be permitted to progress until those issues are satisfactorily resolved.

11.70. Greater transparency is required over contract strategies and commercial arrangements so that risks, assumptions and exclusions can be properly scrutinised. Competitive procurement should be the default, with independent assurance or audit of procurement processes to ensure value for money.

11.71. Committed benefits must be clearly defined at approval and tracked at project level through delivery and asset life, with enhanced, regular reporting to the CAA and airlines. This should include mandatory performance reporting against G3 commitments to ensure delivery of consumer outcomes.

11.72. This approach addresses the well-documented limitations of the H7 IFS and governance model and is essential for effective consumer protection in H8. Accordingly, the CAA should establish and administer a strengthened, layered independent assurance function with a broader remit and clearer authority, mandate independent procurement assurance and audit, require mandatory business case

performance reporting against G3 commitments, and develop enhanced, credible material consequences for HAL governance failures.

c. Continued reprioritisation of the portfolio

11.73. We propose that the H8 price control incorporates mechanisms to ensure airline engagement and approval during the evolution of the portfolio during period. As an example, if some budgeted projects are cancelled or deferred (due to evolving circumstances or better alternatives emerging), the regulatory framework should allow that capital to be either returned to consumers (via lower charges) or redirected to other high-value projects (subject to governance).

11.74. Such adaptability maximises the chances that capital in H8 is spent where it adds most value for users, rather than being locked into a predetermined list irrespective of changing needs. This approach aligns with the focus in CAA12 on meeting all reasonable demand (continuity and range of services) without imposing undue cost burdens. It also reflects regulatory best practice: being targeted and proportionate in interventions (CAA12 section 1(4)(b)), intervening (i.e. releasing funds) only when necessary and justified.

d. Formal escalation and 'pause' mechanisms

11.75. In addition to the above, we propose codifying a clear process to deal with disputes or major concerns at project lifecycle stage gates.

i. If airlines (representing collectively a substantial portion of Heathrow's traffic) or the independent assurer indicate that a project is not in consumers' interests, such as due to excessive cost, timing, or doubts about its necessity, then a "pause" should be triggered.

ii. During a pause, HAL would be prevented from incurring further significant capital expenditure on that project. The matter would be escalated to the CAA for review, potentially with input from a senior independent expert panel or the CAA Board itself, given the importance.

iii. The project would only proceed once the CAA is satisfied that issues are resolved and that moving forward is consistent with consumers' interests (and, if applicable, any conditions or modifications may be applied). Introducing this escalation mechanism ensures that consumer interest truly acts as a hard checkpoint in the process, not just a nominal consideration.

11.76. These safeguards would prevent situations seen in H7 where HAL could push ahead and effectively create "sunk cost" pressure on the regulator on projects that the airlines have already expressed their non-support.

11.77. By resolving issues upfront, the CAA can prevent inefficient spending before it happens, which is the best way to protect consumers (far better than trying to claw back costs later). This measure is a practical expression of the regulator's duty to act

pre-emptively in consumers' interests, ensuring that if conflicts between stakeholder views occur, the CAA steps in decisively on consumers' behalf.

11.78. The current framework places cost and risk exposure predominantly on consumers, with limited accountability or incentives on HAL for non-compliance.

e. Summary

11.79. We are very confident that the above proposals are achievable within the H8 timeframe and are tightly aligned with the CAA's statutory responsibilities. They do not undermine HAL's ability to invest, rather they ensure HAL invests in the right things, at the right cost, at the right time. We acknowledge that these measures fall short of our ultimate CIC vision, but they are critical stepping-stones that will substantially improve outcomes in H8 itself. Indeed, failing to implement these changes would, in our view, leave the H8 governance framework incompatible with the CAA's primary duty, given what we now know about the weaknesses of the current approach.

11.80. As a reminder to the CAA, our push for regulatory reform began prior to the return of Heathrow expansion, and we therefore request a broader, system-wide view of reform rather than one limited to expansion.

11.81. To summarise how our proposals address specific consumer risks, the table below outlines each key issue in capital governance, the current state (and associated risk to users), and our proposed solution with its consumer benefit and statutory rationale.

Our proposed solutions for H8 capital governance

H7 Governance failure	Description and identified consumer risk	Proposed H8 solution
Lack of prioritisation approval by airlines of the capital portfolio – aligning investment with strategy	The capital portfolio is currently driven by HAL through a bottom-up approach without robust, transparent prioritisation or formal airline endorsement, creating a risk that investment decisions are misaligned with strategic objectives and do not maximise consumer value	Introduce a transparent, CAA-mandated, and recurring prioritisation framework supported by an integrated, dynamic portfolio view and formal airline sign-off, ensuring capital is continuously allocated to the highest-value projects aligned with strategy and passenger outcomes. Reintroduce G0 and G1 gateways.
Assurance not truly independent	The current capital assurance model lacks true independence, authority, and rigor, resulting in insufficiently robust, transparent, and decision-grade information to support	Establish a CAA-led, fully independent and empowered multi-layered assurance function—spanning portfolio to project level—with strengthened governance, mandatory

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H7 Governance failure	Description and identified consumer risk	Proposed H8 solution
	effective governance and protect consumer interests	procurement and business case scrutiny, and clear accountability to ensure decisions are based on high-quality, financially rigorous evidence.
No oversight or approval by airlines of capital portfolio during regulatory period.	The H8 framework risks locking capital into a fixed portfolio without sufficient flexibility or airline oversight, potentially leading to inefficient allocation that fails to reflect evolving priorities or maximise consumer value. Programmatic approach has not worked for portfolio-type programmes for the airlines; it has not delivered expected transparency or engagement.	Introduce mechanisms enabling dynamic portfolio adjustment with airline engagement—allowing funds to be reallocated to higher-value projects or returned to consumers where appropriate—to ensure capital is deployed efficiently and aligned with changing needs.
Information asymmetry & poor transparency	Limited sharing of information as HAL controls information on project costs/option. This risks suboptimal decisions due to missing scrutiny, leading to excess costs or mis-prioritised investments that hurt service quality.	Obligations on transparency must be strengthened, such that HAL must share full business cases, breakdowns, benchmarks at each stage. This enables informed challenge which prevents wasteful spending, aligning with consumers' interest in fair charges and ensuring projects indeed improve service quality and resilience.
Lack of formal pause/escalation of disputes until it is too late	The absence of early stage and frequent formal escalation and pause mechanisms allows HAL to progress projects despite material airline or assurance concerns, creating sunk cost pressure and exposing consumers to inefficient, misaligned, or unjustified capital spend	Introduce a codified pause and escalation process triggered by airline or independent assurance concerns, empowering the CAA to halt projects at stage gates until issues are resolved and ensuring only investments demonstrably in consumers' interests proceed

11.82. Interim governance reforms are not discretionary enhancements but necessary measures for the CAA to fulfil its primary duty to consumers during H8. By adopting this package in the H8 Final Proposals, the CAA will strengthen the incentives and checks around Heathrow's capital programme in a way that delivers more efficient

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investment, more accountable decision-making, and better outcomes for passengers.

11.83. This will establish a strong foundation heading into H8, ensuring that consumers will benefit from needed projects delivered at lower cost and improved quality, while enhancing confidence in the regulatory framework. Looking beyond the start of H8, the experience gained from these measures will provide a clear pathway for all parties to prepare for the eventual introduction of a full CIC or similar enduring reforms, further progressing capital governance to a model fully aligned with consumer interests and the requirements of CAA12.

11.84. We note that these H8 governance proposals are fully complementary to the four regulatory models shortlisted in the CAA's CAP3251 consultation on the shortlist of regulatory models for Heathrow and are deliberately model agnostic. Regardless of whether the CAA ultimately pursues incremental improvements to the existing RAB-based framework, notably competitive delivery elements or an alternative developer model, the near-term governance measures we recommend for H8 constitute "no-regrets" safeguards. By strengthening oversight, challenge, and stakeholder engagement now, the CAA can protect consumers' interests and improve decision quality during H8 under any scenario. Indeed, CAP3251 itself highlights the need for enhancements to capital governance and incentives and, as such, our proposals align with that imperative and can be implemented immediately through H8. In short, these measures will set a stronger baseline for efficient, accountable investment at Heathrow regardless of the expansion model ultimately adopted.

Capex uncertainty mechanism

11.85. The 5% headroom to the capital envelope has not operated as envisaged by the CAA in H7. HAL incorporated this headroom into its baseline budget from the outset when forecasting expenditure across the control period, rather than it being applied to specific overruns or additional projects, effectively assuming its utilisation from the beginning of the period.

11.86. While we support the 5% headroom concept, this should be allocated explicitly to address additional scope or for unforeseen developments within the portfolio, rather than being assumed as part of the baseline envelope and consumed as a matter of course.

11.87. HAL has subsequently applied "an over-booking rate" against the capital envelope to account for the slippage in the delivery of projects and programmes. While this in itself is not a concern, the fact that the 5% headroom has already been allocated has resulted in projects being paused in 2026 to ensure expenditure remains within the cap, introducing inefficiency into design and planning. We do not believe this was the intent of introducing the uncertainty mechanism.

11.88. We support the CAA's proposal to retain the ability to revisit the overall cap jointly with HAL during the control period in response to unforeseen circumstances,

allowing the envelope to be set at an appropriate level while preserving flexibility to deliver additional value for consumers where justified.

Capital governance – Summary and recommendations

11.89. Based on our analysis above, we recommend that the CAA:

i. Strengthen capital governance materially for H8 in line with our proposed solutions in the table above rather than relying on minor refinements, ensuring the framework is fit for purpose and capable of delivering efficient, consumer-focused outcomes.

ii. Require clear, timely and substantive airline engagement from initial project identification through to project delivery and benefit realisation, enabling meaningful challenge on scope and options.

iii. Mandate full transparency and information sharing by HAL, including timely provision of complete, decision-grade business cases, cost breakdowns, option appraisals and portfolio-level visibility linking capex to the RAB and charges.

iv. Establish a genuinely independent assurance function, appointed by and reporting to the CAA with structured airline input, with a broadened remit covering, portfolio validation and, for individual projects, rigorous assessment of underlying need and requirements, scope and proposed solution, delivery approach and procurement strategy, design and technical specifications, robust business case, including quantified costs and benefits as a default and external benchmarking to test efficiency and value. .

v. Introduce a transparent and CAA-mandated portfolio prioritisation framework, supporting a single integrated and regularly updated portfolio view, with formal airline endorsement of priorities.

vi. Require ongoing portfolio reprioritisation during H8, with mechanisms to reallocate capital to higher value projects or return it to consumers where appropriate.

vii. Require earlier and structured airline involvement in portfolio formation and project initiation, including agreement on which projects are progressed, to improve prioritisation and avoid inefficient spend.

viii. Mandate full and continuous portfolio transparency, including monthly sharing and review of a live portfolio covering all projects from early-stage concepts through to delivery.

ix. Introduce formal pause and escalation mechanisms at gateway stages, allowing projects to be halted where there are material airline or assurance concerns until issues are resolved.

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x. Strengthen ex-ante governance processes, including reverting to the full Heathrow Gateway Lifecycle (G0–G7) for portfolios and limiting programme governance to true programmes.

xi. Ensure governance processes are adhered to in practice, preventing progression of projects or contract commitments ahead of gateway approval and limiting the use of change requests to bypass scrutiny.

xii. Reform Delivery Obligations to focus on outcomes rather than outputs, prevent routine re-baselining through change control, and ensure that consumer benefits are demonstrably delivered.

xiii. Strengthen Delivery Obligation design by improving the definition of outcomes, preventing disaggregation that weakens accountability.

xiv. Review the Delivery Obligation framework during H8 once more projects have completed the process, to ensure it operates effectively and aligns with the "fair bet" principle.

xv. Amend the treatment of outperformance to prevent permanent retention through the RAB without reset, ensuring consistency with opex treatment and protecting consumers.

xvi. Ensure the 5% headroom is not embedded within the baseline envelope and instead used explicitly for unforeseen developments or additional scope as intended.

xvii. Retain the flexibility to revisit the overall capex envelope during H8 in response to unforeseen circumstances, ensuring additional investment is tightly targeted and demonstrably beneficial for consumers.

12. Cost of Capital

BA contests the CAA's proposed H8 WACC of 5.87% pre-tax CPIH-real. Independent analysis by CEPA, supported by two leading independent academics on the beta, indicates **a WACC of 4.68%** pre-tax CPIH-real (3.74% vanilla), almost 120 bps lower, demonstrating that the proposed allowance is materially overstated. This would **over-remunerate HAL by more than £1.2 billion** beyond what required to finance its operations efficiently. **The resulting returns for HAL would be excessive**, driving **higher charges** (by over £3 per passenger) and **inefficient costs**, contrary to the CAA's statutory duties to protect consumers and secure efficiency.

Our independent analysis shows that the CAA has applied the principles of stability and predictability inconsistently, and has applied UKRN guidance both inconsistently and incompletely, while diverging from its previous decisions for HAL and NERL. The CAA has rejected more robust, better-evidenced approaches without sufficient justification or credible alternatives. The CAA's assessment is internally inconsistent, relies on factual errors and non-transparent information, fails to take proper account

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of airport-specific evidence and relevant precedent from other airport regulators. It disregards the views of its own advisers and introduces policy changes that will harm the consumer without adequate justification. It also applies its chosen approaches inconsistently both within and across different parameters.

BA's position has been informed by three independent reports from CEPA, Professor Robin Mason and Professor Donald Robertson[49]. The authors of these reports are experts in the cost of capital and have a long track record of working on behalf of regulatory bodies.

All three advisers worked on behalf of Ofwat for the PR24 regulatory determinations and CMA appeals.

CEPA has worked on cost of capital studies for Ofgem, Ofcom the Northern Ireland Utility Regulator, government departments and several international regulators.

Professors Mason and Robertson have worked on expert reports on behalf of the UK Regulators Network (UKRN).

Professor Mason is a decision-making member of the Competition Appeal Tribunal (CAT) and served on the Competition Commission/CMA for eight years, alongside other roles at economic regulators.

Professor Robertson is Professor of Econometrics at the University of Cambridge.

For the asset beta – representing the level of systematic risk faced by HAL – both Professor Mason and CEPA estimate an asset beta of 0.42, compared to the 0.50 in the H8 IPs[50]. **This demonstrates that the CAA is overestimating the systematic risk faced by HAL by 20%, adding around £1.30 per passenger.** This is because the CAA has:

- **Made factual errors in parts of its assessment**, including incorrect assumptions on capacity constraints within comparator airport groups.
- **Used unstable, inconsistent and inefficient beta estimates with embedded volatility that are not aligned with the regulatory horizon. Both Professor Mason and Professor Robertson identify this weakness** and recommend a materially better approach than the CAA's mechanistic application of a historical average by using the available evidence with explicit judgement to address that instability. **Professor Mason estimates that the CAA has overestimated the beta by almost 0.06 through that inconsistency alone.**
- **Failed to adjust for the lower systematic risk borne by HAL as a single capacity constrained hub operating under a single till framework,** compared to its comparator airport groups AENA, ADP and Fraport which operate riskier unconstrained airports internationally. The CAA acknowledges these differences

[49] The CEPA report covers the cost of capital in full; the reports from academic advisers are limited to the beta estimation.
[50] Professor Robertson's report focuses on process and critiques the CAA's approach but does not independently estimate beta or the overall cost of capital.

yet opts not to reflect them. The upward bias of comparing to those airports is also recognised by the French ART, which regulates AdP, one of the comparators used by the CAA for estimating HAL's risk. In fact, **Professor Mason finds that the CAA inconsistently applied its own implicit formula** to estimate HAL's lower systematic risk against its comparator airports, by applying one systematic risk reduction alone (TRS), rather than applying it consistently and coherently across all recognised sources of lower systematic risk (capacity constraint, single till, TRS). Professor Mason demonstrates that a **consistent recalibration** materially reduces beta and estimates that the CAA's inconsistency **leads to a further overstatement of HAL's beta of 0.11**.

Moreover, the CAA's 60% notional gearing assumption, combined with inadequate treatment of financial resilience, creates material risks for consumers It will transfer the consequences of HAL's financing choices to users through higher charges. **In fact, CAA has proposed concerning policy changes, by moving from a notional to an actual approach to debt.** This proposal has been made without sufficient justification or transparency to users, and despite the CAA's own acknowledgement that it will lead to perverse incentives for HAL, inefficient financing and higher cost for consumers. **We estimate that policy choice alone to be adding almost £2 per passenger which is a significant amount.**

We provide materially better evidence-based alternatives to deliver a more accurate assessment of the WACC and ensure efficient costs. Our approach is grounded in specialist academic advice and improves accuracy, consistency and predictability, while reducing the risk of overcompensating HAL to the detriment of consumers.

In fact, the overall regulatory package is significantly imbalanced in favour of HAL by providing several layers of protection against multiple sources of risk. HAL's compensation through both the WACC and the wider financial framework is therefore excessive. Risks relating to traffic shocks, inflation, financing conditions, input cost pressures and uncertain investment needs are, in large part, mitigated or transferred to consumers. An allowed return above efficient levels, combined with this overly protective framework, creates perverse incentives for HAL to expand the RAB irrespective of consumer value. We set out the sources of over-compensation in detail in the WACC and financial framework chapters. Consistent with recent regulatory precedent, **we propose appropriate remedies, such as through a lower point estimate within the WACC range**, to reflect these layered protections and ensure HAL is not over-compensated at the consumer's expense. These remedies are **in line with recent precedent by prominent airport regulators**, notably the French ART.

We therefore consider that there are **specific improvements required in the CAA's WACC estimation**, both in the calibration of individual parameters and in the selection of the appropriate point estimate within the WACC range.

The CAA's approach to the WACC, and HAL's compensation more broadly, will **have consequences beyond the two-runway H8 control**. This includes the return on expansionary spend. This is not a hypothetical risk, as the CAA has already proposed

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that early expansion costs for 2025-2026 should attract HAL's WACC. Setting the WACC too high would risk locking in inefficient costs and higher consumer charges for decades.

Concerns with the CAA's approach, significantly higher charges for the consumer, inefficient costs and over-compensating HAL

12.1. BA contests the CAA's assessment of HAL's H8 cost of capital (also referred to as WACC – Weighted Average Cost of Capital). The CAA's proposal for a pre-tax real WACC of 5.87% CPIH-real is more than 100 basis points above the pre-tax real WACC of 4.83% proposed by CEPA on behalf of the airlines in the Alternative Business Plan of October 2025 and equates to an additional £2.64 per passenger on the average H8 charge for the consumer or £1 billion in additional allowed returns.

12.2. Based on **CEPA's revised estimate** for Initial Proposals for a pre-tax CPIH-real **WACC of 4.68%**, which **aligns to the independent academic findings on the beta**, the overcharge **grows to more than £3 per passenger or £1.2 billion (i.e. +120 basis points on the WACC), leading to excessive charges for the consumer and excess profits for HAL**.

12.3. These are very significant differences, and we consider that they will result in significantly **higher charges than necessary at the detriment of the consumer**. The CAA's approach therefore **leads to higher and inefficient costs**, which goes **against the CAA's statutory duties to protect the consumer and ensure efficiency**.

12.4. We are fundamentally concerned that the CAA has applied its stated principles for analysing the WACC inconsistently, harming regulatory predictability and certainty, inconsistently applying UKRN guidance and inconsistently applying the threshold for evidence. The CAA's analysis on capacity constraints across HAL's comparators group is also factually incorrect, fails to take into account the differences between comparator airports and HAL, and therefore fails to make appropriate adjustments.

12.5. Proposals tabled by the airlines to improve the method for estimating the WACC, notably on the relative risk adjustment for the beta, would address the inherent inconsistency of comparing Heathrow as a single constrained hub under single till regulation to riskier airport groups with unconstrained airports and international airport holdings.

12.6. The principle that these airport groups are riskier has been widely recognised in regulatory precedent. We consider that the CAA has erred in rejecting these proposals without an attempt to robustly quantify the risk differentials, that it has inconsistently applied the standard for exercising judgement and that it has disregarded regulatory precedent both by itself and other regulators.

12.7. In fact, the CAA inconsistently applied its own implicit formula to reflect one systematic risk reduction alone (TRS), rather than applying it consistently and coherently across the different systematic risk reductions for HAL that it has acknowledged (capacity constraint, single till, TRS). Similarly, the CAA has opted to use unstable, inconsistent and inefficient beta estimates with embedded volatility

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that are not aligned with the regulatory horizon. The CAA should consider in depth what is a materially better methodology in the interests of users of airport services. Indeed, the CAA's approach to the beta has a material impact on charges, with its use of unstable empirical betas and failure to adjust for HAL's risk differentials adding around £1.30 per passenger.

12.8. The CAA has furthermore proposed policy changes, such as allowing Heathrow's actual cost of debt rather than notional debt without sufficient justification or transparency to users, and despite the CAA's own acknowledgement that this will lead to perverse incentives for HAL, inefficient financing and higher cost for consumers. It is thus materially weaker as an approach. This policy choice by the CAA alone could increase costs by up to £2 per passenger.

12.9. We do not therefore consider that the CAA's approach constitutes a robust way to estimate the WACC and will harm consumers by allowing inefficient costs. Importantly, CEPA's advice and the independent academic advice we have commissioned (described below) recommend materially better alternatives to the CAA's approach with regards to estimating the beta to account for beta instability, quantifying HAL's lower relative risk to its comparator airports, and improving the CAA's methodology. These recommendations would yield a materially better evidence-based method to ensure consistency, predictability and avoiding overcompensating HAL at the consumer's expense.

12.10. We note a significant difference in the robustness and predictability of the CAA's methodological framework for opex, commercial revenues and capex in comparison to the CAA's WACC analysis. A regulator should keep under review whether its existing methods still best give effect to those principles. This is all the more relevant as H8 will be baselining the future cost of expansion at Heathrow thus embedding higher charges for the consumer and potentially inefficient costs into the long run.

12.11. The CAA should be seeking to review its approaches to satisfy itself that it is applying the materially better methods to deliver efficient costs at the time of the price control decision. Leaving those issues identified early in the process to be addressed upon an eventual appeal to the CMA or further legal action is not good regulatory practice, risks harming the consumer until such an appeal is decided and requires the less proportionate remedy of reopening the price control.

12.12. In fact, we continue to be deeply concerned with the cumulative effect of the CAA's proposed policy choices that afford HAL several layers of compensation for risk, including an overestimated beta and proposals for debt protection, despite the existence of materially better alternatives to estimate those parameters. The CAA's regulatory package provides for several layers of protection, including multiple protections to HAL's exposure to traffic shocks, inflation protection, financing conditions, input cost pressure and uncertain investment needs and overcompensate HAL for its profile of risk. We therefore consider the CAA's proposal for an equity beta of 1.14, thus assuming HAL being riskier than the market, coupled with an estimate at the mid-point of the WACC range, not to be reasonable or defensible.

12.13. The regulatory package should represent a fair bet. This should account for both the level of compensation provided to Heathrow and the distribution of possible outcomes. We strongly consider that the compensation provided to Heathrow is higher than the level of risk it faces. This is relevant not only to the cost of capital, but also to the financial framework. We discuss HAL's overcompensation below in chapters of our response on the WACC and the financial framework and propose what we consider to be appropriate remedies aligned with regulatory precedent.

12.14. The CAA's approach to the WACC, and HAL's compensation more broadly, could have consequences beyond the two-runway H8 control. This includes the return on expansionary spend. Setting the WACC too high would risk locking in inefficient costs and higher consumer charges for decades. This is not a hypothetical risk. The CAA proposes using HAL's H7 WACC as the benchmark return for early expansion costs incurred in 2025–26[51] and the H8 WACC may likely apply to equivalent costs incurred after 2027."

CEPA report

12.15. The airline community has commissioned CEPA to assess the WACC proposed by the CAA in its IPs. CEPA identifies a number of inconsistencies in the CAA's approach and proposes certain recommendations to improve the CAA's estimation of the WACC, particularly on the beta, calculating the notional debt allowance and adopting a notional gearing.

12.16. CEPA provides **an indicative pre-tax CPIH-real WACC of 4.68% (equivalent to 3.74% vanilla)**, suggesting that a materially lower figure than the CAA's proposal of 5.85% pre-tax CPIH-real (4.86% vanilla) continues to be justified. In fact, the **CEPA's recommendation is almost 120 basis points lower than the CAA's proposal, suggesting that charges would reduce by more than £3 per passenger**. **On this basis, we consider that the CAA's proposed allowance for HAL's H8 financing costs is overstated by more than £1.2 billion, leading to concerns over excessive charges, over-remuneration and excess profits for HAL.** CEPA's findings are in line with the recommendations to improve the CAA's beta estimate by the independent academics set out in this chapter. We set out the findings of CEPA's report further below.

Independent academic advice

12.17. The airline community has also commissioned two independent academics on distinct pieces of advice evaluating the CAA's IP methodology on beta estimation:

i. **Robin Mason, Professor and Pro-Vice-Chancellor at the University of Birmingham, and Ordinary Member at the Competition Appeals Tribunal.**

12.18. Professor Mason's report finds the CAA's choice of its pre-adjustment beta in the face of instability in comparator airports is inconsistent and overestimates the beta because it gives too much weight to long-window estimates that may no longer be

[51] See CAP3238.

representative. Professor Mason proposes a materially better approach compared to the CAA's mechanistic application of identifying a simple historical average. This because it uses the available evidence with explicit and consistent judgement to address that instability. Recent estimates should receive particular weight in an unstable setting with the long-term evidence only used as a cross-check. The approach would provide a more transparent and economically grounded basis for setting the beta range, bounded by estimates that are most relevant to the current risk environment.

12.19. In addition, Professor Mason's report identifies that the CAA has inconsistently applied its own implicit approach to estimate HAL's lower systematic risk against its comparator airports, by applying one systematic risk reduction alone (TRS), rather than applying it consistently and coherently across the different systematic risk reductions for HAL that it has acknowledged (capacity constraint, single till, TRS). Professor Mason recalibrates and improves the CAA's formula to apply it consistently across the different systematic risk reductions.

12.20. Professor Mason's approach is equally a materially better and targeted alternative by applying a disciplined adjustment to the CAA's framework to correct for these errors rather than adopting a wholesale departure from it.

ii. **Donald Robertson, Professor of Economics, University of Cambridge.**

12.21. Professor Robertson's report details how the CAA's purely mechanical application of OLS regression relies on unstable, inconsistent and inefficient beta estimates with embedded volatility that are not aligned with the regulatory horizon. It sets out the need for an explicit framework to assess the beta to increase confidence in the estimation to address time variation, outliers, highly influential data points and structural breaks. The report proposes when certain methods should be considered suitable for beta estimation to address for that instability.

12.22. The CAA's duty is to create a robust, predictable and independently verifiable approach for the calculation of the WACC that avoids overcompensating HAL and harming consumers. The proposed improvements to the CAA's approach would result in a materially better method for estimating the WACC for a single constrained airport hub which is not directly comparable to other regulated utilities or airport providers.

12.23. We refer to those reports for the detailed recommendations and set out our views below. We consider that the approaches by CEPA and the independent academic experts will enhance and improve the CAA's approach for estimating the WACC and offer a materially better alternative to the shortcomings of its existing approach.

The CAA's inconsistent application of its principles

12.24. The CAA has set out in the IPs the principles it has adopted for calculating the WACC:

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i. Regulatory stability and predictability with previous CAA decisions: "*We retain our approach from the H7 price control, unless there is a clear reason why this would not be appropriate*."

ii. Consistency with other UK regulators where possible: "*We align our approach with the UKRN cost of capital guidance, unless there is a clear reason why this would not be appropriate*."

iii. New issues: "*Where new issues or evidence emerge that are not adequately addressed by either the UKRN cost of capital guidance or the CAA's H7 approach, we exercise our judgement taking into account the available evidence, including the CMA's Provisional Determination of the PR24 price control. For example, we have considered new evidence in respect of the impact of non-core holdings by comparator airports and in relation to the impact of the "single till" we use to regulate HAL*."

iv. Thresholds for subjective judgement: *"Where it is practicable and reasonable, we have sought to simplify our approach and avoid relying on approaches that rely excessively on subjective assumptions*."[52]

12.25. We agree with those principles. However, we remain concerned that the CAA has not applied these principles appropriately resulting in excessive subjectivity, inconsistency, factual inaccuracies and failing to adopt materially better alternatives to ensure efficient costs which would avoid overcompensating the monopoly provider and protect the consumer. Indeed, the CAA's approach in certain areas fails to guarantee the very regulatory stability and predictability it is seeking to achieve.

12.26. A regulator should keep under review whether its existing methods still best give effect to those principles. The fact that the CMA did not find the CAA was 'wrong' at H7 does not establish that the H7 approach was the best available approach, or that it remains the best approach for H8. The data, market conditions and precedent now at the CAA's disposal are materially different from those relevant to H7. Consistency across decisions, sectors and time is desirable. Consistency is not achieved merely by repeating an earlier method without testing whether it remains fit for purpose in different circumstances. This is all the more relevant as H8 will be baselining the future cost of expansion at Heathrow.

Concerns with inconsistences and errors in the CAA's approach

12.27. In contrast to the CAA's approach on capex, opex and commercial revenues, we believe that the CAA has applied those principles inconsistently and erroneously in relation the WACC. The CAA has disregarded evidence and methods available that would have yielded a materially better approach for avoiding overcharging the consumer while ensuring HAL can finance its activities. We provide evidence of this below.

[52] See Initial Proposals, paragraph 9.25.

Inconsistent application of the principle of regulatory stability and predictability

12.28. The CAA has retained a notional gearing at 60%, at the higher end of the regulated utilities sector in the UK and significantly above other regulated airport hubs, on the basis that there is no clear reason to change it. However, despite not identifying stronger reasons, the CAA is proposing to move from a notional to an actual approach to debt allowances, which sits uncomfortably with a notional gearing. The CAA appears to apply the principle of regulatory stability and predictability inconsistently.

Inconsistent and incomplete application of UKRN guidance, unjustified policy change and lack of transparency on cost of debt, unstable and inconsistent beta estimates, notional gearing

12.29. Despite UKRN guidance highlighting that different approaches in UK regulated sectors may be required due to sector-specific issues and key sectoral differences may require bespoke approaches by regulators, the CAA deploys approaches failing to reflect that HAL operates a single airport hub and not a water or energy company. The regulatory task is not to mirror methods used in those sectors but adopt methods that properly reflect HAL's circumstances.

a. Cost of debt

12.30. The CAA now proposes an actual cost of debt approach for HAL following Ofwat and Ofgem's industry approaches assessing actual debt costs across the sector to set a sector-wide allowance. However, the CAA has failed to explain why this approach is appropriate for HAL as a single asset company, whereas in networks Ofwat and Ofgem are working with cohort regulation. The result of this adjustment is an approach that is an effective pass through of actual costs from a highly leveraged company onto consumers (where the costs of debt will be higher due to that leverage than they would be if the company were levered at the notional leverage) and therefore removing incentives for HAL to be efficiently financed. This approach risks embedding significant risk protection into HAL's regulatory settlement, something which the CAA has not reflected in its WACC analysis, such as in the beta or the choice of point estimate within the range. We explain this further in the section on HAL's layers of overcompensation.

12.31. The CAA has also failed to reflect that stakeholders have had no access to the HAL's underlying debt costs required to interrogate the resulting cost of debt allowance. Airlines have written on multiple occasions to HAL and the CAA requesting access to HAL's debt book which has so far been refused – see the community's letters to the CAA of 13 October 2025, 30 January 2026, 5 March 2026 and 8 May 2026. However the CAA has not instructed HAL to share this information, has not shared its analysis with the Initial Proposals, and has not shared its rationale for preventing the granting of access to users subject to applicable confidentiality safeguards, such as confidentially rings This has precluded effective engagement and raises concerns as to the suitability of the CAA's policy choice. The CAA's policy choice to move to actual and away from nominal debt could increase costs by up to £2 per passenger.

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12.32. Importantly, we highlight the CAA's own acknowledgement that its proposal to compensate HAL for its actual cost of senior debt for HAL's embedded debt poses risks through "***a limited incentive on HAL to issue senior debt efficiently**, since the cost of new senior debt would effectively be **passed through to consumers once it became embedded debt in future price control periods**.*" (our emphasis)[53]

12.33. BA therefore contests the CAA's approach to compensate HAL for its actual cost of debt lacks justification as it is unsuitable for a single regulated company and risks harming the consumer in the long-term by passing on HAL's inefficient higher debt costs. This approach is all the more risky as it would not control for HAL's level of gearing – for which the overall Heathrow group rather than only the narrowly regulated entity is relevant – ahead of significant expansionary spend. This will in turn set inefficient costs and higher charges for consumer for decades to come. An actual debt approach at H8 would create an expectation that future debt costs will be passed through. If expansion proceeds, Heathrow may need to issue substantial further debt.

b. Unadjusted OLS betas – unstable, inconsistent and inefficient estimates

12.34. Secondly, the CAA relies on unadjusted 2-year and 10-year OLS betas. The CMA concluded in PR24 that unadjusted OLS betas were appropriate in the water sector after considering the effect of the COVID-19 period. The CMA concluded at H7 that it was appropriate for the CAA to <u>not</u> use unadjusted OLS betas in light of the COVID pandemic. The UKRN has expressly recognised that aviation was affected differently. In such circumstances, an approach that deals properly with those sector-specific features in aviation would be more consistent with the UKRN guidance, even if it differs from the approach adopted in water. As noted above, our independent academic advice by Professors Mason and Robertson indicate concerns that the CAA's proposed H8 approach relies on unstable, inconsistent and inefficient beta estimates with embedded volatility that are not aligned with the regulatory horizon. Both academics propose adjustments to address this inconsistency and to improve the robustness of the estimate.

c. Notional gearing

12.35. Thirdly, the retention of a 60% notional gearing assumption does reflect UKRN guidance or recent regulatory practice, where Ofwat and Ofgem have reduced notional gearing to provide an appropriate equity buffer and greater financial resilience.

<u>Inconsistent application of the threshold for subjective judgement: relative risk adjustment – single capacity constrained hub and single till risk mitigation</u>

12.36. The cost of capital is not directly observable and relies on the exercise of judgement. As HAL is not publicly listed, therefore the CAA will need to apply its duties in method selection, the choice of evidence, the ranges adopted and the point estimate within the range. The CAA suggesting that a relative risk adjustment has a higher

[53] See Initial proposals, point 9.247, CAP3232C.

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evidential threshold than the other areas of the price review is therefore wrong in principle. Adjustments should be adopted if the evidence points to a materially better way of estimating the cost of capital in the specific circumstances, and risk protections, faced by Heathrow Airport.

12.37. The CAA's treatment of the TRS mechanism is a relevant example of effective adjustments for sector specific considerations. At both H7 and H8 Initial Proposals, the CAA has been willing to apply adjustments to beta where that produced a materially better estimate than a zero adjustment to reflect that specific risk protection for HAL.

12.38. However, the CAA has not applied a downward relative risk adjustment to comparator airport betas to reflect that HAL is a single constrained airport hub, protected from a systematic risk (traffic) compared to its comparators that operate hubs that are unconstrained and/or smaller group airports across the world (AdP, AENA, Fraport). The CAA has preliminarily decided that such an adjustment would require a high evidential threshold.

12.39. We disagree that the CAA should apply a more stringent, and therefore inconsistent standard, in the exercise of any adjustments for the airport comparators than the one applied in its application of other adjustments in H8 and in its previous decisions for Heathrow for the same risk reductions that it has now rejected (see CEPA report for full list of examples). For instance:

i. H8: The CAA accepted and quantified the asymmetric risk allowance and the TRS impact of the beta.

ii. H7: The CAA determined that Heathrow's pre-pandemic beta was 0.50, the lower part of their empirical range, with a statement that the pandemic had increased the top end of the risk range by up to 0.10.

iii. Q6: The CAA adjusted comparator group betas for AdP and Fraport groups downward to reflect risk characteristics relative to Heathrow. The CAA set different betas for Heathrow and Gatwick Airports to reflect risk differences.

12.40. The CAA also rejected the relative risk adjustment to account for HAL's risk reduction to single till regulation despite evidence from other regulators, notably the Irish Aviation Authority (IAA) that single till is credit protective and the risk reducing effect of periodical rests of commercial revenues[54]. While the CAA does not deny that a single till structure may matter in principle, it has rejected CEPA's approach proposed with the Alternative Business Plan without proposing a materially better alternative, opting to continue overestimating HAL's risk.

12.41. We note in this regard Professor Mason's independent analysis which has found that Heathrow-specific features – notably capacity constraints, single till and the TRS, should all be reflected in the estimation of the beta. The analysis proposes a

[54] See IAA's Issues Paper for the 2026 Determination at Dublin airport, paragraphs 4.25 and 10.9, https://www.iaa.ie/docs/default-source/publications/corporate-publications/economic-regulation/2026-determination-on-airport-charges-at-dublin---issues-paper-consultation.pdf?sfvrsn=714ca45f_9.

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materially better alternative to estimate those risk reducing effects, as opposed to the CAA's approach of not applying the adjustment at all. Professor Mason's approach focuses on consistently applying the CAA's own implicit formula to reduce the beta across all systematic risk reductions (capacity constraint, single till, TRS) rather than applying it inconsistently across one risk reducing factor alone (TRS). We discuss this further in this chapter.

Factual inaccuracies – capacity constraints at comparator airports

12.42. The CAA bases itself on factual inaccuracies and superficial assessments of evidence – such as on purported capacity constraints at the European comparators – notably Madrid, Barcelona and Paris CDG to justify not adjusting Heathrow's beta downwards to reflect its capacity constraint in line with practice in previous regulatory periods.

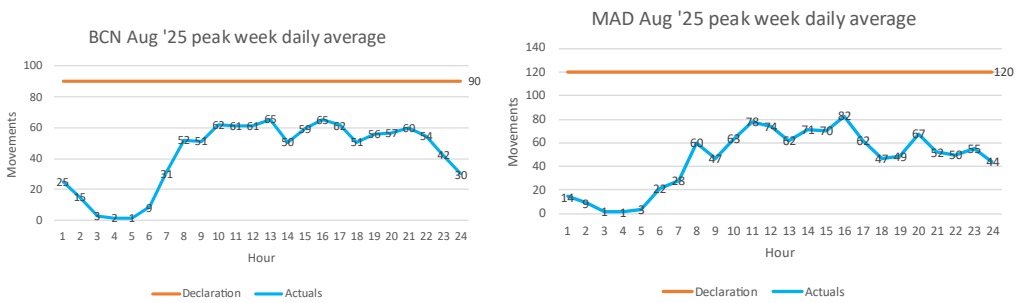
12.43. The CAA has not shared its analysis underpinning those findings. We do not recognise those findings and believe that they are factually inaccurate. Our analysis of the airports demonstrates all three airports operate well below their declared runway limits, in contrast to Heathrow which operates at or close to its runway limits for most of its operating day. We note that runway capacity is the hard capacity limit for most airports. Our analysis uses OAG schedule data during August 2025 peak.

i. Where LHR is at or above 90% of its runway limit for much of the day, MAD, BCN and CDG all operate well below their declared limits.

ii. Using an August 2025 peak week and OAG data, BCN's peak hour averages at 65 vs its declaration of 90; MAD at 82 vs 120; CDG at 96 vs 120. LHR by contrast is 90 vs 92 (or 91 vs 92 in Sept).

iii. Further, LHR remains close to its limit through much of its operating day, whereas MAD, BCN and CDG are all 'peakier'.

Runway capacity utilisation across Heathrow, Madrid, Barcelona and Paris CDG – August 2025



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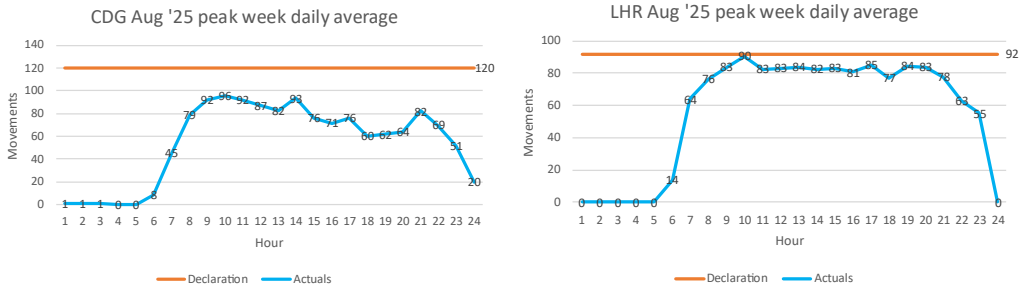

Source: IAG analysis, OAG schedule data, declared capacities by COHOR (CDG), DORA II (MAD/BCN)

12.44. We also note that the CAA has made specific reference to Madrid and Barcelona airports, without recognising that AENA – which is the listed airport operator used as a comparator for HAL – operates 44 other smaller airports across Spain which are also not capacity constrained.

Airport sector-specific evidence: precedent from other European regulators removing the upward bias for comparator airport groups

12.45. In addition to UK regulatory precedent, the CAA ought to factor in its analysis precedent from prominent EU charges regulators on adjusting. This particularly concerns the single airport hub risk as well as removing the upward bias for comparator airport groups with activities in smaller airports and other markets. Indeed, this difference cannot be covered through a simple comparison to other UK regulated sectors due to key sectoral-specific references.

12.46. We draw specific attention to the recent opinion by the French Transport Regulatory Authority (ART) on the upcoming regulatory agreement at AdP (Paris Airport). The ART identifies the inherent upward bias in the comparison of AdP to airport groups with holdings in international airports such as AENA, Fraport and Zurich – which together with AdP are the same comparators the CAA uses in the peer group for estimating HAL's beta. The ART also underscores that, due to those activities, the overall risk profile may exceed that of the regulated activity alone and proposes how to adjust for that risk.

12.47. Nevertheless, while the CAA compares HAL to AdP for the purposes of establishing the asset beta, it does not use its judgement in a similarly consistent manner to the ART and fails to produce a materially better method for adjusting for the upward bias and estimating the WACC more accurately.

French ART opinion on AdP Economic Regulation Agreement 2027-2034, April 2026

"[T]he choices made by ADP in estimating the beta also result in a high end of the range. The sample of comparables selected, comprising AENA, ADP, Fraport (Frankfurt) and Flughafen Zürich, appears to be both particularly limited and focused on companies engaged in diversified activities, including in particular commercial activities or holdings in international airports.

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> *The Authority points out that a broader and more balanced sample, including operators with a narrower scope of activities,* ***provides a more accurate estimate of the risk within the regulated sector by limiting the upward bias associated with diversified groups****.*
>
> *[…]****Furthermore, listed airport groups most often engage in diversified activities, including in particular commercial activities or international investments, the overall risk profile of which may exceed that of the regulated sector alone.***"[55] (our emphasis in bold)

Inconsistent and arbitrary data cut-off dates: not in line with regulatory practice and preventing effective engagement

12.48. The CAA is inconsistent and arbitrary with its choice of cut-off dates on financial parameters. This increases uncertainty of the final figure that will be used and precludes effective engagement. This increases uncertainty of the final figure that will be used and precludes effective engagement.

12.49. The CAA proceeded with a headline cut-off date of 1 November 2025 for proposals published on 31 March 2026. This is 5 months or 21 weeks prior to publication.

12.50. This date is too early to provide relevance based on prevailing market data for the CAA's IPs given reductions in betas since December 2025. It is also arbitrary as the CAA has not explained why such an early cut-off date is relevant or appropriate. It captures older shocks (such as data shocks in November 2020) not relevant to the regulatory horizon for H8 that artificially raise the beta and that have been repeatedly raised by stakeholders with the CAA over the past five years – such as in the lessons learned exercise, the method statement and during engagement with the CAA.

12.51. It is furthermore internally inconsistent, as, on inflation, the CAA has directly used the OBR's 26 November 2025 publication, notably after the headline cut-off. On the cost of debt, the Initial Proposals use Heathrow's debt book from December 2024.

12.52. The approach equally prevents effective engagement as any prevailing data cannot be assessed until Final Proposals, creating further uncertainty and unpredictability.

12.53. The airlines encouraged the CAA to use a later cut-off date prior to publication of Initial Proposals. This provides a materially better alternative as it is in line with regulatory practice and increases certainty by maintaining relevance of the proposals to the most recent market data:

[55] See ART opinion on ADP Economic Regulation agreement 2027-2034, 20 Apri 2026, paragraphs 233-235. https://www.autorite-transports.fr/actualites/avant-projet-de-cre-daeroports-de-paris-lart-formule-ses-recommandations-pour-securiser-un-cadre-economique-equilibre-dans-la-mise-en-oeuvre-du-projet-industriel-de-lexp/

i. Ofwat: The PR24 Final Determinations used an end-September cut-off for a publication on 19 December 2024. This is 11 weeks rather, with the CAA using twice as long a period (21 weeks).

ii. ART: In its recent opinion dated 9 April 2026 on the upcoming regulatory agreement for AdP, the French ART has used a cut-off date of 10 February 2026, which is 8 weeks. The period used by the CAA is more than three times longer.

12.54. We believe the time taken to update for a later cut-off date in time for IPs would have been minimal demonstrating that the CAA has not opted for the most proportionate, predictable and robust solution.

CAA pre-empting policy choices before the issuance of its independent consultant's report

12.55. The CAA also appears to have pre-empted policy choices on several issues prior to the issuance of the report of its independent consultants, including making policy changes, which would raise concerns over the independence and robustness of the estimate as well as the predictability and certainty of its approach.

12.56. The report by FTI commissioned by the CAA points to several places where the CAA appears to have made a policy change prior to its report, which in our view restricted its ability to reach to reach a truly independent and robust estimate:

i. The CAA made a policy decision to adopt OBR medium-term inflation forecasts in H8, which FTI then implemented, rather than allowing the consultant to reach an independent view. FTI highlights that this approach is inconsistent with other regulators: "*[The CAA's policy decision] is, however, different from the decisions made by other regulators. Specifically, Ofgem at RIIO-3, Ofwat at PR24, and the CMA in its PR24 appeal Provisional Determinations ("PR24 PD") have all adopted longer-term inflation assumptions in their regulatory frameworks*".[56]

ii. The CAA made a policy decision to adopt the same framework as at H7 with respect to the assessment of the impact of its capacity constraint on its relative risk to its comparator groups for the beta, which has significant ramifications for the beta estimate. Importantly, FTI notes that it may have reached a different position that was constrained by CAA pre-empting its report:

> "*At H8, the CAA's policy decision is to adopt the same regulatory framework as at H7. However, and contrastingly, HAL has now fully recovered from the impact of the pandemic and has achieved all-time high passenger numbers.* ***As a result, there is no conclusive evidence to suggest that HAL's systematic risk (under the existing two-runway solution) is any higher than it was at H7. In fact, it would not be unreasonable to suggest that HAL's systematic risk is somewhat lower than at H7.***" (our emphasis)[57]

[56] See FTI report, paragraphs 2.32-2.33, 2.38 and further repeated references in the report.
[57] See FTI report, paragraph 6.132.

CEPA 's recommendations to materially improve the CAA's WACC methodology

12.57. CEPA has proposed a number of recommendations which would yield a materially better estimate of the WACC that reflects HAL's true risk, avoids overcompensating HAL and ensure consumers and users of airport services do not overpay.

12.58. This approach would consistently apply the principles of regulatory certainty and predictability, align with regulatory precedent and apply the regulatory standard for judgement in a consistent manner reflecting the sector-specific characteristics for HAL. We set out those recommendations below and refer to CEPA's report for a more detailed explanation.

Recommendation 1: Apply a downwards relative risk adjustment, supported by independent academic advice

12.59. The CAA has applied no relative risk adjustment from empirical beta comparators to estimate HAL's H8 asset beta. In CEPA's view, a downwards relative risk adjustment would represent a materially better alternative than no adjustment as it is justified on the basis of established systematic risk differences between comparators and HAL represented by Heathrow's capacity constraint, single till regulation and TRS mechanism. Such an approach would also be consistent with CAA precedent, the CAA's evidentiary bar in other H8 proposals (including the TRS adjustment itself), and the approach by other regulators discussed above.

12.60. The CAA is currently using empirical betas from AENA, AdP, Fraport and Zurich. These are airport comparator groups with international holdings as opposed to single constrained airport hubs such as HAL. For instance, AENA operates 46 airports – the vast majority of airports across Spain – not just Madrid or Barcelona. Spanish airports had 321 million passengers in 2025, which compares to 302 million across all UK airports.

12.61. In contrast, Heathrow has materially lower traffic volatility and is capacity constrained. It is therefore appropriate for HAL to have a lower asset beta reflecting that lower systematic risk linked to traffic against its listed comparators.

12.62. Similarly, all comparator airports are in dual till as opposed to HAL's single till regulation and their empirical betas reflect all activities of the operator rather than regulated aeronautical activities.

12.63. The upwards bias in comparators' empirical betas is confirmed by the following evidence:

i. The French ART's recognition and adjustments to empirical betas, set out above in relation to the same airport groups that the CAA is employing to set HAL's beta (AENA, AdP, Fraport, Zurich).

ii. The CAA's approach in Q6 described above.

iii. The CAA's own approach in H7 when it chose to increase HAL's asset as "*the pandemic has narrowed the risk differential that previously existed between HAL and comparator airports.* ***This is because HAL previously benefitted to a greater extent than other airports from excess demand (supported by capacity constraints) that insulated it from volatility in unconstrained demand****. In the context of the pandemic, we do not expect that HAL will benefit from substantially greater excess demand than other airports in H7. We estimate that this effect increases HAL's asset beta by 0.10 at the upper end of the range*" (our emphasis added) [58]. Given that the capacity constraint is effective for Heathrow at H8, all else unchanged, a roll-forward of the H7 approach would involve a downwards relative risk adjustment asset beta retained by the CAA.

iv. The CAA's consultants, FTI, acknowledge that *"HAL is expected to remain capacity constrained under a two-runway solution in line with its pre-pandemic operations. This implies that* ***the company's risk profile (based on passenger volumes), has lowered since H7*** *and is largely unchanged from the previous price control (Q6)."* (our emphasis added)[59]. FTI further state that: "*Over H7, HAL was expected to have spare capacity due to the impact on passenger traffic from the Covid-19 pandemic and the expected time to recover from this impact.* ***However, HAL is currently handling record levels of passenger numbers and over H8, it is expected to face capacity constraints.*** *This indicates the normalisation of operating conditions. From a passenger traffic standpoint, this is reflective of operating conditions during the Q6 price control (2014 to 2021)."*[60]

12.64. However, the CAA has chosen to reverse its approach and not apply a relative risk adjustment for H8 with no clear justification other that the quantification of the differential is complex, despite previously quantifying that differential itself.

12.65. If the CAA is adopting a different perspective, the change in approach harms regulatory predictability and certainty, is inconsistent to precedent and is not consistent with the CAA's duty to ensure efficient costs under the Civil Aviation Act 2012.

12.66. If the CAA considers the differential is now zero, this would go against its own consultant's advice that the H8 risk is lower than H7 and could imply that the only reason for no adjustment is to avoid a further reduction on top of the reduction in empirical comparator airport risk.

12.67. CEPA states **an indicative relative risk adjustment of -0.075**, which is the mid-point of its -0.15 estimate in its November 2025 report given the reduction it proposes in the empirical (pre-adjustment) asset beta (see Recommendation 2 below). We note that if the empirical beta is higher, the relative risk adjustment would increase.

[58] CAA (2022) H7 Final Proposals, Section 3.
[59] See FTI report, paragraph 5.10.
[60] See FTI report, paragraph 12.4.

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12.68. CEPA subsequently adopts the CAA's mid-point assumptions for the impact of the TRS mechanism, although it has not conducted a new full assessment of these input assumptions. **This results in a post-adjustment asset beta of 0.42**.

CEPA Asset beta estimate (using 0.075 debt beta)

	CEPA estimate
Empirical (Pre-adjustment) Asset Beta	0.53
Relative Risk Adjustment	-0.075
Heathrow pre-TRS asset beta	0.455
Network Utility Asset Beta	*0.360*
Proportion explained by traffic risk	*80%*
Proportion mitigated by TRS mechanism	*50%*
Impact of TRS mechanism	-0.04
HAL post-adjustment asset beta	**0.42**

Source: CEPA analysis

12.69. We consider that the CAA has therefore erred in its analysis and the recommendations by Professor Robin Mason provide a materially better alternative for quantifying the risk differential. Indeed, Professor Mason employs the CAA's own implicit methodology in a consistent, coherent and evidence-based manner across all systematic risks (capacity constraint, single till and TRS). Professor Mason's analysis has yielded a similar result to CEPA with a post-adjustment asset beta of 0.42. This is described in the academic advice section below.

> Recommendation 2: Change approach to empirical beta estimation which yields a distorted higher beta not aligned with the regulatory horizon, supported by independent academic advice

12.70. The CAA's H8 Initial Proposals use spot 2-year and 10-year OLS regressions to derive an empirical asset beta range of 0.47 to 0.70, with a midpoint of 0.59.

12.71. However, the CAA should place less weight on unadjusted spot OLS regressions – in particular the 10-year OLS regression output – and should instead use empirical beta methods that better reflect two features of the airport comparator evidence: that airport betas vary over time, and OLS estimates are materially affected by unusual observations.

12.72. CEPA's analysis and evidence indicate that a small number of observations have a disproportionate effect on airport beta estimates. These are March 2020 and November 2020 as particularly influential, reflecting the onset of the COVID-19 pandemic and the vaccine announcement respectively. The impacts from 'Liberation Day' and US trade policy in April 2025 is also visible but is of a magnitude less than the COVID related shocks.

12.73. Indeed, the CAA itself in H7 did not rely on unadjusted OLS because COVID-period observations could dominate the beta estimate and overstate forward-looking

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systematic risk. Adopting unadjusted 10-year OLS therefore requires a stronger justification than the CAA has provided based on its own previous assessments.

12.74. The impact of the distortion is material. CEPA's analysis shows that outlier-mitigation techniques reduce the long-window 10-year asset beta by around 0.07. By contrast, the downward bias in short-term (e.g. 2-year betas) is much smaller and does not offset the upward bias in the 10-year estimate. This indicates that the CAA's upper bound is too high.

12.75. CEPA proposes three alternative materially better methods to reduce the effect of influential unstable observations, rather than relying on unadjusted OLS or subjective exclusion of individual data points:

i. CAA could place a greater weight on short-term spot OLS estimates, particularly 2-year and 5-year estimates[61]. Using an end-March 2026 cut-off, those estimates support an asset beta range of **0.45 to 0.56**.

ii. The CAA could use robust regression techniques. These methods apply transparent rules to reduce the influence of high-leverage observations. They support a range of 0.46 to 0.56 for 2-year and 5-year estimates, or **0.46 to 0.61** if 10-year estimates are included.

iii. The CAA could use time-varying beta models, such as GARCH. CEPA's GARCH results support an empirical asset beta range of **0.48 to 0.55**.

12.76. All three materially better methods point in a consistent direction that the CAA's empirical asset beta range of 0.47-0.70 is too high, particularly the upper bound. A range of **0.45 to 0.61, with a 0.53 empirical asset beta estimate,** covers the full breadth of data yielded by CEPA's analyses.

12.77. The independent advice commissioned by the airline community agrees with these findings. Both Professor Mason and Professor Robertson find that the CAA's approach overestimates the beta as it gives too much weight to long-window estimates that may no longer be representative and are not aligned to the regulatory horizon. Professor Mason proposes an approach that is more transparent, economically grounded and evidence-based for setting the beta range, bounded by estimates that are most relevant to the current risk environment. The approach does not create a new mechanical formula but rather disciplines the CAA's judgement required under instability. Professor Robertson proposes when certain methods should be considered suitable for beta estimation. We describe those reports further below.

Recommendation 3: Remove market-cap weighting on beta aggregation

12.78. CEPA finds that the CAA has erred in relying upon market-cap weighted betas. Market capitalisation is affected by each comparator's capital structure and makes for a poor basis on which to weight asset betas as it gives weight to comparators

[61] The 5yr recommendation is contingent on the November 2020 vaccine announcement having left the estimation window sample.

that have selected lower geared capital structures. This includes re-levering comparators from lower-geared comparator gearings of around 20% to 60% which is the CAA's notional gearing assumption. There are equally concerns that AENA's asset beta may be overstated and that its larger market cap is due to the 50+ airports within and beyond Spain, making it less suitable as a comparator as relative risk needs to be controlled for.

12.79. The CAA's market-cap weighting has a material impact as it increases the comparator beta by 0.03

Recommendation 4: Re-calculate the TRS adjustment

12.80. BA supports the use of the TRS adjustment applied by the CAA. However, CEPA finds that the CAA has not justified why it considers a 90% differential to be appropriate for the low and 70% differential for the high case. This generates a smaller adjustment than using applying either a mid-point value or using 70% in the 'low' case and 90% in the 'high' case, which we consider a materially better alternative.

12.81. In addition, BA recommends the recalibration of the TRS to account for the additional protections to HAL in H8 in case of failure to deliver key capacity programmes, notably terminal occupancy and Terminal 5 capacity optimisation. It is critical that Heathrow does not benefit from delaying these key capacity programmes, including through any change to passenger forecasts. We equally contest the notion of HAL being protected through the TRS from any reductions in traffic caused by its own failure to deliver these delayed projects, that the CAA itself has scored highly in its H8 capital prioritisation. We therefore recommend that the CAA should be applying a larger downward adjustment to HAL's asset beta to account for those additional protections, a clawback mechanism or, in the alternative, carve out those projects from the ambit of the TRS mechanisms to remove those perverse incentives on HAL. We elaborate on those concerns further in the sections on capital and the financial framework.

12.82. Moreover, with Heathrow airport expected to be operating at its capacity constraint for the duration of H8, the likelihood the TRS mechanism kicking in for any shortfalls in traffic is significantly higher than any additional traffic. This would benefit HAL to a greater extent that airlines and the consumer, as the latter would be expected to fund (part of) HAL's shortfall. Given the skewed way in which the TRS is expected to apply in H8, BA asks the CAA to reflect this imbalance in a higher downwards adjustment to HAL's asset beta than already applied.

Recommendation 5: Adopt a notional approach for debt allowances to avoid perverse incentives, unjustified higher charges and longer-term implications for expansion

12.83. The CAA's proposal to employ an actual cost of debt for Heathrow – including HAL's more expensive senior debt for the cost of embedded debt – as opposed to a notional company is wrong for several reasons:

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i. It has poor incentive properties. Where there is just one regulated company such as HAL, an allowance based on actual debt costs operates as a pass-through. That weakens incentives to minimise financing costs and creates a risk of higher charges on consumers and users of airport services.

Indeed, the CAA recognises this risk in its IPs concerning the proposal to use HAL's actual cost of (embedded) debt:

"*There is* ***a limited incentive on HAL to issue senior debt efficiently, since the cost of new senior debt would effectively be passed through to consumers*** *once it became embedded debt in future price control periods.*" (our emphasis)[62]

ii. It lacks transparency and users have been unable to interrogate the data underpinning the decision. The publication of regulated companies' debt books is permissible in other regulated industries, with Ofwat publishing calculations of water company debt instruments on its website.[63] This includes evidence for both publicly listed companies and private companies. However, despite repeated requests to the CAA requesting access to this information, the CAA has not instructed HAL to share this information, has not shared its analysis with the IPs or its rationale preventing it from granting access to users subject to applicable confidentiality safeguards, such as confidentiality rings.[64] Stakeholders therefore cannot test the proposed allowance adequately which undermines the transparency of the price control decisions and make its extremely challenging for users to properly interrogate the CAA's decisions. The CAA's policy choice to move to actual and away from nominal debt increases costs by up to £2 per passenger.

iii. Heathrow-specific features make an actual cost of debt particularly unreliable.

- HAL's actual gearing materially exceeds the notional gearing assumed by the CAA, meaning debt will reflect HAL's financing choices and may cost more than the costs of an efficiently financed company.
- HAL has a substantial share of non-GBP debt, which makes cost estimation more complex, and this is likely to increase in expansion scenarios.
- Heathrow has bonds novated from BAA Airports following restructure, which adds complexity.

iv. Longer-term ramifications and perverse incentives for HAL: An actual debt approach at H8 would create an expectation that future debt costs will also be passed through. If expansion proceeds, Heathrow may need to issue substantial further debt. In those circumstances, a weak approach creates a real risk of higher

[62] See IPs, paragraph Point 9.247.

[63] https://www.ofwat.gov.uk/regulated-companies/price-review/2024-price-review/final-determinations-models/

[64] See the airline community's letters to the CAA of 13 October 2025, 30 January 2026, 5 March 2026 and 8 May 2026.

gearing and windfall gains to equity from substituting debt for equity while continuing to be compensated for that higher gearing.

12.84. There is also evidence of inconsistency across parameters, with FTI suggesting that the cost of debt could revert to a notional approach in less volatile conditions, yet stating that the beta methodology changes at H8 because conditions are now less volatile.

12.85. The fact that a notional debt approach requires regulatory analysis and complexity is not alone reason to avoid implementing as an approach, particularly when this approach would protect consumers from inefficient financing and higher charges. An actual debt approach also requires significant assumptions, notably given the issues above and the treatment of non-GBP debt through GBP-equivalent values. In addition, as noted above, users have been restricted from interrogating the cost of debt approach despite repeated requests to access the underlying data.

12.86. CEPA also identified apparent problems with the CAA's and FTI's estimation of HAL's actual cost of debt, which it details in its report.

12.87. In order to avoid the issues above, CEPA therefore recommends that the CAA reverts to a notional debt allowance as a materially better approach for estimating HAL's efficient cost of debt and ensure that the consumer is not overcharged. CEPA's notional approach yields **an estimated cost of debt of 1.85% real-CPIH**. This is premised on an overall cost of embedded debt of 1.35%, an overall cost of new debt of 3.57% and the same share of a new and embedded debt as assumed by the CAA (15.4%). CEPA's calculations **demonstrate a significant overcharge of almost £2 per passenger** due to the CAA's proposing to allow for HAL's actual cost of debt.

Comparison: Cost of debt

Real, CPIH	**CAA**	**CEPA**
Cost of debt	**3.14%**	**1.85%**
Cost of new debt	3.93%	3.57%
Cost of embedded debt	2.77%	1.35%
Share of new debt	15.4%	15.4%
Issuance and liquidity costs	0.19%	0.15%

Source: IPs, CEPA report.

12.88. BA has strong concerns that the level of debt in the HAL structure is too high and that this informs the CAA selecting a level of notional gearing that is also too high. This leads to weaker financial ratios and places risk from Heathrow's choice of capital structure onto consumers. Credit rating agencies have been explicit around concerns on the level of debt in Heathrow's structure; for example, S&P (2026) state:

> *We think that the scale of the planned investments would likely add debt to Heathrow's already indebted capital structure, thus impacting the company's*

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ability to sustain FFO to senior debt above 8% and FFO to debt above 6% from 2029, when the third runway works are expected to begin."[65]

12.89. BA therefore contests the CAA's approach to compensate HAL for its actual cost of debt as it lacks justification, is unsuitable for a single regulated company and risks harming the consumer in the long-term by passing on HAL's higher debt costs and inefficient capital structure. This approach is all the more risky as it would not control for HAL's level of gearing – for which the overall Heathrow group rather than only the narrowly regulated entity is relevant – ahead of significant expansionary spend which will embed inefficient costs and higher charges for consumer for decades to come. An actual debt approach at H8 would create an expectation that future debt costs will be passed through to consumers however inefficient these may be.

Recommendation 6: Remove Heathrow-specific premium on cost of new debt

12.90. CEPA's report demonstrates that the CAA's analysis conducted to estimate a +12bps HAL-specific premium on primary issuances is not robust and no adjustment represents a materially better approach. A more coherent and robust approach is to rely on benchmark indices without a HAL-specific adjustment. We refer to the CEPA report for the community for the detailed analysis of those issues.

Recommendation 7: Remove indexation for nominal fixed rate debt

12.91. CEPA recommends that inflation indexation is removed for fixed rate debt. This is because:

i. Expected inflation is difficult to estimate reliably, such as absence of direct market evidence of CPIH which is the CAA's preferred inflation measure and uncertainty over the wedge between CPI, CPIH and RPI.

ii. Outturn inflation can depart materially from expectations, giving rise to significant windfall profits due to that policy alone. Recent experience shows greater volatility and sensitivity to shocks than was seen in the decade before the post-2022 inflation shock. Differences between expected inflation embedded in allowances and subsequent outturn inflation created what Ofgem has described as an 'inflation leverage effect'. Ofgem responded by moving to a semi-nominal cost of debt approach for RIIO-3.

12.92. A fixed-inflation approach is a materially better approach as:

i. It would give HAL greater certainty as its financing covenants are linked to the RAB

ii. It would not be creating intergenerational inequity in expectation or to change charges on an expected basis.

[65] https://www.heathrow.com/content/dam/heathrow/web/common/documents/company/investor/credit-ratings/sp/Heathrow_report_Feb_25_02_2026.pdf

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12.93. Furthermore, CEPA agrees with the CAA and FTI that it is currently most appropriate to not assume any additional compensation is provided by HAL to index-linked bondholders due to the transition in the RPI methodology used from 2030. Making an adjustment would be very subjective and not linked to evidence. We make further representations on inflation indexation in our response on the financial framework below.

Recommendation 8: Reduce notional gearing

12.94. CEPA considers that the CAA's use of a 60% notional gearing assumption is sub-optimal and that a lower level of notional gearing would better reflect evidence and better support financial resilience.

12.95. The CAA and FTI propose a 60% notional gearing assumption for H8. That is higher than:

i. The gearing of the airport comparator set (AENA, AdP, Fraport).

ii. The gearing adopted by the CAA for NR23, where a similar comparator set was used, leading to a notional gearing of 34%.

iii. The notional gearing adopted by other UK regulators for companies they regard as facing lower risk and therefore requiring a smaller equity buffer. Ofwat for PR24 reduced notional gearing to 55%. The water regulator indicated that a reduction to 55% gearing provides "*sufficient headroom to reflect the risks faced by the company, and to provide a capital structure that allows efficient access to the debt market through an investment grade credit rating.*"

12.96. Similarly, financial resilience is of the utmost importance, particularly ahead of expansion where Heathrow may need to issue substantial further debt. The COVID pandemic and the CAA's £300 million adjustment to HAL's RAB showed the importance of financial resilience in the case of Heathrow. The experience of Thames Water and with the potential for other regulated water companies to become sub-investment grade highlight the importance of financial resilience.

12.97. If the CAA retains 60%, it should explain why the approach adopted by other regulators is overly conservative, or why HAL is materially different.

Independent academic findings on improving the CAA's approach to estimating the beta

12.98. As mentioned above, the airline community has commissioned two independent academics on two distinct pieces of advice evaluating the CAA's IP methodology on beta estimation by Professors Robin Mason (University of Birmingham, Ordinary Member at the Competition Appeals Tribunal) and Donald Robertson (University of Cambridge).

12.99. Both academics identify significant issues with the CAA's choice of its pre-adjustment beta as it relies on unstable, inconsistent and inefficient beta estimates

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with embedded volatility giving rise to an overestimate. Professor Mason also identifies inconsistencies with the CAA's approach to the differences in risk in comparator airports and proposes a quantification of this relative risk differential for capacity constraints, single till and the TRS.

12.100. In fact, both academics believe the CAA has materially better, targeted and proportionate alternatives at its disposal to more accurately calculate the beta. We set out a summary of their analysis below and request the CAA to reflect their approaches in a revised beta estimate to improve the accuracy of the analysis.

Professor Robin Mason: An independent report on aspects of Heathrow's beta (May 2026)

12.101. Professor Mason's report focuses on two aspects of the CAA's beta estimation:

i. Whether the CAA's estimated beta series for the European airport comparators have been drawn from a statistically stable process and, if not, how that should affect the way the CAA sets a range for Heathrow's asset beta.

ii. The quantification of relative risk differentials for comparator airports for Heathrow specific features, especially capacity constraints, single till and the Traffic Risk Sharing (TRS) mechanism.

a. Inconsistent estimation of CAA's pre-adjustment beta

12.102. The CAA uses spot 2-year and 10-year OLS regressions to derive an empirical asset beta range of 0.47 to 0.70, with a midpoint of 0.59.

12.103. Professor Mason finds that the CAA's choice of its pre-adjustment beta in the face of instability in comparator airports is inconsistent and overestimates the beta as it gives too much weight to long-window estimates that may no longer be representative.

Stationarity test results for the comparator asset-beta series

Horizon	AdP	AENA	Zurich	Fraport
2-year	Non-stationary	Non-stationary	Non-stationary	Non-stationary
5-year	Non-stationary	Mixed: rejects unit root and level-stationarity	Non-stationary	Non-stationary
10-year	Mixed: rejects unit root and level-stationarity	Non-stationary	Mixed: rejects unit root and level-stationarity	Non-stationary

Source: Professor Robin Mason

12.104. In particular, while the CAA uses recent spot estimates and considers 2-year, 5-year and 10-year window, its pre-adjustment range of 0.47–0.70 gives decisive weight to the 10-year weighted-average estimate in setting the upper bound

estimate (and therefore determines the pre-adjustment beta by 50%). In an unstable setting, that is too strong: a 10-year estimate is informative, but it also blends older regimes that may no longer be representative of H8.

12.105. Indeed, the averaging across a long 10-year period includes materially different market and airport-risk conditions, including the pre-pandemic period, the pandemic shock, the reopening period, the inflation and interest-rate shock, and more recent market developments. Where beta is unstable, any smoothing property of the longer estimate is not an unqualified advantage. It may reduce noise, but it also dilutes the relevance of the estimate for the current period. Greater weight should normally be placed on shorter and medium-length estimation windows to reflect the current risk environment.

12.106. Professor Mason proposes not to simply identify a single historical mean as the CAA has done, but to use the available OLS evidence with judgement to define a robust and defensible forward-looking range based on four practical rules detailed further in his report.

12.107. More specifically, Professor Mason proposes to use the full set of OLS spot estimates as evidence on the empirical beta envelope, but to apply explicit judgement to that evidence. Recent estimates should receive particular weight in a non-stationary unstable setting. The 2-year and 5-year estimates should be treated as especially relevant to the current regime. The 10-year estimates should be retained as a cross-check but should not alone determine the upper bound unless there is a clear explanation of why the older data remain representative. This would have the advantage of improving the CAA's method to account for the implication of instability. The approach would provide a more transparent and economically grounded basis for setting the beta range, bounded by estimates that are most relevant to the current risk environment.

12.108. Professor Mason applies the recommended rules to the CAA's pooled comparator averages on a 2-year, 5-year and 10-year windows and concludes that:

i. The 10-year estimate of 0.70 is difficult to justify as a forward-looking estimate as it is too high once the non-stationarity evidence is taken seriously. A more defensible upper bound is 0.64. This still gives some weight to the 10-year evidence, but it avoids treating the current 10-year estimate as the sole determinant of the upper bound estimate.

ii. In contrast, the CAA's lower bound of 0.47 is close to the current 2-year average and therefore grounded in recent market data reflective of the regulatory horizon.

iii. The central (not midpoint) estimate should not be chosen by taking the midpoint of a range whose endpoints are generated by different estimation windows, as the CAA has done. They are outputs from windows with different sensitivities to current and older data. Given the instability of data, the central estimate should be a forecast for the regulatory period, not simply the arithmetic midpoint of some historical range. A more defensible central estimate can be derived by

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computing a simple weighted average that gives greater weight to shorter windows: first 2-, and then 5-year estimates, while retaining some weight on the 10-year estimates. This produces results in the range of 0.50–0.58, with an average and median of 0.53.[66] These figures can be compared with the midpoint of the recommended range 0.47–0.64, i.e. 0.56.

12.109. Professor Mason therefore recommends a **pre-adjustment asset beta of 0.53**. This sits well below the CAA's estimate of 0.585, and in line with CEPA's recommendation of 0.53 set out above.

Comparison: Empirical asset beta estimate prior to relative risk adjustment and TRS

	CAA	CEPA	Professor Mason
Empirical (pre-adjustment) asset beta	0.585	0.53	0.53

Source: IPs, CEPA report, Professor Mason report.

12.110. Professor Mason's approach is **materially better than the CAA's mechanistic application of the beta estimates** as it is **simple, predictable, and reflects the market evidence and the regulatory horizon, while also encoding the exercise of defensible regulatory judgement**. Its purpose is **not to create a new mechanical formula, but to discipline the judgement required under non-stationarity**. It shows that a central estimate of 0.53, is **supported by the evidence**. In all cases, the appropriate central estimate sits below the CAA's midpoint of 0.585, having a material impact on charges.

b. Relative risk adjustment: adjusting for differences in risk to comparator airports

12.111. Professor Mason agrees with the CAA that there is no perfect listed comparator for HAL and that HAL cannot sensibly be treated as equivalent to a network utility as it remains exposed to traffic. He also agrees with the CAA that an adjustment, reflecting HAL's specific features and circumstances, is both appropriate and proportionate.

12.112. While there is agreement by the CAA that the TRS mechanism is a HAL-specific feature that reduces HAL's traffic risk, Professor Mason argues that there are two other systematic risk reductions that the CAA has not taken adequately into account: capacity constraints and till structure.

i. Heathrow's capacity constraint means that HAL is protected by excess demand which reduces its exposure to systematic traffic risk (exposure reduction)

[66] This range is generated by taking a distribution of weights on the 2-year, 5-year and 10-year spot beta estimates, with the weights satisfying three criteria: (i) the 2-year weight is the largest of the three, but no larger than 0.80; (ii) the 5-year weight is the second largest; (iii) at least some weight is given to the 10-year spot. Note that the mean/median of the distribution of betas generated by this process is not the same as the midpoint of the range: the induced beta distribution is slightly skewed and is not simply uniform.

ii. Heathrow's single till regulation mitigates HAL's exposure to the equity consequences of traffic-driven commercial revenue shocks as those revenues are periodically reset at every price control (mitigation).

12.113. **Professor Mason argues that this can already be done via the formula implied by the CAA's calculation of the reduction to HAL's asset beta from the TRS mechanism**[67]. According to this "reduced form" formula, the reduction in HAL's risk differential compared to utility networks (β_N) brought about systematic risk reductions such as the TRS is subtracted from HAL's pre-adjustment beta calculated from the comparator airports (β_0). The extent of the reduction in HAL's risk is determined by the extent of the protections to traffic risk-exposure (t) and by the extent to which HAL's traffic-related equity risk is mitigated by the framework, rather than being borne by investors (r).

$$\boldsymbol{\beta = \beta_0 - tr(\beta_0 - \beta_N)}.$$

Source: Professor Robin Mason based on CAA's Initial Proposals

12.114. Indeed, the approach recognises that airports are more traffic-exposed than utilities and that HAL sits somewhere between them owing to its protections due its capacity constraint and single till. A higher t and r factors mean Heathrow should be moved further away from the raw airport comparator and further toward the utility benchmark because Heathrow is not fully airport-like in its traffic sensitivity and because equity shocks are absorbed by the regulatory framework.

Capacity Constraints

12.115. Professor Mason finds that the CAA accepts that capacity constraints and lower demand risk can matter in principle. However, the CAA considers that comparator airports, especially the two main Spanish airports within AENA (Madrid and Barcelona) are also highly constrained. This is an evidence question as opposed to a question of principle.

12.116. We have described above why this analysis by the CAA is factually incorrect and superficial when looking at runway capacity which is the hard capacity limit at most airports. Madrid, Barcelona and Paris CDG all operate well below their declared runway limits, in contrast to Heathrow which operates at or close to its runway limits for most of its operating day. Professor Mason agrees with this view and highlights that even if the CAA's analysis may imply that the gap between Heathrow and the comparator airports has narrowed, it does not follow that the gap has fully closed, or that the remaining difference is too small to affect the calibration of parameter *t*.

Till structure

12.117. Professor Mason finds that single till is one of the clearest and most economically relevant differences of HAL against comparators which are in dual till. It changes the way sustained commercial gains and losses are retained by equity shareholders and offset through future aeronautical charges. Indeed, **Professor**

[67] See Initial Proposals, Table 9.7.

Mason's report finds that the CAA does not deny that till structure may matter in principle. The CAA's objection is rather on CEPA's method in its report supporting the airline Alternative Business Plan of October 2025, finding that the quantification of the effect is too sensitive to assumptions. I return to this issue below.

12.118. While Professor Mason agrees that the CAA's criticisms of the CEPA method may be valid, he finds that **the CAA's conclusion that single till should play is not correct**. The CAA issue treats the question as a binary choice. The correct response to a fragile direct-adjustment method is to ask whether the same recognised underlying economic effect can be handled more simply and robustly elsewhere. The reduced-form formula expressed above provides exactly such a route through parameter r.

12.119. The CAA further relies too heavily on broad arguments about regulatory discretion, investor preference for commitment, and the absence of hindsight. These arguments may not be wholly irrelevant, but they are not specific to single till. They are generic points about regulation and review structure.

12.120. In fact, **the CAA's own calibration of the impact of the TRS on the beta is exactly the same type of judgement for which it criticises CEPA in relation to single till.** Professor Mason stresses that if the CAA accepts that route for TRS, then it cannot object to the same route for single till solely on grounds of imprecision.

Application to the CAA's formula

12.121. Professor Mason finds that the CAA has effectively set t in the range 0.7–0.9 and r at 0.5 on the basis of the TRS alone.

12.122. While there is recognition that the choices of both t and r are, to some extent, subject to regulatory judgement, as they are not parameters that can be read directly off the data, they are neither free policy choices. The CAA's choices still should be disciplined by economic structure, internal consistency, and plausibility bounds.

12.123. Professor Mason therefore argues that capacity constraints and single till operate in a clear direction, to increase t and r respectively, in addition to the impact from the TRS, and therefore reduce HAL's asset beta.

i. **Capacity constraints increase t from 0.7-0.9 to a central estimate of 0.85**. This applies a modest increase bringing the central estimate to 0.85 to account for HAL's particularly acute capacity constraints. This sits slightly above the midpoint of the CAA's 70–90% TRS adjustment.

ii. **Single till increases r from 0.5 to 0.75** to reflect the attenuation of traffic-related commercial risk. This is on the basis that single till protects HAL's commercial revenues (around a third of its total revenues), compared to the TRS which protects the remaining two thirds. However, as single till reflects a lagged reset compared to the TRS, Professor Mason halves the 50% share of revenues protected from the TRS, resulting in a 0.25 increment. Professor Mason finds

that the overlap between single till and TRS is limited in practice and therefore has to be reflected separately.

12.124. As a result of these increased adjustments to the pre-adjustment beta identified above, **Professor Mason recommends a central estimate for the asset beta of 0.42**, compared to the CAA's estimate of 0.50.

12.125. Professor Mason's approach is therefore materially better to the CAA's methodology. It **recalibrates and improves the CAA's implicit formula to apply regulatory judgement consistently and coherently across the different systematic risk reductions for HAL that the CAA itself has acknowledged (capacity constraint, single till,** TRS), rather than applying the adjustment for one factor alone (TRS). Professor Mason's recommendation applies the CAA's approach in a **simple, predictable, transparent, consistent and evidence-backed manner, while remaining anchored in the same comparator set, the same formulaic methodology employed by the CAA, and the same broad regulatory framework**.

12.126. These targeted improvements have an important reducing effect on the beta, and therefore **a material impact on charges**. BA estimates that the CAA's beta-overestimation across both the pre-adjustment beta and the lack of relative risk adjustment is adding around £1.30 per passenger. For those reasons, we urge the CAA to improve on its approach to improve the accuracy of the beta estimate and avoid overcompensating HAL at the consumers' expense.

The effect of capacity constraints and single till on asset beta

	CAA Low	CAA High	CAA Mid	**Professor Mason Recommended central estimate**
Pre-adjustment asset beta	0.47	0.70	0.585	0.53
Network utilities beta	0.36	0.36	0.36	0.36
Exposure (t)	0.90	0.70	0.80	0.85
Mitigation (r)	0.50	0.50	0.50	0.75
Adjusted asset beta	0.42	0.58	**0.50**	**0.42**

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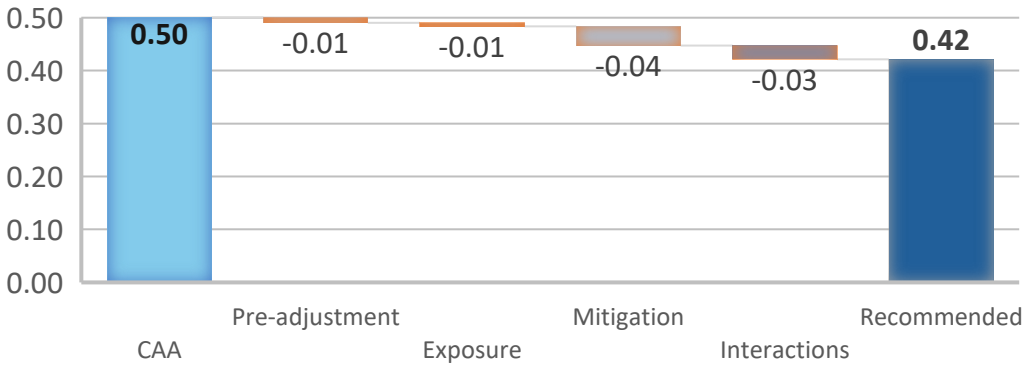
Difference between CAA's point asset beta and Professor Mason's recommended central estimate



Source: Professor Robin Mason

12.127. Professor Mason's recommendation of an adjusted beta of 0.42 is aligned with CEPA's post-adjustment beta of 0.42 above, albeit applying the adjustment framework in a different way. This sits well below the CAA's estimate of 0.50 and has a significant impact on the level of charges for the consumer.

Comparison: Adjusted beta following relative risk adjustment and TRS

	CAA	CEPA	Professor Mason
Empirical (pre-adjustment) asset beta	**0.585**	**0.53**	**0.53**
Adjusted beta	**0.50** TRS alone	**0.42** Capacity constraint, single till and TRS	**0.42** Capacity constraint, single till and TRS

Source: CAA Initial Proposals, CEPA report, Professor Mason report.

Professor Donald Robertson: Estimating beta (May 2026)

12.128. Professor Robertson's report focuses on the CAA's estimation of the pre-adjustment beta.

12.129. In a similar vein to Professor Mason, Professor Robertson's report details how the CAA's purely mechanical application of an unweighted OLS regression relies on unstable, inconsistent and inefficient beta estimates with embedded volatility not aligned with the regulatory horizon. When those principles are not respected, the OLS estimator, even if technically correct, may not yield the best forward-looking measure required for a regulatory price-control.

12.130. Professor Robertson finds that the CAA has not tested, justified or treated for the fact that the unweighted OLS regression may include outliers with influential observation, time-varying volatility and structural breaks (e.g. COVID). The CAA's use of multiple windows of 2-year, 5-year and 10-year assumes that beta is stable within those windows and to the future without checking for persistence of instability. The approach equally places a disproportionate weight to volatile periods that may not be reflective of the regulatory horizon.

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12.131. Professor Robertson proposes instead an explicit, model-based framework that selects estimation techniques according to the underlying data issues, models time variation directly where relevant, and assesses a range of estimates to reflect uncertainty. This approach is materially better as it is coherent, statistically robust, transparent in its assumptions, and better suited to informing regulatory judgement on allowed returns.

Regulatory precedent: French ART's scepticism on the use of long-window estimates in the asset beta.

12.132. In its recent opinion on the upcoming Economic Regulation Agreement at AdP for 2027-2034, the French ART has recognised that the use of long-window estimate for the beta is not representative as they skew the estimates upwards by including atypical periods linked to COVID:

> "*[T]he eight-year observation period used to estimate the beta parameter [by AdP] is not satisfactorily aligned with the choices made for the other parameters, including the risk-free rate and the cost of debt**, and includes atypical periods, particularly those linked to the health crisis, which are likely to skew the estimates upwards***."[68]

Updated WACC estimate based on CEPA's and independent academics' recommendations

12.133. Based on its recommendations above, **CEPA provides an indicative pre-tax real WACC of 4.68% CPIH-real (equivalent to 3.74% vanilla).** This estimate integrates CEPA's recommendations on calculating the asset beta, including the pre-adjustment empirical beta and the post-adjustment beta including the relative risk adjustment and the TRS. CEPA's post-adjustment beta is in line with the adjusted beta recommended by Professor Mason, at 0.42.

12.134. CEPA's indicative WACC is materially lower figure than the CAA's proposal of 5.85% pre-tax CPIH-real (4.86% vanilla) by 120 basis points and demonstrates that a lower figure aligned with the airline Alternative Business Plan continues to be justified.

12.135. **If the CAA proceeds with its proposed WACC, it will overcharge the consumer and over-remunerate HAL more than £1.2 billion in additional returns, which are not justified given its level of risk against its comparator airports and its notional debt. This translates to more than £3 per passenger in unjustified charges on the consumer, and an overcompensation of at least £1.2 billion to HAL, leading to higher charges and inefficient costs.**

12.136. **This over-remuneration excludes further overcompensation granted by additional protections granted to HAL in the proposed regulatory package for which the choice of a lower point estimate in the WACC range may be required.**

[68] See ART opinion on ADP Economic Regulation agreement 2027-2034, 20 Apri 2026, paragraph 230. https://www.autorite-transports.fr/actualites/avant-projet-de-cre-daeroports-de-paris-lart-formule-ses-recommandations-pour-securiser-un-cadre-economique-equilibre-dans-la-mise-en-oeuvre-du-projet-industriel-de-lexp/

We therefore urge the CAA to reconsider its proposal and adopt the materially better alternatives tabled by CEPA and the independent academics to establish a consistent, robust and accurate method of estimating the WACC and avoid harming the consumer. The CAA should equally consider whether the choice of a mid-point range is justified given the additional risk protections granted to HAL by the regulatory package (see below).

H8 WACC Comparison (real, CPIH)

	CAA H8 IPs	CEPA H8
Cost of New debt	3.93%	3.57%
Cost of Embedded debt	2.77%	1.35%
Share of new debt	15.4%	15.4%
Issuance and liquidity costs	0.19%	0.15%
Cost of debt	3.14%	1.85%
RfR	2.33%	2.08%
TMR	6.82%	6.72%
EMRP	4.49%	4.64%
Asset beta	0.50	0.42
Debt beta	0.075	0.075
Equity beta	1.14	0.77
Cost of equity (post-tax)	7.44%	5.63%
Notional Gearing	60%	50%
Vanilla WACC	4.86%	3.74%
Assumed tax rate	25%	25%
Cost of equity (pre-tax)	9.92%	7.51%
Pre-tax WACC	5.85%	4.68%

Source: CEPA analysis

Remedying the cumulative impact of HAL's multiple risk protections which lead to an over-compensation of HAL

12.137. The CAA's H8 Initial Proposals have not resolved our long-standing concerns from the H7 lessons learned exercise over the regulatory package overcompensating HAL on multiple layers at the expense of the consumer. In fact, the Initial Proposals continue to provide HAL with cumulative protections under a low-risk regulatory framework. Those protections reduce HAL's exposure to traffic shocks, financing conditions, inflation, input cost pressure and uncertain investment needs and overcompensate HAL for its profile of risk. We consider that an allowed return above truly efficient costs coupled with an overly generous regulatory package generate the perverse incentive on HAL to maximise the RAB regardless of consumer value.

Our view on HAL's H8 balance between risk and reward

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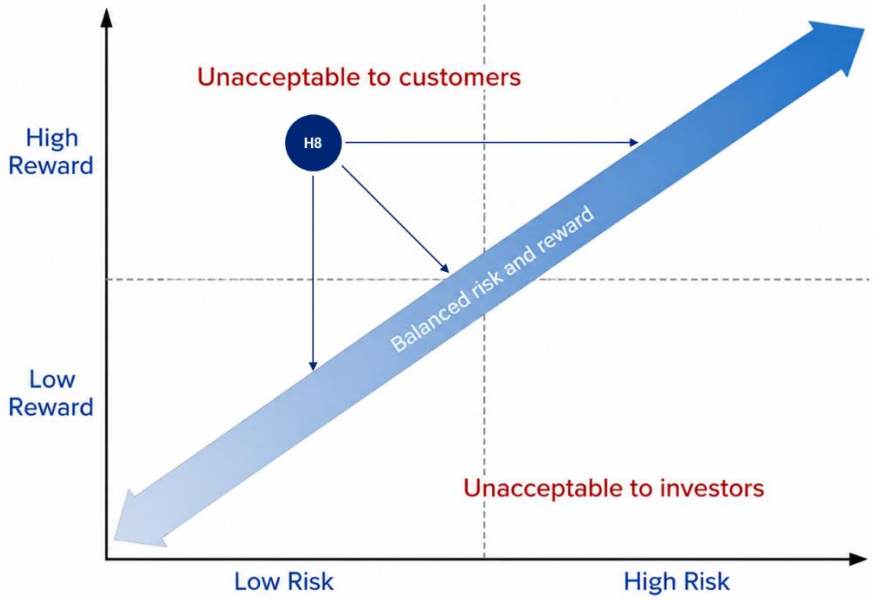

12.138. The CAA should address this overcompensation as a priority, and can do so by

i. reducing HAL's risk, and/or

ii. reducing HAL's return by adjusting the point estimate in the WACC.

12.139. On the latter remedy, this is a policy already applied by the CAA. For Heathrow's early expansion costs spent in 2025-2026, the CAA has issued a draft decision in April 2026 allowing HAL to recover those costs using a WACC from the bottom of the H7 range, in recognition of the lower risk profile of these costs[69].

12.140. Furthermore, the French ART's opinion on the upcoming Economic Regulation Agreement 2027-2034 at AdP, stipulating that the positioning in the WACC range is dependent on the risk sharing between AdP and users.

[69] See CAP3238, paragraph 3.96.

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French ART opinion on AdP Economic Regulation Agreement 2027-2034, April 2026

It should first be noted that, in the airport sector, the WACC is not an independent parameter detached from the regulatory framework within which it operates: ***the fair return on capital invested within the regulated scope cannot, in principle, be assessed independently of the actual risk-sharing arrangements*** *resulting from the contractual framework comprising the [regulatory agreement] and its annexes.* ***It must, therefore, remain proportionate to the risks actually borne by the operator****.*

This framework has a twofold objective. On the one hand, it must ensure a fair return on the capital invested by the operator in order to preserve their ability to finance the necessary infrastructure. On the other hand, it must prevent any excessive remuneration resulting from the exercise of market power to the detriment of users. The aim is therefore to ***ensure that the operator's remuneration is not disconnected from its actual exposure to risk****, in accordance with the principle cited above [...], without depriving it of the fair remuneration to which it is legitimately entitled* ***in view of the reality of that risk****.*

The WACC included in the draft [regulatory agreement], which will be submitted to the Authority for its opinion, must be based on more robust methodological choices and be ***consistent with the proposed risk-sharing arrangement****.*

Recommendation: Review the WACC in order to [...] where appropriate only adopt the upper limit of the range in return for a ***rebalancing of risk sharing between the operator and users****.* (our emphasis).[70]

12.141. We also address the financeability aspect in our response on the financial framework below.

HAL's layers of overcompensation under the regulatory package and proposed remedies

12.142. We list those protections and overcompensation of HAL under the regulatory package, as well as our proposed remedies below.

1. Overstated beta

12.143. As analysed above, the CAA has overestimated HAL's beta in two ways, leading to an overcompensation of HAL for its level of risk:

i. CAA's unweighted OLS approach for calculating the pre-adjustment beta in the face of instability in comparator airports is inconsistent and overestimates the beta as it gives too much weight to long-window estimates that may no longer be representative. CEPA, Professor Mason and Professor Robertson all identify this issue. Similarly to CEPA's recommendations, Professor Mason proposes a

[70] See ART opinion on ADP Economic Regulation agreement 2027-2034, 20 Apri 2026, paragraphs 218, 220, section 6.1.5 and Recommendation 3.

refinement of this estimate to remedy this instability, with **a central estimate of 0.53**.

ii. The CAA has not applied risk reductions against the airport comparator groups to reflect HAL's lower systematic risks (single hub capacity constraint, single till, TRS) but only adjusted for one factor alone (TRS). Both CEPA and Professor Mason identify this issue. Professor Mason proposes an additional adjustment to the beta beyond the TRS (and in addition to the pre-adjustment calculation above) to account for capacity constraints and single till leading to a **central estimate of 0.42**.

12.144. These remedies would address the issue of overestimating HAL's beta, including overestimating its lower risk compared to its riskier comparator groups and overestimating a beta that is unstable and not reflective of the regulatory horizon.

2. Inflation protections

12.145. Inflation protection is extensive, as the CAA estimates a real WACC by deflating to inflation forecasts, yet indexing the RAB to outturn inflation. In recent years, this has allowed and over-inflating the RAB by outturn inflation in periods of high inflationary shocks, allowing HAL to pass the entirety of that inflation shock to consumers. The CAA recognises that this happened for instance during the start of the Russia-Ukraine war.[71] Between 2019-2025, HAL's regulatory accounts demonstrate a 28% growth in the RAB due to inflation alone, from £16.6 billion to £21.3 billion.

12.146. We welcome the CAA's proposal to deflate fixed rate debt with a fixed inflation assumption and index the part of the RAB, such as the part financed by debt. However, this would not resolve the issue as the remainder of the RAB would continue to be indexed to outturn inflation. The CAA has proposed no remedy for this risk protection and has rejected our requests for a cap and collar or risk sharing mechanisms without sufficient explanation. We refer to our views in the financial framework chapter.

12.147. If the CAA maintains an outturn inflation indexation for the remainder of the RAB, an alternative remedy would be to combine its proposal on fixed rate debt indexation to a fixed rate inflation above with the choice of a lower point estimate in the WACC range.

3. Debt protections

12.148. The proposed H8 framework significantly limits HAL's exposure to financing risk. The CAA proposes to use HAL's actual cost of debt – including HAL's more expensive senior debt for the cost of embedded debt – as opposed to a notional company. In addition, the CAA uses a HAL-specific uplift for both embedded and new debt. This passes on costs and risks of HAL's gearing up and possibly inefficient debt structure to consumers. Furthermore, the cost of new debt is subject to an

[71] See IPs, paragraph 10.72.

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indexation mechanism, providing protections for inflation. There is also what we consider to be an unjustified specific Heathrow premium on primary issuances rather than relying on benchmark incidents.

12.149. CEPA has proposed remedying this over-remuneration of HAL by moving from an actual to a notional If the CAA retains for debt allowances. Alternatively, should the CAA retain its proposals, it should recognise the protections afforded to HAL through the choice of a lower point estimate in the WACC range.

4. Traffic Risk Sharing (TRS) mechanism

12.150. The CAA already proposes a reduction of the beta to account for the risk reductions to HAL against its comparator airports. We welcome the reduction in beta from the TRS mechanism, given that it clearly allocates risk away from HAL and onto consumers. We note our comments in the traffic forecast and financial framework chapter over the overlaps between the TRS and other traffic protections, such as the traffic forecast shock factor.

12.151. BA also considers that the TRS will most likely be applied in a skewed way in H8 and we would argue for the CAA to reflect this imbalance in a higher downwards adjustment to HAL's asset beta than already applied.

12.152. Furthermore, BA is strongly concerned that the TRS creates significant moral hazard by allowing Heathrow to pass on the financial impact of its delayed delivery of critical capacity projects onto consumers – notably the terminal occupancy programme needed to deliver a [REDACTED] passenger increase. BA considers this a perverse incentive structure and calls on the CAA to mitigate it through targeted regulatory adjustments which we explain further in the financial framework section.

5. Passenger shock factor

12.153. The central passenger forecast includes a downwards adjust via a traffic shock factor, based on historical events such as the Gulf War, 9/11 and volcanic ash clouds. We explained in the traffic forecast section why the passenger shock factor ought to be removed as it has failed to deliver on its objective of delivering a more accurate traffic forecast, as well as its overlaps with the TRS mechanism which the CAA appears to acknowledge in its Initial Proposals.[72]

12.154. Absent the removal of the shock factor, we have proposed to the CAA how to improve its estimation in our response on the traffic forecast. However, this would not resolve the concern over the overlap between the shock factor and TRS. If the CAA retains the shock factor, we recommend the CAA choose a lower point estimate in the WACC range.

[72] See IPs, paragraph 10.93: "*Business-as-usual traffic shock events are already catered for through existing traffic risk policies such as the "shock factor" adjustment in our traffic forecast for the H8 Period [.] Reducing the outer band [for the TRS] to 5% could risk the TRS overlapping with existing traffic policies designed to deal with less extreme traffic deviations*"

6. Asymmetric risk adjustment

12.155. HAL also receives further protection against extreme demand shocks. The CAA include an asymmetric risk allowance that will be funded by users to the value of over £122 million (nominal) in additional revenues over H8, based on an assessment the probability and impact of pandemic-scale events that we consider is not supported. It is also unclear how the CAA controlled for the other traffic protections in calculating this allowance. We refer to our concerns with the calculation of the ARA and the additional levels of protection it provides to HAL in our chapter on the financial framework.

12.156. If the CAA retains the asymmetric risk allowance, we consider that this would be accompanied with the choice of a lower point estimate in the WACC range reflecting this protection.

7. Taxation

12.157. The CAA is proposing to set a pre-tax allowance for HAL. We explain in our response to the financial framework how this would create a perverse incentive but also protect HAL by allowing it to increase gearing and reduce its tax liability, while making windfall profits. In line with the CAA's findings in H7, we support the introduction of a tax uncertainty mechanism. This is all the more relevant given the CAA's proposals to allow HAL's actual cost of debt (thus not controlling for the level of gearing) and ahead of significant expansionary spend.

12.158. However, the CAA appears to have now ignored its position in H8. If the CAA proceeds with no remedy on this issue, it should accompany its proposals for pre-tax allowances with the choice of a lower point estimate in the WACC range.

8. Other protections

12.159. The CAA's regulatory package provides further significant risk protections to HAL. These include pension deficit recovery, full cost pass-throughs to airlines such as through the Other Regulated Charge framework, the possibility to increase the capex envelope by 5% as well as in case of uncertain capex requirements and effective pass-through of HAL's increases in Business Rates at each re-evaluation.

12.160. All these significantly reduce HAL's risk exposure and should be reflected through the choice of a lower point estimate in the WACC range.

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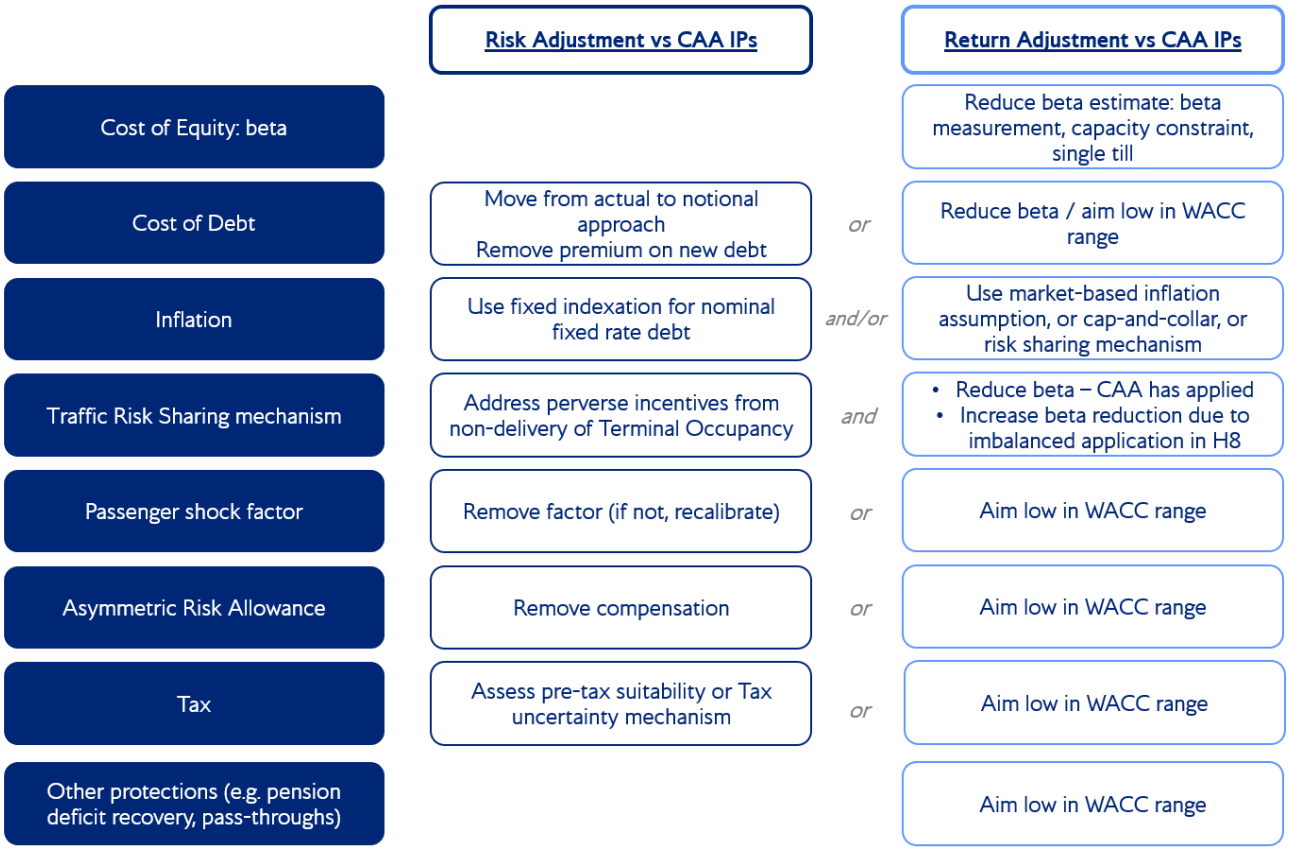
Layers of HAL's over-compensation under the regulatory package and proposed remedies



Source: BA analysis

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13. Financial Framework

The CAA's proposed financial framework fails to deliver a balanced "fair bet", instead overcompensating Heathrow for multiple sources of risks it faces, both through the WACC and a series of overlapping risk protections. The CAA has not undertaken a fresh assessment of the framework following H7, relying instead on precedent despite changed evidence and its own identified shortcomings, and has applied its judgement inconsistently and without transparency.

Significant concerns arise across key components. The use of the Fixed Asset Register to set depreciation is neither transparent nor robust, given the absence of disclosure to airlines and limited regulatory assurance, raising risks of overstated depreciation to the detriment of consumers. Similarly, the current approach to taxation fails to address incentives created by a pre-tax WACC and does not reflect the need for proper regulatory scrutiny of HAL's effective tax rate. On inflation, while partial reforms are welcome on fixed indexation, the framework continues to expose consumers to inflation-driven windfall gains.

The package also includes multiple, overlapping risk protections – particularly through the TRS, ARA and other traffic risk mechanisms – which collectively skew outcomes in HAL's favour, create perverse incentives, and weaken accountability for delivery, including on critical capacity investments, most notably the long-delayed Terminal Occupancy. **These protections are not consistently reflected in the financial framework and further contribute to overcompensation.**

Against this backdrop, **the resulting financial framework exceeds what is required to ensure financeability**, with the CAA's own analysis indicating headroom against key metrics. We consider that this supports a **recalibration of the package**, including lower compensation and revised assumptions (e.g. gearing), alongside a more thorough forward-looking assessment of financeability and affordability. Critically, ensuring that the framework is robust, balanced and efficiently calibrated is essential to support credible and financeable expansion while protecting consumers from bearing unnecessary risk and cost.

13.1. Before considering the individual proposals by the CAA, we note that the regulatory package should represent a fair bet. This should account for both the level of compensation provided to Heathrow and the distribution of possible outcomes.

13.2. We consider that the compensation provided to Heathrow is higher than the level of risk it faces. This is relevant not only to the cost of capital – where the CAA has proposed an overestimated beta and protecting HAL for its actual cost of debt – but also to the financial framework. Our responses below should be read in conjunction with our chapter on the WACC, including the section on HAL's overcompensation.

13.3. We are disappointed that the CAA does not appear to have revisited the suitability of the financial framework. The H7 determination was developed while uncertainty around the COVID-19 pandemic remained, and decisions were being made without the evidence now available on how circumstances have evolved. The CAA instead appears to have treated H7 as the benchmark and considered changes only where it deemed them absolutely necessary. However, the CAA appears to have applied its

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judgement inconsistently, not transparently, going against its previous findings, and based on factual inaccuracies, therefore failing to adopt materially better alternatives to ensure efficient costs.

13.4. Given the issues identified with the financial framework – including by the CAA itself in both its lessons learned work and the H8 Initial Proposals - we would have expected a fresh assessment of the suitability of the H8 framework. Regulatory policy ought to be periodically reviewed for effectiveness, accuracy and regulatory certainty, and reconsidered if those objectives have not been delivered.

Depreciation

13.5. The CAA states that, because using Heathrow's Fixed Asset Register (FAR) is "*logical, transparent, understood by stakeholders and produces a stable profile, [it] considers that it remains an appropriate basis for determining the allowance for regulatory depreciation.*"[73]

13.6. To suggest that the figures used by the CAA are "transparent" and "understood by stakeholders" is untrue. The FAR has not to date been shared been with users despite multiple requests and it cannot therefore be deemed as being "*transparent, logical or* understood". Airlines have requested information on the FAR since the publication of the Heathrow BP in July 2025. These requests have been refused by HAL[74] and highlighted by the community to the CAA[75] on multiple occasions. However, the CAA did not share the information for its proposal in the IPs, nor do the IPs explain why this information has not been made available, leaving users unable to interrogate the assumptions used or whether these are in the interest of consumers.

13.7. Similarly, we understand that the CAA has not requested, and therefore has not had sight of, Heathrow's Fixed Asset Register. We consider this problematic in the sense of the CAA undertaking sufficient assurance of data presented by Heathrow. Auditors focus on backwards-looking reporting, and these depreciation figures are included on a forward-looking basis, meaning that the CAA cannot suitably discharge its duties through auditors or accountants.

[73] See IPs, paragraph 10.30.

[74] See response paper by HAL dated October 2025 to airline Query Log Item 13 submitted on 8th August 2025 requesting transparency on existing assets under FAR and understanding the approach taken on new assets, including original spend not sharing the FAR and referring to HAL's published regulatory accounts: "*[HAL's] depreciation approach is based on an inflated version of the Fixed Asset Register (FAR) and uses a straight-line method by year. While the FAR calculates depreciation monthly and at more a granular level, [HAL's] method ensures that the Regulatory Asset Base (RAB) and FAR remain broadly consistent over time, even if not identical*".

[75] See the community's letters to the CAA of 13 October 2025, 30 January 2026, 5 March 2026 and 8 May 2026

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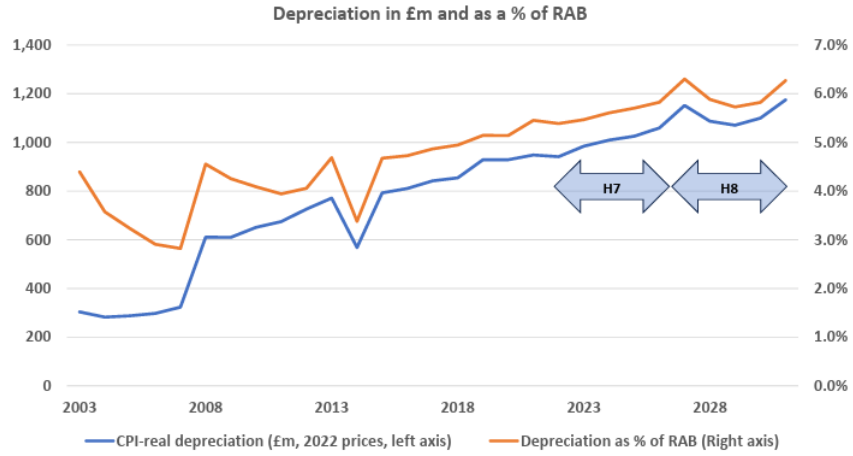
13.8. The higher 'run-off' rate over the last two decades leads to higher depreciation charges. Figure 10.1 from the CAA is shown below.



Source: CAA Initial Proposals

13.9. Higher depreciation charges would generally need to be justified by either: i) a greater share of shorter-life assets in the overall asset mix; or ii) shorter technical asset lives for RAB assets of each type.

13.10. We have not had sight of the FAR, so we cannot determine which of these two drivers is leading to the higher depreciation charge. If the driver is a greater share of shorter-life assets in the mix, a relatively linear upward trend does not appear consistent with investment cycles. If the driver is shorter technical lives for individual assets, the CAA should properly interrogate why this is the case and whether Heathrow is managing its assets appropriately. If Heathrow is able to accelerate depreciation cashflows of existing assets while putting forward higher capex for new replacement assets, this is likely to be at the expense of consumers.

13.11. The CAA's rationale for presenting alternative run-off rates of 5% and 7% is also unclear. The presentation appears to suggest that depreciation per passenger per unit of RAB is a relevant metric and that the 5% and 7% figures are suitable reference points. The effective H8 run-off rate is c.6%, and the CAA appears to take comfort from the fact that 5% would produce lower depreciation figures while 7% would produce higher depreciation figures without justification.

13.12. We therefore request that the CAA:

i. obtains Heathrow's FAR.

ii. shares the FAR with airlines and relevant stakeholders[76].

iii. reviews the driver of increasing depreciation charges.

13.13. For the purposes of calculating the BA proposed price cap, we have adopted a pragmatic mid-point position on asset lives, reflecting both the available evidence

[76] If full FAR is not shared, a second-best outcome would be a list of categories, outstanding balances and asset lives, alongside calculations of how inflation indexation of the RAB is dealt with under such the statutory approach.

and the uncertainty around the CAA's approach. In the absence of compelling countervailing evidence, we consider a 20-year average asset life to be a robust and appropriate proxy, grounded in HAL's audited statutory accounts. However, we recognise the possibility that the CAA may accept higher depreciation rates consistent with HAL's proposed 18-year asset lives upon further review of the available evidence, subject to appropriate transparency and consultation with users. Rather than rely on either assumption in isolation, we therefore take a balanced approach by applying a mid-point estimate of 19 years. This provides a proportionate and evidence-based compromise, capturing the range of plausible outcomes while avoiding over-reliance on a single, uncertain regulatory decision.

Taxation

13.14. In H7, the H7 lessons learned exercise and our response to the H8 method statement, we have expressed our view that the CAA should review Heathrow's effective tax rate to satisfy itself that setting a notional pre-tax allowance is appropriate. This is particularly important now that the CAA is proposing to use Heathrow's actual cost of debt directly in the WACC and thus would not control for the level of HAL's gearing (debt), for which the overall Heathrow group, rather than only the narrowly regulated entity, is relevant.

13.15. As CEPA stated in its report accompanying the airline Alternative Business Plan submitted to the CAA in October 2025, a pre-tax WACC creates perverse incentives for HAL to increase gearing above the notional gearing assumption to reduce its taxable profits and tax liabilities and thereby increase its financial returns.

13.16. Indeed, in H7 the CAA stated that *"[a]s there may be differences between the assumed corporate tax rate and the rate of corporation tax experienced by HAL during the H7 period, we consider that [the pre-tax WACC approach for determining an allowance]* ***should be coupled with a tax uncertainty mechanism*** *[...] We propose to implement any adjustments arising from this tax uncertainty mechanism* ***through a revenue adjustment in the H8 price control period****, but, if these adjustments were to be significant, we retain the flexibility to make a RAB adjustment instead."* (our emphasis)[77]

13.17. However, the CAA appears to have now ignored its own position indicating in the IPs "*if stakeholders provide evidence to suggest that an alternative approach is appropriate, we will consider these representations ahead of our Final Proposals.*"[78]

13.18. This statement does not provide a balanced assessment, as airline stakeholders do not have sight of Heathrow's tax information and therefore cannot provide such evidence. Given that requests for information on actual debt costs and the FAR have been rejected by HAL and not responded to by the CAA, we do not consider that a request by airlines for evidence on tax would generate a different outcome. Nor

[77] See CAA H7 Final decision (CAP2524D), Section 3: Financial issues and implementation, paragraph 12.44.
[78] See IPs, paragraph 10.47.

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should it fall to airline stakeholders to undertake this analysis, as this is the responsibility of the regulator with a duty to protect the consumer from overpaying.

13.19. We also note that the depreciation analysis indicates that asset lives and values appear to be changing, which could affect tax.

13.20. Indeed, an assumption of no impact on tax is on the basis of simplicity and the fact that a "stable" capex profile is being proposed by the CAA for H8. However:

i. We note that CAA mentions that its approach could change with expansion

ii. It may be too difficult to change the approach "mid-way" the price-control. For example, multi-billion pound expansion related capex during H8 is already being discussed and therefore there could be significant differences between a theoretical tax calculation and an actual one.

iii. We note that the CAA wishes to treat expansion decisions separately, but "tax related" decisions cannot be dealt with in isolation.

13.21. We therefore request that the CAA:

i. Assesses the effective tax rate paid by the HAL business. In doing so, the CAA ought to conduct a more detailed and balanced assessment on tax recognising the above issues, and considers where the tax uncertainty mechanism should be introduced for the H8 period to contain HAL's perverse incentives, in line with the CAA's own findings.

ii. Considers whether or not this supports the use of a pre-tax WACC approach at H8.

Inflation indexation

13.22. We welcome the CAA's proposal to consider deflating fixed rate debt by a fixed inflation forecast with the same fixed forecast being used to index the RAB. We consider this an appropriate remedy to address the issues on 'inflation leverage' as well to reduce the likelihood of windfall gains and over-inflating the RAB by outturn inflation in periods of high inflationary shocks, resulting in higher charges for consumers. The CAA recognises that this happened for instance during the start of the Russia-Ukraine war.[79] The use of a medium-term inflation forecast approach does not address that problem, or the value market participants place on inflation indexation.

13.23. However, the CAA's approach would not entirely remove the risk of over-inflating the RAB or avoiding the mismatch between forecast inflation in deflating the WACC and outturn inflation used to index the RAB. The CAA notes that its proposed policy above would mean that only the portion of the RAB that is assumed to be funded by fixed rate debt would be indexed by the fixed rate inflation forecast. The

[79] See IPs, paragraph 10.72.

remaining portion of the RAB assumed to be funded by equity and index-linked debt would continue to be indexed to outturn inflation.

13.24. As the CAA has expressed a preference to maintain a fully real WACC to avoid any frontloading charge impacts in H8, we believe it should be looking at mechanisms to contain the risk of windfall profits and higher charges for consumers in periods of high inflationary shocks for the remaining part of the RAB as well. We therefore ask the CAA to:

i. Explain why the medium-term inflation forecast it is considering would address this risk, especially as they "*remain subject to some degree of forecast error, particularly during periods of economic disruption*"[80]

ii. Justify why its view that a "cap and collar" mechanism for inflation driven returns or a risk sharing mechanism to allow customers to benefit when inflation windfall gains occur are unenforceable. The CAA states that they would be complex to administer, require monitoring and require recovery of adjustments.

However, the CAA has to date enacted multiple adjustments to the price cap formula within the regulatory period that is updated during the annual charges consultations (for example, for investment delays and overspends/underspends, quality of service bonuses and the TRS mechanism adjustment). The CAA is monitoring the application of those adjustments by HAL annually. We therefore consider that the CAA's justification over a presumed complexity is not substantiated and is inconsistent given implementation to date of other adjustments. These adjustments would protect consumers from being overcharged and there seem to be no apparent reasons why they should not be taken forward.

In addition, cap and collar is enacted in other regulated sectors and are therefore in line with regulatory precedent. Fo instance, cap and collar approaches on returns have been used for interconnectors in energy and through Return Adjustment Mechanisms for energy networks. The CAA itself is considering a cap and collar mechanism on longer term returns as part of the shortlist of future regulatory frameworks for HAL in its recently launched consultation.[81]

13.25. We therefore request that the CAA:

i. Makes any provisional decision available ahead of Final Proposals (to give stakeholders sufficient time to respond to policy changes).

ii. Adopts a 'fixed indexation' approach.

iii. Reflects the use of CPIH rather than CPI in the cost of capital (discussed separately).

[80] See IPs, paragraph 10.76.
[81] See CAP3251, paragraphs 5.43-5.47.

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iv. Considers how to remedy the risk for any parts of the RAB not indexed to fixed inflation (such as cap and collar)

v. If not adopting fixed indexation, it looks to aim down in the WACC range for financial risk (discussed in the WACC section above in relation to the layers of overcompensation afforded by the regulatory package).

Traffic Risk Sharing (TRS) mechanism

13.26. We welcome the reduction in beta from the TRS mechanism, given that it clearly allocates risk away from Heathrow and onto consumers. We have made comments in the WACC chapter on how the implicit formula used by the CAA to adjust HAL's beta downwards for the TRS affect should be applied consistently and coherently across the different systematic risk reductions for HAL that the CAA itself has acknowledged (capacity constraint, single till, TRS).

13.27. We have also set out how the combination of protections afforded by the CAA are overcompensating HAL and how they should be addressed to ensure a balanced regulatory backage for the consumer, either through the WACC or in the other parameters of the financial framework. Our responses below should therefore be read in conjunction with our responses in the WACC chapter.

a. Overlap of TRS with other traffic risk protections for HAL

13.28. The CAA notes the risk of the "*TRS overlapping with existing traffic risk policies designed to deal with less extreme traffic deviations*" if the outer band were reduced to 5%[82]. More specifically, the CAA states that:

> *"Business-as-usual traffic shock events are already catered for through existing traffic risk policies such as the "shock factor" adjustment in our traffic forecast for the H8 Period [.] Reducing the outer band [for the TRS] to 5% could risk the TRS overlapping with existing traffic policies designed to deal with less extreme traffic deviations*".[83]

13.29. We have also analysed this overlap in the traffic forecast section of our response, including using a shocked forecast as the basis for the TRS mechanism and our view that the shock factor ought to be withdrawn for having to delivered on its objectives and its overlap with other traffic risk protections. In the ARA section below, we discuss the concept of overlap and the protections available to Heathrow under the proposed H8 regulatory framework.

b. Moral hazard for HAL's key capacity delivery in H8 and impact on consumer – terminal occupancy

13.30. As mentioned in our response on the capital envelope, BA is deeply concerned about the moral hazard risks created by de-risking Heathrow through the TRS mechanism. Parts of the H8 investment programme are necessary to deliver H8

[82] See IPs, paragraph 10.93.
[83] See IPs, paragraph 10.93.

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traffic, notably terminal occupancy work ([REDACTED]) that is due to be delivered in H8 and is expected to deliver a [REDACTED] passenger capacity increase per annum. [REDACTED].

13.31. It is critical that Heathrow does not benefit from delaying these key capacity programmes, including through any change to passenger forecasts. We contest the notion of HAL being protected through the TRS from any reductions in traffic caused, by passing on shortfalls onto the consumer, because of its own failure to deliver these delayed projects that the CAA itself has scored highly in its H8 capital prioritisation.

13.32. We note in particular the perverse incentives for HAL to delay those projects at the expense of the consumer, including on customer experience and punctuality, while at the same time passing on the financial consequences of its inaction to consumers.

13.33. While we acknowledge that the CAA does not set specific investments, it should identify the mechanisms necessary to avoid HAL benefitting from those perverse incentives to harm the consumer. We therefore recommend that the CAA:

i. A TRS deadband under which consumers would not pay any adjustment to Heathrow if the relevant capacity were not delivered.

ii. Applies a larger downward adjustment to HAL's asset beta to account for those additional protections.

iii. Applies a clawback mechanism for any benefits HAL generates by being able to pass on the cost of lower passengers associated with this programme onto the consumer.

iv. Carve out this programme from the ambit of the TRS mechanisms to remove those perverse incentives on HAL.

c. TRS kicking in "one way" in H8 due to capacity constraints

13.34. Moreover, with Heathrow expected to be operating at its capacity constraint for the duration of H8, the likelihood the TRS mechanism kicking in for any shortfalls in traffic is significantly higher than any additional traffic. This would benefit HAL to a greater extent that airlines and the consumer, as the latter would be expected to fund (part of) HAL's shortfall. Given the skewed way in which the TRS is expected to apply in H8 we would argue for the CAA to reflect this imbalance in a higher downwards adjustment to HAL's asset beta than already applied.

Asymmetric Risk Allowance

13.35. HAL also receives further protection against extreme demand shocks. The CAA include an asymmetric risk allowance (ARA) that will be funded by users to the value of over £122 million (nominal) in additional revenues over H8.

13.36. The ARA is calibrated using a series of assumptions in relation to the frequency of any pandemic event, the impact on passenger numbers, elasticities and the cost of

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capital. The results are therefore highly sensitive to inputs which themselves are largely subjective.

13.37. At Q6, the CAA considered that the shock factor adjustment to passenger forecasts controlled for asymmetry of risk in volume forecasts, even in the absence of a TRS mechanism.

13.38. In H7, the CAA introduced the TRS mechanism, including compensation of 105% of revenues outside the 10% threshold band, and added the ARA, while retaining the shock factor. This represented a significant change with additional layers of risk protections for Heathrow, with risks allocated to users. Please see our analysis on the layers of HAL's overcompensation afforded by the regulatory package in the WACC section of our response.

13.39. In particular, HAL is implicitly compensated by £124 million (nominal) of additional revenues over H8 due to the shock factor, based on the CAA's IPs. If the shock factor were to be retained in H8, without prejudice to our position that it ought to be withdrawn, we consider that there is an overlap this is sufficient to address any risk asymmetry without applying a further revenue uplift to Heathrow. We are unclear how the CAA has suitably controlled for this additional shock factor compensation when estimating the ARA.

13.40. We request that the CAA:

i. Removes the ARA. Our BA proposed price cap is premised on the assumption that the ARA ought to be removed.

ii. If not, present the equivalent threshold factor that would be needed to remove the ARA. In any event, as ARA forms part of the multiple layers of protection creating an imbalanced regulatory package in HAL's favour, reflect through the choice of a lower point estimate in the WACC range, as we noted in our responses in the WACC section above.

13.41. If the CAA considers that there is no overlap and there remains a shortfall, we would welcome the CAA indicating the potential 'outside threshold' factor (currently 105%) that would create equivalence with a zero ARA outcome.

Financeability and Affordability

13.42. The CAA's analysis indicates that, in expectation, the notional company easily meets all relevant financeability metrics under the CAA's H8 Initial Proposals. This implies that there is room to reduce the level of compensation from the IPs without being constrained excessively by financeability.

13.43. Any financial metrics should take into account Heathrow's 'Excellent' business risk profile and the layers of protections seen through the lens of being a regulated infrastructure provider.

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13.44. We have highlighted in our response on the WACC that we consider that the level of debt in the HAL structure is too high and that this informs the CAA selecting a level of notional gearing that is also too high. This leads to weaker financial ratios and places risk from Heathrow's choice of capital structure onto consumers. Credit rating agencies have been explicit around concerns on the level of debt in Heathrow's structure; for example, S&P (2026) state:

> *"We think that the scale of the planned investments would likely add debt to Heathrow's already indebted capital structure, thus impacting the company's ability to sustain FFO to senior debt above 8% and FFO to debt above 6% from 2029, when the third runway works are expected to begin."*[84]

13.45. Indeed, HAL's choice of capital structure cannot be allowed to constrain the CAA's regulatory options in H8 or for the broader reform options set out in the recent shortlist published by the CAA in CAP3251. One of the options that could be considered by the CAA is to reduce reliance for expansion financeability on a single highly indebted operator.

13.46. We are concerned that the CAA has not sought to assess financeability or affordability beyond the H8 period. This risks non-NPV neutral adjustments being made by the CAA on financeability grounds in future controls, when changes in policy for H8 may alleviate those concerns.

13.47. We request that the CAA:

i. Models financeability and affordability out for four additional price controls under two scenarios: i) 'steady-state capex' run-rate, and ii) under the latest official projections of capacity expansion. These for instance include firmed up estimates on early expansion costs for 2025-2026 (part of an ongoing separate CAA process) and estimates on further early expansion and overall expansion costs.

ii. Reduces notional gearing in the WACC and for financial modelling.

iii. Considers policies adopted by other economic regulators for improving financial resilience for HAL.

iv. Considers options for reducing reliance for expansion financeability on a single highly indebted operator.

[84] https://www.heathrow.com/content/dam/heathrow/web/common/documents/company/investor/credit-ratings/sp/Heathrow_report_Feb_25_02_2026.pdf

14. Price cap, profiling and holding price cap

Implementing our recommendations set out in our response results in **a materially lower price cap than the CAA's Initial Proposals, with an average charge of £24.48 (2024 CPIH)** and a reduction of 15% relative to the CAA's proposal of £28.80. We consider the CAA's **proposed 2027 holding cap to be overstated**, noting further charge increases from the proposed recovery of early expansion costs from users. In order to avoid a repeat of the unintended consequences from the 2022-2023 holding caps, the **CAA should also address risks from its design of the holding cap**, including the treatment of inflation-related windfalls. **We do not support the CAA's proposed front-loading of increases, as a smoother profile better enables our business planning and reflects our investment constraints**, and note that a flat real cap does not in itself deliver stability given inflation, in-period adjustments and the compounded effect of early expansion costs.

14.1. Based on our analysis, implementing the recommendations set out in our submission leads to an average price cap of £24.48 in 2024 CPIH prices, against the CAA's proposal for an average charge of £28.80 (also in 2024 CPIH). Our proposal represents a reduction of 15% against the CAA's proposal. The unprofiled trajectory implies a starting charge of £25.13 in 2027, reducing to £23.44 in 2031.

14.2. Our proposal further represents a reduction of 14% to the CAA's assumed H7 average charge of £28.40, and an 9% reduction to the average of £27.0 over 2024-2026 (in 2024 CPIH) where traffic reflects steady-state conditions post-pandemic.

14.3. We detail the building blocks retained in our estimates below:

BA forecasts – H8 building blocks

£m 2024, CPIH-real	2027	2028	2029	2030	2031	Total
Operating costs	1,488	1,518	1,507	1,487	1,480	7,480
Regulatory depreciation	1,045	1,061	1,067	1,085	1,084	5,342
Allowance for asymmetric risk	0	0	0	0	0	0
Allowed return (incl. tax)	914	928	934	941	939	4,655
Gross revenue requirement	**3,446**	**3,507**	**3,508**	**3,513**	**3,503**	**17,478**
Commercial and other revenues (incl. cargo and ORCs)	1,265	1,285	1,299	1,328	1,342	6,519
Commercial Revenues	*1,123*	*1,143*	*1,158*	*1,188*	*1,203*	*5,815*
ORCs	*123*	*123*	*123*	*123*	*122*	*614*
Cargo	*19*	*19*	*18*	*17*	*17*	*90*
Net revenue requirement	**2,181**	**2,222**	**2,209**	**2,185**	**2,161**	**10,958**
Passengers, m	86.8	88.2	89.5	90.9	92.2	447.6
Unprofiled yield per pax	**25.13**	**25.19**	**24.68**	**24.04**	**23.44**	**24.48**

Source: BA analysis, CAA Initial Proposals

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Comparisons between BA and CAA IPs mid-point building block forecasts (full period)

£m 2024, CPIH-real	H8 BA	H8 CAA IP	Difference
Operating costs	7,480	7,790	-309
Regulatory depreciation	5,342	5,740	-398
Allowance for asymmetric risk	0	107	-107
Allowed return (incl. tax)	4,655	5,769	-1,114
Gross revenue requirement	**17,478**	**19,406**	**-1,928**
Commercial and other revenues (incl. ORCs)	6,519	6,781	-262
Commercial Revenues	*5,815*	*5,403*	*412*
ORCs	*614*	*1,289*	*-674*
Cargo	*90*	*90*	*0*
Net revenue requirement	**10,958**	**12,625**	**-1,666**
Passengers, m	447.6	438.3	9.3
Unprofiled yield per pax (£ per pax)	**24.48**	**28.80**	-4.3

Source: BA analysis, CAA Initial Proposals

14.4. We note that the CAA is proposing a profiled **holding cap for 2027** of £26.62 (mid-point of £25.79 and £27.44 CPIH-real). We believe that this is too high when compared to our proposal. This number would equally be higher following the outcome of the CAA's proposed decision on to levy early expansion costs on users.

14.5. While we note the CAA's intention to consult separately on the level of the one-year holding price cap, it must remain mindful of potential unintended consequences. In particular, the 2023 holding cap was set on the basis of inflation assumptions materially above outturn, allowing HAL to retain upside without any requirement to return that benefit. The CAA should therefore consider ex ante how windfall gains or losses will be treated. We would welcome further engagement with the CAA on mechanisms to avoid a repeat of this outcome.

14.6. With regards to the phasing of the price cap over H8, note that the CAA's Initial Proposals assume front-loading of charge increases over the first two years, followed by a flat profile in real terms. The stated rationale is to provide airlines with greater "predictability" and facilitate incorporation into pricing, with the CAA suggesting this approach reflects airline preferences.

14.7. While phasing is less of an issue under the BA proposed cap (as we are proposing a reduction), we nonetheless comment on the CAA's rationale. BA does not support front-loading high increases to deliver "stable prices" later in the period. Where increases are unavoidable, our preference is for a smoother profile over the regulatory period. This would provide us time to implement mitigating actions, recognising constraints from business planning cycles in the early years, and better align with our investment profile.

14.8. In fact, we do not consider that a flat real price cap in the later years of the period necessarily delivers stability. In practice, charges will continue to vary with inflation and a range of other adjustments embedded within the price cap formula, as well as the cumulative impact of the CAA's proposed decision to recover HAL's early expansion costs from users, potential further expansionary spend and the outcome of the 2029 Business Rates re-evaluation.

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14.9. With respect to the individual components of the charging formula, we consider that the S factor is broadly operating as intended, although the design of the deadband may warrant further review. Similarly, the bonus factor provides a degree of predictability, notwithstanding our rejection of service level bonuses set out in the section on service levels (MTIs) above.

15. Business Plan Incentive

We strongly agree with the CAA's assessment that HAL's H8 Business Plan is of "low quality", reflecting repeated shortcomings from H7 in transparency, engagement and evidencing as well as the pronounced information asymmetries built into the current regime. The CAA's findings point to **widespread and fundamental deficiencies** across core areas, including insufficient transparency, **lack of a "golden thread"** linking proposals to demonstrable consumer benefits or priorities, weak cost and financing evidence, lack of robust optioneering, lack of efficient targets, and incomplete and inconsistent financial and operational data. These failings have **materially constrained effective scrutiny by the CAA airlines and resulted in a plan that is neither sufficiently evidenced nor appropriately ambitious**, as reflected in the substantial downward adjustment in the CAA's Initial Proposals. We consider that these deficiencies **clearly justify a BPI penalty, preclude the case for any bonus**, and, more broadly, have undermined the Constructive Engagement process, requiring the **CAA to apply a very high bar to any late information**. We also request the CAA to **address the repeated airline concerns on transparency and engagement**, which are similar to its own findings, in its Final Proposals.

Our agreement with the CAA's classification of HAL's Business Plan as "low quality"

15.1. We support the CAA's view to classify HAL's H8 Business Plan as "low quality" under the Business Plan Incentive (BPI) introduced in the H8 Method Statement. As recognised in the CAA's lessons learned exercise, it was pivotal to avoid the transparency and engagement shortcomings experienced in H7. However, many of those issues were repeated, demonstrating the pronounced information asymmetries built into the current regime. Our response should be read alongside our chapter on H8 Constructive Engagement, the gaps in HAL's Business Plan, and the standards and process the CAA should apply when considering any new information from HAL.

15.2. We agree with the CAA's assessment of HAL's material deficiencies across several core areas. These include a lack of granularity and transparency in opex assumptions, inconsistencies in presentation across years, and a failure to adopt a robust bottom-up approach. The CAA also noted that ORC information did not comply with Business Plan guidance. HAL should not benefit, through increased allowances, from deficiencies in evidence that were within its control.

15.3. More specifically, we agree with the CAA's finding of numerous failures in HAL's Business Plan against the requirements in the H8 Method Statement and Business Plan Guidance. The CAA's "Fail to Meet" (FTM) ratings consistently point to

fundamental shortcomings in transparency, evidencing of efficiency and value for money, linkage to consumer priorities, as well as the robustness and completeness of core financial, cost and investment data underpinning HAL's plan.

i. **Transparency:** Failure to provide key non-commercial information (e.g. historic data, cost detail), limiting stakeholder scrutiny and engagement.

ii. **Efficient costs and financing:** Insufficient evidence and comparability of cost and financing assumptions against independent benchmarks.

iii. **Affordability and value for money:** Assertions made but not supported by robust evidence, particularly in light of significant charge increases.

iv. **Trade-offs and optioneering:** No clear demonstration that trade-offs (e.g. affordability vs service levels) were properly assessed, with weak justification of preferred options.

v. **Link between research, plan and consumer benefits ("golden thread"):** Failure to clearly evidence how consumer insights directly inform the business plan and investment programme and the expected benefits for the consumer.

vi. **Assurance of consumer engagement:** Limited visibility of assurance findings and outcomes, and no clear assurance that the plan reflects consumer priorities.

vii. **Resilience**: Focus on existing processes, with insufficient articulation of additional planning required to enhance future resilience for consumers.

viii. **Environmental Sustainability**: Insufficient detail on how H8 initiatives contribute to delivery of Net Zero. Weak optioneering and lack of robust justification that proposed investments are efficient and necessary.

ix. **Opex granularity and consistency:** Forecasts lack required detail and are not consistently aligned with historic baselines.

x. **Opex drivers and assumptions:** Insufficient explanation of cost drivers, changes, and efficiency assumptions.

xi. **Commercial revenues:** Lack of granularity and consistency across periods. Insufficient evidence on key revenue drivers and forecasting methodology.

xii. **Other Regulated Charges (ORCs):** No meaningful disaggregation (e.g. by facility). Missing cost drivers, forecasts, and linkage to traffic assumptions.

xiii. **Capex and Cost Assessment:**

- **Efficiency assumptions:** Lack of transparency and justification for the application of efficiency challenges (including profiling).

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- **Project-level detail and benchmarking:** Mature projects lack sufficient cost build-up and benchmarking evidence. Less mature projects lacked adequate justification of need and cost.

xiv. **Cost incentives:** No clear statement or assessment of the balance of incentives across the regulatory framework.

xv. **Target credit rating:** No balanced assessment of costs vs benefits or linkage to financing needs and investment programme.

xvi. **Regulatory depreciation and RAB:** No transparent reconciliation of RAB evolution. Insufficient treatment beyond impact on charges.

xvii. **Tax:** No forecast of tax liabilities or reconciliation against regulatory allowances.

15.4. We also highlight HAL's continued refusal to share key information, in particular on the cost of debt and the Fixed Asset Register. This has materially undermined users' ability to scrutinise two key components of the cost base: financing costs for the cost of capital and depreciation.

15.5. Moreover, we strongly agree with the CAA's concerns regarding the absence of a clear "golden thread" linking consumer research, service quality, capex and demonstrable consumer benefits. A Business Plan cannot be considered of good quality if consumers cannot clearly see what improvements they will receive.

15.6. The scale of the adjustment in the CAA's Initial Proposals – approximately £2.2 billion lower than HAL's proposed revenue requirement and £3.8bn lower in capex allowances over H8 – demonstrates that the Business Plan was not appropriately ambitious in its targets, as required by the Method Statement.

15.7. Taken together, the number and breadth of areas where the CAA has identified the need for further information, clarification and correction demonstrates that the Business Plan falls materially short of the required standard.

A penalty under the BPI should be triggered

15.8. HAL's failure to meet multiple Business Plan criteria provides clear justification for a penalty under the BPI. While the CAA has previously indicated that a full penalty would apply where deficiencies are widespread, it may consider applying a proportionate penalty where some criteria are met. We consider that this is the case here.

15.9. The failing of four BPI criteria provides clear evidence there is a need to trigger a penalty. We note that the CAA's has indicated in the past that it would only apply a full penalty if the BP were of low quality across a significant number of areas. Noting that there are some criteria that has been satisfied, then the CAA could consider applying a significant portion of such penalty. This would reflect the number and breadth of areas where HAL's Business Plan has failed against the CAA's requirements.

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Safeguards for new information

15.10. However, HAL's failures are not solely relevant to the calibration of a penalty. The lack of adequate, timely and transparent information has materially hindered users' ability to engage, assess and scrutinise the plan in line with the Constructive Engagement framework. This has in turn materially undermined the Constructive Engagement process given the reliance placed by the CAA on airline challenge which is a key aspect of the price control consistent with its primary duty to further the interests of users of air transport service.

15.11. The CAA should therefore exercise particular caution in how it treats any new information provided by HAL after the conclusion of Constructive Engagement. The purpose of a high-quality Business Plan is to enable meaningful engagement and scrutiny ex ante. A Business Plan that fails to meet the CAA's own quality standards should not be capable of being remedied through late submissions outside of the defined process.

15.12. In fact, allowing deficiencies to be remedied ex post risks undermining that framework. Indeed, it would undermine the integrity of the process, bypass structured scrutiny, risk perverse incentives and regulatory gaming, and risk reintroducing allowances previously rejected due to insufficient evidence. This would be at the detriment of the consumer. We therefore consider that a very high bar must apply to any late submissions, limited to narrow clarifications with clear consumer benefit that the airlines can test meaningfully and respond to.

15.13. We refer the CAA to Section 3 ("H8 Constructive Engagement and HAL's Business Plan") for further detail on the safeguards that the CAA ought to apply.

No bonus can be justified

15.14. A related point concerns the bonus side of the BPI. Our position remains that producing a compliant, fit-for-purpose Business Plan is the baseline obligation of a regulated monopoly, not an exceptional achievement warranting additional reward. The BPI bonus that the CAA introduced should be reserved for plans that demonstrate genuine above-and-beyond engagement and evidence quality throughout the Constructive Engagement process—plans that materially supported airline engagement, reduced the need for regulatory re-work, and enabled a well-evidenced and appropriately ambitious settlement. That standard has clearly not been met here.

Lack of CAA assessment of airline transparency concerns

15.15. Notwithstanding our agreement with the CAA's assessment of the quality of HAL's Business Plan, we are disappointed that the CAA has not substantively responded to the repeated airline concerns regarding HAL's lack of transparency and refusal to share key information contained in the letters by the airline of community of 27 May 2025, 8 August 2025, 13 October 2025, 30 January 2026 and 5 March 2026. Indeed, the community's concerns are very similar to the CAA's identified shortcomings. A letter was subsequently sent by the community on 8 May 2026 regarding the CAA's

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lack of response on instructing HAL to share its debt book and Fixed Asset Register to enable the community to interrogate the respective cost of debt allowances and depreciation retained by the CAA.

15.16. We request that the CAA reflects those concerns in its Final Proposals.

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Appendix A – Opex: Comparisons of BA proposals against HAL Business Plan and CAA Initial Proposals

Opex Baseline: Comparisons between HAL baseline, CAA baseline and BA proposals

Baseline Opex (2024 CPI)	Category	HAL 2024 baseline	CAA adjustments	CAA Adjusted baseline	BA further challenges	BA adjusted baseline
Security Staff	Staff	197.1	-23.5	173.6	[...]	[...]
Other Operational Staff	Staff	131.1	-8.3	122.9	0.0	122.9
Non-Operational Staff	Staff	155.7	-6.6	149.0	0.0	149.0
Pensions and Capitalised Staff Costs	Staff	1.0	-1.0	0.0	0.0	0.0
Other Operational Costs (excl. PRM and IT)	Other opex	420.3	9.0	429.3	[...]*	[...]
PRM costs	Other opex	65.2	-13.0	52.2	0.0	52.2
IT & computer services maintenance	Other opex	80.8	-8.1	72.8	0.0	72.8
Insurance	Insurance	19.7	5.9	25.6	-5.9	19.7
Facilities/ Maintenance	Maintenance, facilities management & equipment	239.7	-4.2	235.4	-2.4	233.0
Rent and Rates	Rent & rates	116.4	0.0	116.4	0.0	116.4
Utilities	Utilities (excluding distribution contract)	126.1	-16.7	109.4	0.0	109.4
Distribution Contract	Electricity distribution contract	33.1	0.0	33.1	0.0	33.1
Adjustment for POD parking	Other opex	-2.7				
Total OPEX		**1583.5**	**-66.5**	**1519.7**	[...]	[...]

* "Other Operating Costs" BA challenges: Elimination of MTIs rebates (£15 million), Inclusion of capitalized Rents and Rates ([REDACTED]), implementation of a 5% Other opex efficiency assumption ([REDACTED]) = [REDACTED]

Source: BA analysis; HAL H8 Business Plan, CAA H8 Initial Proposals

Opex overlays – Comparisons between HAL baseline, CAA baseline and BA proposals

Opex Overlays (£m, 2024 CPI)	2027	2028	2029	2030	2031	Total
HAL overlays (BP)	47.0	51.0	51.0	52.0	55.0	256.0
CAA overlays (IP)	7.5	8.1	8.1	3.2	3.2	30.1
BA proposal overlays (IP Submission)	[...]	[...]	[...]	[...]	[...]	[...]

A positive figure indicates an increase in opex. The main difference between CAA overlays and BA overlays are the differences in the assumptions on Security overlays

Source: BA analysis; HAL H8 Business Plan, CAA H8 Initial Proposals

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Appendix B – Commercial revenues: Comparisons of BA proposals against HAL Business Plan and CAA Initial Proposals

Commercial Revenue Baseline: Comparisons between HAL baseline, CAA baseline and BA proposals

Revenue sub-category	Category	HAL 2024 baseline	CAA adjustments	CAA Adjusted baseline	BA further challenges	BA adjusted baseline
Catering	Retail and catering	88.6	8.4	97.1	8.4	105.5
Retail	Retail and catering	272.7	15.0	287.7	7.5	295.2
Other Retail	Retail and catering	49.1	2.5	51.5	1.2	52.8
Bureaux	Retail and catering	23.0	0.0	23.0	0.0	23.0
Other services	Retail and catering	3.7	0.0	3.7	0.0	3.7
Car parking	Surface Access & Car Parking	175.6	0.0	175.6	6.2	181.8
Other surface access (adds Taxi feeder Park)	Surface Access & Car Parking	27.3	0.0	27.3	[...]	[...]
Service revenue	Service revenue (excl. surface access)	69.6	0.2	69.7	6.8	76.6
TDOC	Terminal drop-off charge revenue	53.1	0.0	53.1	0.0	53.1
Property	Property	145.0	1.4	146.4	1.4	147.8
Rail	Rail	117.8	3.5	121.2	0.0	121.2
Other Commercial Revenue	Other commercial revenue	7.3	0.0	7.3	0.0	7.3
Cargo	Cargo revenue	21.4	0.0	21.4	0.0	21.4
Total Commercial Revenue (incl. cargo revenues)		**1054.1**	**30.9**	**1085.1**	[...]	[...]

Source: BA analysis; HAL H8 Business Plan, CAA H8 Initial Proposals

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Commercial revenue overlays – Comparisons between HAL baseline, CAA baseline and BA proposals

Com Rev Overlays (£m, 2024 CPI)	2027	2028	2029	2030	2031	Total
HAL overlays (BP)	-17.9	-18.7	-19.4	3.1	3.1	-49.8
CAA overlays (IP)	-17.9	-18.7	-19.4	3.1	3.1	-49.8
BA proposal overlays (IP Submission)	[...]	[...]	[...]	[...]	[...]	[...]

A positive figure indicates an increase in commercial revenues. The main difference between CAA overlays and BA overlays are 1) the differences in the assumptions on MSCP4 TDOC revenues and 2) Allocation of a portion of the increases of business rates to retailers

Source: BA analysis; HAL H8 Business Plan, CAA H8 Initial Proposals

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