



Civil Aviation Authority
Westferry Circus
Canary Wharf
London EH14 4HD

cc: economicregulation@caa.co.uk

18th January 2022

Dear Paul,

Economic regulation of Heathrow Airport Limited: H7 Initial Proposals on outcome based regulation ("**OBR**")

1. INTRODUCTION

- 1.1 Thank you for the opportunity to provide comments on the economic regulation of Heathrow Airport Limited ("**HAL**") for H7 and specifically, the proposals of the Civil Aviation Authority ("**CAA**") on OBR. These proposals are set out in (i) Section 4, Chapter 14 of the "*Economic regulation of HAL: H7 initial Proposals – H7 Price Control Consultation*" (CAP2265) (the "**Initial Proposals**"), (ii) the "*Working paper on outcome based regulation*" (CAP2264) (the "**OBR Working Paper**"), and (iii) the Arcadis report titled "*OBR Targets Assessment*" (CAP2274A) (the "**Arcadis Report**"), (together the "**OBR Proposals**").
- 1.2 This letter constitutes the response of Virgin Atlantic Airways ("**VAA**") to the CAA's Initial Proposals in relation to the OBR framework that should be applied to HAL for H7. This response should be read in conjunction with VAA's response to the consultation on the CAA's Initial Proposals, dated 17 December 2021, which sets out VAA's views on other aspects of the Initial Proposals for H7.
- 1.3 VAA is grateful for the short extension granted by the CAA to respond to the OBR Proposals but considers that overall the timeframe has remained limited (and significantly shorter than VAA had requested) to put together a comprehensive response, particularly in light of the other deadlines which the CAA has set in this time period. VAA has therefore produced this response in as much detail as possible given the time available and reserves the right to comment further on certain matters as set out below.
- 1.4 Overall, VAA supports in principle the move to a framework that is based on developing a set of outcomes with associated measures and targets. However, VAA is disappointed at the CAA's proposed approach on how to implement OBR. In particular, despite extensive engagement by VAA on this area of regulation over a long period of time (VAA notes that the CAA's first consultation on OBR was in 2016, to which VAA responded), the CAA's OBR Proposals do not appear to properly take into account and/or fail to engage with the detailed submissions which VAA (as part of the airline community) has previously made on OBR and more work could be done by the CAA to explore the issues at hand.
- 1.5 OBR is an area which is evidently linked directly to the interests of consumers. Decisions implemented in this area should be driven by analysis of consumers' needs and experience when using Heathrow airport, particularly in the context



of the substantially higher passenger charges that HAL is proposing should be implemented for H7.

- 1.6 VAA considers that the CAA should do more in this area to gather the relevant research and data, in order to drive decisions based on impartial and robust information. In some areas of the OBR Proposals, it is regrettable that the CAA does not yet appear to have done so. For example, the CAA appears to have deferred to HAL to control the area of consumer research which drives the outcomes and measures within an OBR framework; this is an unacceptable position given that HAL's approach to consumer research will likely be biased. In addition, as outlined in the Arcadis Report, there are areas of OBR where critical data to make an informed decision has not been supplied by HAL. It is also not clear why the CAA has chosen to disregard some of the proposals in the Arcadis Report, particularly in relation to targets.
- 1.7 In order to assist the CAA in taking these matters forward, VAA outlines below the steps that the CAA should take going forward to develop a framework that furthers consumers' interests. VAA urges the CAA not just to re-consider the approach based on the evidence to date, but to dedicate the necessary resources to gathering the necessary detailed information, data and analysis to enable it to engage fully with the questions that need to be answered before OBR should be implemented. This would include carrying out further independent consumer research, not least in the area of key driver of satisfaction analysis that would help better determine the major outcomes to be measured. Independent consumer research and expert analysis is currently clearly lacking in relation to the ability to move to daily measurements and in certain areas, the CAA's OBR Proposals suggests a lack of knowledge and awareness of essential operational elements of the airport, such as baggage movements, that are critical to the overall consumer journey.
- 1.8 In the circumstances, VAA reiterates the submissions which it has previously made as to the proper approach to OBR which should be adopted. VAA does not repeat here the content of these submissions which it requests that the CAA reads in full. These previous submissions include:
 - 1.8.1 "*High level Outcomes 1106*" sent on 11 June 2021 from VAA to the CAA, as found at Appendix 1,
 - 1.8.2 "*H7 OBR – Interim position update*" sent on 16 July 2021 from VAA to the CAA, as found at Appendix 2, and
 - 1.8.3 "*Outcome Based Regulation*" sent as part of the document titled "*Annex 6.1 – Heathrow H7 RBP Feedback – Airline OBR Response_Final*" which was submitted as part of the airlines' response to the RBP to the CAA in February 2021. This is found at Appendix 3, (together "**VAA's previous submissions**").
- 1.9 Building on VAA's previous submissions, VAA has further set out below its views in response to the OBR Proposals on (i) the proposed outcomes, (ii) the proposed measures, including the need to move to daily averages, (iii) the proposed targets, and (iv) the proposed rebates and bonuses. VAA also refers to the response submitted on behalf of the LACC and Heathrow AOC (the "**Airline Community response**") to the OBR Proposals which it fully endorses. VAA does not address Governance Arrangements and Continuous Improvements in



this response and refers to the views set out in the Airline Community response on these matters, which VAA fully endorses.

- 1.10 VAA urges the CAA to consider carefully the detailed content of VAA's previous submissions and the Airline Community response, in conjunction with this response. In the event that there are any inconsistencies between the responses due to any matters which have progressed since VAA's previous submissions, VAA favours the position as set out in this response.
- 1.11 VAA also invites the CAA to discuss any such matters further with it, in order that VAA might assist the CAA to understand properly its position. To the extent that the CAA disagrees with any aspect of this response or VAA's previous submissions, VAA invites the CAA to respond with detailed explanations as to why, in order to enable VAA to understand the CAA's views and consider its position further. It is, unfortunately, not possible to fully understand the CAA's rationale for the positions that it has adopted based on the information which has so far been published.

2. PROPOSED OUTCOMES

- 2.1 The CAA's Initial Proposals outline that it proposes to accept nearly all of HAL's proposed outcomes. VAA does not agree with this approach and does not view these outcomes as fit for purpose. VAA refers to VAA's previous submissions on this matter, which gave detailed reasoning as to why the outcomes proposed by HAL (and now adopted by the CAA in its OBR Proposals) are not in the best interests of consumers and should be refined and/or amended. Overall, as stated by the Airline Community response, this is because the current proposed outcomes are not specific enough to provide a clear definition of the best outcomes for the consumer and the CAA has provided insufficient evidence to support its proposed outcomes.
- 2.2 From the material which the CAA has published, VAA is concerned that the CAA has not paid detailed regard to VAA's previous submissions which include carefully considered proposals for alternative outcomes. Those proposals are based on work done to best reflect what consumers need and value from their airport experience using recognised and comprehensive customer journey mapping analysis, tools and techniques.
- 2.3 As stated to the CAA in July 2021, *"Through our engagement on the H7 OBR scheme, the Airline Community have voiced concerns about the level of precision and tangibility of Heathrow's proposed outcomes and have provided an updated view of consumer outcomes for H7"*¹. The CAA makes reference to these detailed submissions, however, it states that, *"While airlines have proposed an alternative set of outcomes to refine and clarify HAL's proposals, there is significant overlap between the two sets of proposals and we consider that the outcomes HAL has proposed are broad enough to cover the airlines' proposals"*². This dismissal of VAA's previous submissions gives the implication that the CAA has not adequately engaged with the alternative proposals provided; it is due to the very fact that HAL's proposed outcomes were so broad that VAA as part of the airline community felt they were not fit for purpose. VAA's alternative proposals were carefully considered and are deliberately specific; the difficulty with the broad outcomes proposed by HAL is that they do not suit outcomes that can be suitably measured. For example, VAA's previous

¹ Appendix 2, page 3.

² CAA's Initial Proposals, Chapter 14, paragraph 14.38. See also paragraph 14.15.



submission at Appendix 2, sets out 12 pages of detailed submissions that are based on comprehensive customer journey analysis in order to try and put forward the best possible outcomes with the consumer in mind.

- 2.4 The CAA's proposals note the CAA's view that, *"More importantly...it is the measures, rather than the higher level outcomes, that are included in HAL's licence...For this reason, we consider it better to take account of particular views and evidence when deciding which measures to adopt, rather than attempting to refine HAL's broader outcomes"*³. VAA is concerned that this statement attempts to justify the CAA disregarding VAA's submissions on proposed outcomes, simply because the outcomes are not included in HAL's licence and the CAA takes the position that the measures are "more" important. While VAA agrees that the measures are essential to get right in relation to OBR, that should not preclude the CAA from determining the correct outcomes at the outset. By the very definition of OBR, the outcomes should define the work (i.e. the measures and targets), otherwise what is left is simply the SQRB system, which as VAA understand, is what the CAA wants to move away from to further the interests of consumers.
- 2.5 VAA disagrees with the CAA's position. In particular, VAA considers that it is outcomes which form the foundation of the proposed shift to outcome-based regulation. On that basis, VAA is disappointed that the CAA appears to have failed to engage with VAA's submissions on alternative proposed outcomes. Indeed, as the CAA acknowledges, *"One implication of this approach is that some outcomes may have only a small number of measures associated with them"*. This approach is to essentially accept that some of the outcomes accepted may not have a meaningful impact on how HAL's service to consumers is measured. This defeats the purpose of trying to move towards an outcome-based framework and the rationale for doing so.
- 2.6 VAA does not consider that it is an answer to this issue to state that *"we do not consider this approach is problematic and there will be scope to further develop the outcomes framework over time"*. Such a response does not offer any explanation as to why the proposed outcomes should not be clarified and refined now, particularly given the detailed explanations and alternatives that VAA and the other airlines have offered in relation to this. If the CAA is to maintain its statement that it has *"emphasised the importance of a broader outcome-based approach in H7 [which]...will ensure that consumers' interests remain at the heart of airport regulation"*⁴, then it must properly engage with determining the very outcomes upon which this entire framework and shift in approach is based. In this context, its current proposals and approach to outcomes is untenable when considering its stated intent to shift to OBR. Unfortunately, and contrary to the CAA's stated intention to move to an OBR approach for the sake of consumers, in reality its proposals reflect an approach which gives very little weight to having effective outcomes, which is nothing more than a slightly modified SQRB which is labelled as OBR.
- 2.7 It is important that the outcomes in OBR are derived from the best possible understanding of what consumers want when using Heathrow airport in the context of regulation of HAL's performance, prioritising factors such as punctuality and reliability. The CAA's responsibility as regulator is to regulate HAL's performance, however, the current proposed outcomes fail to do this by setting vague and imprecise outcomes, some of which are even outside of the

³ CAA's Initial Proposals, Chapter 14, paragraph 14.39.

⁴ CAA's Initial Proposals, Chapter 14, paragraph 14.3.



scope of HAL's control. VAA's previous submissions outline how these outcomes can be refined by reference to consumers' expectations of performance from HAL. By failing to engage with the consumer-based proposals that VAA has offered, the CAA has not adequately considered the best interests of the consumer.

2.8 Rather than repeat its detailed comments on outcomes and a proposed alternative set of outcomes, VAA refers the CAA to:

2.8.1 The Airline Community response, which VAA endorses fully. This sets out in detail the areas of the proposed outcomes which could be made more specific and the detailed reasoning as to why that would achieve a better position for consumers.

2.8.2 VAA's previous submissions at Appendices 1-3 which set out VAA's views on the outcomes that should be used in the new OBR framework.

2.9 VAA would be pleased to engage further with the CAA in relation to these proposals and invites the CAA into further discussion on how the outcomes could be refined and clarified based on the content of the submissions that have been made, in order to lay the foundation for a proper OBR framework, taken seriously.

3. **PROPOSED MEASURES**

VAA's detailed comments on the proposed measures

3.1 VAA also disagrees with the CAA's approach to proposed measures. While the CAA emphasises the importance of measures for OBR in its Initial Proposals, VAA is concerned that it has not engaged with the substance of VAA's previous submissions and has not demonstrated how the proposals it has put forward are in the interests of consumers. The CAA states that it has provided "*the broad rationale for the inclusion or exclusion of specific measures*"⁵. VAA does not consider this to be appropriate and is concerned that simply providing the "broad" rationale for rejecting most of VAA's previous submissions demonstrates a lack of engagement with the detail of those issues.

3.2 In this regard, VAA fully endorses the detailed views set out in the Airline Community response on the proposed measures, which should be read in conjunction with VAA's previous submissions.

3.3 In particular, this outlines why the CAA should re-consider its stance on not introducing a common hero measure such as Net Promoter Score as the overarching measure and the airlines' views on how security performance could be best measured. The Airline Community response, which VAA fully endorses, sets out detailed commentary on the measures proposed by the CAA.

Daily measurement

3.4 As has been outlined in VAA's previous discussions with the CAA and VAA's previous submissions, VAA is of the view that there must be a shift in H7 to daily and not just monthly averages. This is crucial in order to uphold the proper expectations of HAL's level of performance for each individual consumer using Heathrow airport. The CAA states that it "*acknowledge[s]*" these arguments and gives reasons as to why the change should not be introduced now. VAA does

⁵ CAA's Initial Proposals, Chapter 14, paragraph 14.42.



not accept these arguments as adequate as they do not appear to be founded on a rational view of the current factual position⁶. In particular:

- 3.4.1 The CAA states that one reason for not introducing this change would be that targets would need to be reset. VAA does not accept that this is a valid reason for not introducing change in favour of consumers. Indeed, it is the CAA's very remit to set the targets that would need to be changed and to allocate the appropriate expertise and resources to set these targets. Further, the CAA has commissioned the Arcadis Report to comment on one aspect of targets already. The fact that daily reporting would have a knock-on effect to targets is not a good reason to avoid introducing daily reporting. Instead, the fact that measuring daily averages *would* have a consequential effect on the targets should be a reason in itself that shows that daily averages would give a clearer position on the levels of performance that HAL should be measured against.
- 3.4.2 The CAA suggests that "*If the data is very volatile, for example, then a target for the daily average might have to be set at quite a low level*"⁷. This suggests that the CAA has not reviewed the actual data that exists for any of the measures that VAA should move to daily measurement; the CAA should point to specific data sets that outline any volatility. Rather than proposing not to introduce daily measure reporting without substantiation, the CAA should review the facts and make a determination based on actual data.
- 3.4.3 The CAA refers to the reason that "*there could be risks associated with trying to introduce too many changes at the current time*".⁸ VAA does not agree that this is a good reason for not engaging with the issue. Indeed, the CAA has not even taken the step of identifying the nature of the risks which it says "*could*" be associated with this change. Airlines are therefore evidently not in a position to respond fully to this rationale and VAA invites the CAA to explain what it has in mind, in order that VAA can comment. From VAA's understanding, the CAA is barely proposing to any "*changes at the current time*". Indeed, the CAA should consider the consequences and risks of not implementing daily measures which would have a greater effect on the services offered to the consumer.
- 3.5 VAA acknowledges the CAA sees this as an "*important issue that merits further consideration*"⁹. In order to assist the CAA, VAA as part of the airline community, has commissioned independent experts, ICF, to explore this issue further. ICF's report is appended to the Airline Community response. This report shows that even on the limited data available to airlines which ICF were given, and the short timeframe available, ICF were able to run analysis which led them to conclude that "*Heathrow's passengers would experience a benefit from a move to daily reporting*"
- 3.6 VAA emphasises that ICF's promising analysis was produced in a very short window of time on limited data. This demonstrates the need for this area to be further explored and considered by the CAA, which should be based on a fuller

⁶ CAA's Initial Proposals, Chapter 14, paragraph 14.28.

⁷ CAA's Initial Proposals, Chapter 14, paragraph 14.28.

⁸ CAA's Initial Proposals, Chapter 14, paragraph 14.28.

⁹ CAA's Initial Proposals, Chapter 14, paragraph 14.29.



set of data that is available to HAL and could be done comprehensively in a slightly longer timeframe available to the CAA, though one which need not present any delay to the current timeframe envisaged by the CAA.

- 3.7 While the CAA states that "*it is important for HAL to ensure that suitable data is recorded and retained*"¹⁰, it is ultimately the CAA's role as regulator to ensure that it has the proper data at hand and that it properly examines important and relevant options such as daily reporting. Therefore, VAA urges the CAA to lead the analysis and discussions and to take forward further work in this area using third party experts where appropriate.

Overall view on measures

- 3.8 The measures (as the CAA itself recognises) are crucial to setting the performance level that consumers expect and should be offered when using Heathrow airport, and are designed to keep HAL accountable for the services it provides.
- 3.9 VAA welcomes the opportunity to engage in this matter and urges the CAA to consider this carefully as part of the process of making an independent assessment. VAA therefore invites the CAA to engage in detail with VAA's previous submissions on this matter and the points made in relation to specific measures in the Airline Community response.
- 3.10 Overall, VAA strongly urges the CAA to re-consider its position on the proposed measures and to take further time to gather the necessary evidence and information which properly considers the measures that will best further the interests of consumers.

4. PROPOSED TARGETS

- 4.1 As explained above, VAA does not consider that the outcomes or measures proposed by the CAA are appropriate. In these circumstances, and as noted above, VAA expects the CAA to carry out a further review of the proposed outcomes and measures. In addition, VAA proposes that, as part of its review, the CAA should consider amending the proposed targets but reserves the right to comment further on this following the CAA's review of the proposed measures and outcomes in due course.
- 4.2 Overall, VAA makes the following observations which it hopes will assist the CAA when considering these matters in further detail:
- 4.3 First, VAA notes that the CAA has expressly decided not to adopt the conclusions made by Arcadis. The CAA has instead proposed to take "*a deliberately cautious approach bearing in mind the challenges that HAL faces*" (amongst other matters), which it describes as "*therefore [adopting] HAL's optimal plan targets in most cases*"¹¹. VAA does not consider this to be an appropriate, or indeed rational, course of action. It is also evident that this decision will have a clear detriment to consumers and the CAA has provided scant reasoning as to why being "*cautious*" should lead to it adopting HAL's proposals rather than those of the independent consultants which it has engaged. It is further unclear why the CAA considers additional caution to be required in circumstances where Arcadis appears to have been largely aware of the issues said to give rise to the CAA's caution (insofar as that can be

¹⁰ CAA's Initial Proposals, Chapter 14, paragraph 14.29.

¹¹ OBR Working Paper, paragraphs 2.11-2.12.



determined). For example, Arcadis notes that HAL has been outperforming its targets since the onset of Covid (see page 7) and the need to install new security equipment (see page 21).

4.4 VAA is however limited in the observations which it is able to make in this regard because the CAA has not adequately explained its rationale for departing from the conclusions made by Arcadis. For instance, it is unclear what "challenges" the CAA has in mind or why those challenges, even if accurately identified, would justify a lower level of service quality than that proposed by Arcadis. Insofar as the CAA elects to maintain the position which it currently proposes to take, VAA expects the CAA to explain more clearly, and on an item-by-item basis, why it has chosen the targets which it has and why it has not adopted the conclusions proposed by Arcadis.

4.5 Secondly, even without an adequate understanding of the CAA's reasons for proposing particular targets, it is clear from the face of the proposals that there are a number of significant difficulties with them, as explained in the Airline Community response. That response sets out VAA's detailed comments on the proposed targets as associated with each proposed measure, explains VAA's concerns, and proposes alternative targets accordingly. As a general proposition, these comments set out why the CAA should consider setting higher targets for HAL given that many of the current proposed targets are in fact lower than the level of performance which HAL has consistently been able to reach, to date.

5. **PROPOSED REBATES AND BONUSES**

5.1 As with the proposed targets, VAA reserves its right to comment on the CAA's approach to rebates once the CAA has conducted the review of outcomes and measures which VAA considers is necessary, but endorses the comments in the Airline Community response.

5.2 In relation to bonuses, VAA reiterates the comments made in VAA's previous submissions and the Airline Community response. VAA disagrees fundamentally with the suggestion that bonuses should be payable to HAL for delivering its services. VAA considers that delivery should be the expectation, with rebates payable if service levels are not met, but does not agree that bonuses should be payable for delivery.

5.3 However, without prejudice to that position, VAA endorses the comments made in the Airline Community response in relation to the H7 Bonus structure in the Airline Community response.

5.4 VAA reserves its right to comment on the CAA's approach to bonuses once the CAA has conducted the review of outcomes and measures which VAA considers is necessary.

6. **CONCLUSION**

6.1 Overall, VAA urges the CAA to re-consider the OBR Proposals. The current OBR Proposals suggest that the CAA has not taken proper account of or engaged with VAA's previous submissions, with the result that these proposals fail adequately to protect consumers or further their interests in an area which is intrinsically linked with the consumer experience.

6.2 VAA considers that the CAA ought to analyse in more depth what the appropriate outcomes should be. These should be based on what is important



to consumers and should not be characterised as being unimportant, when the whole purpose of moving to OBR is to favour an outcome-based approach.

- 6.3 In addition, the CAA ought to reconsider its approach to the proposed measures and targets including commissioning further analysis in the areas of daily measurement, baggage and taking the advice of its independent advisors, Arcadis, to set targets which properly set a level of performance which consumers expect from HAL.
- 6.4 The CAA's current approach gives rise to concern that the CAA has not done all that it should as an independent regulator to consider all the information and evidence at hand or which would be reasonably available. VAA urges the CAA to dedicate adequate resources, including third party expertise, to properly and thoroughly consider these questions in detail based on the data available.
- 6.5 In the circumstances VAA reserves its right to comment further on the detail of the proposals which the CAA ultimately makes. VAA is of course willing to have further discussions with the CAA in this regard if the CAA is willing to properly engage with the substance of VAA's proposals. VAA notes that the CAA may consider delaying the introduction of some (or all) new measures, for example until the beginning of 2023¹². While VAA would be disappointed with any delay given that this process has been ongoing since 2016, VAA agrees that the CAA should take the time required to fully consider and act on the issues raised in this response.

Yours sincerely,

A handwritten signature in blue ink, appearing to read "C. Koster", written over a light blue horizontal line.

Corneel Koster
Chief Customer and Operating Officer,
Virgin Atlantic Airways Limited

¹² CAA's Initial Proposals, Chapter 14, paragraph 14.61.