NERL response to CAP3174

CAA Update and consultation on the timetable and approach to Constructive Engagement for the next NERL price control review (NR28)

October 2025

1. Introduction

This note provides further input to the CAA from NERL on aspects of the methodology for conducting the NR28 review, and the question of the proposed length of the NR28 price control period. It responds to the CAA's Update and consultation on the timetable and approach to Constructive Engagement for the next NERL price control review (NR28) (CAP3174). [redacted]

2. Context

The CAA proposes in CAP3174 to schedule the NR28 price control review to the following outline timetable:

Dec 2025	CAA draft Method Statement
Jan-Feb 2026	NERL constructive engagement (round 1) with airline customers
May-Jul 2026	NERL constructive engagement (round 2) with airline customers
Nov 2026	NERL submits NR28 business plan to CAA
Jul 2027	CAA initial proposals
Jan 2028	NR28 price control period starts (1 January), based on parameters set out in CAA Initial Proposals
Mar 2028	CAA final proposals
Aug 2028	CAA final decision and licence modifications implemented, backdated to 1 January 2028

We recognise that this timetable, whilst delaying final decisions until some months into the price control period, and thus outside normal practice in UK utility regulation, is an adjustment in the CAA's current circumstances, as it prioritises a number of nationally important projects, in addition to the core regulatory tasks of NERL and Heathrow price control reviews.

To ensure timely and effective delivery of our Business Plan to the CAA by November 2026, it is essential that the first round of constructive engagement with airline customers commences in January 2026.

Between the initial engagement and the submission of the final plan, a series of critical activities must be completed within a highly constrained schedule. These activities include:

- Document development and production – preparation of materials to support engagement and regulatory requirements.
- Governance compliance – adherence to internal and external governance processes.
- Airline issuance and pre-reading – provision of sufficient time for airlines to review materials ahead of any engagement sessions.
- Incorporation of feedback – adequate time to analyse and reflect on feedback from both engagement rounds and integrate necessary adjustments into the Business Plan.

Any deviation from commencing constructive engagement in January 2026 will significantly impact the overall timeline through delay, or alternatively the quality of the final submission due to a compressed timescale. It could also impact our ability to ensure that airline feedback is fully considered and appropriately reflected.

In this response we make some suggestions for streamlining and focusing the work typically undertaken by the CAA as part of a NERL price control review, so that the CAA could fulfil its statutory duties and make efficient use of stakeholder engagement.

3. Review methodology

The NR28 review presents an opportunity for the CAA to design appropriate regulatory frameworks for new services delivered by NERL in support of new airspace users, as well as new functions to be taken on by NERL to support the wider aviation industry, such as the UK Airspace Design Service (UKADS). Against the backdrop of nationally important technology programmes and airspace changes and continuing wider challenges across the European network in providing capacity for growing traffic, the CAA also has the opportunity to consider how best to monitor and incentivise NERL's investment activities.

There is, however, a very real risk that – even on the proposed extended timetable – unless the traditional 'business as usual' aspects of NERL's regulated activities are assessed in a more streamlined, prioritised manner, the CAA may crowd out from the NR28 review the development of regulatory policy to meet the needs of these significant changes. Already in the very earliest stages of the NR28 review, stakeholders have experienced recurrence of the delays to milestones, as seen in the NR23 review. We consider that now would be an opportune moment for the CAA to reconsider the balance of effort and focus it gives to the traditional scrutiny of price control building blocks, to free up its own, and stakeholders', capacities to work on new NERL activities and on some key issues affecting NERL's current business, such as rethinking investment regulation.

We set out below some initial thoughts on how such prioritisation might be developed:

- **Focus the price control decision**: the current price cap is based on an allowance for capital expenditure over the period, with the explicit recognition by the CAA that this can vary within period, for valid reasons, and that the eventual (efficient) costs are 'trued up' through price adjustments. Taking advantage of the inherent flexibility provided by maintaining this mechanism could allow for a much simpler oversight of the overall investment portfolio size and shape at the NR28 review itself, effectively restricting decisions to those that are needed for the price control arithmetic itself, with detailed scrutiny of individual programmes deferred to the subsequent ongoing customer engagement and independent oversight within the NR28 period itself.

- **Recognise the impact of external labour markets**: previous reviews have undertaken focused scrutiny of both the levels of pay and the proposed real terms growth rates over the coming period. The CAA has consistently concluded that wage levels are not materially out of line with comparator job families, and had set determined costs based on modest increases in real wages which are close to NERL's business plan proposals. The CAA could reduce the effort devoted to wage levels and growth by conducting simple cross-checks of recent growth in NERL wages versus the wider economy and allowances in previous regulatory plans, to validate levels, and then setting real wage growth assumptions taking account of official and other forecasts. The focus would therefore be on the anticipated change in wage levels.

- **Validate airlines' preference for resilient operations**: our NR28 planning is based on our current understanding of customers' preference for a safe resilient operation, with sufficient validated staff to meet projected service demand, and to deploy air traffic control officers to training of new colleagues and to technology development and deployment. Our resource modelling enables us to scale ATCO resource to total projected demand over NR28. Our controller workforce is already very highly productive when measured against their European peers. Against this backdrop, we consider that the CAA should recognise the essential stability of the ATC operation, and that customers would benefit directly from better capacity and more resilient service if, during the NR28 period, operational resourcing supply turned out marginally in excess of demand.

- **Simplify assessment of non-operational costs**: NERL's corporate functions, outside the control centres, are subject to similar productivity drivers as other UK regulated sector firms. As such, simple benchmarking of projected costs against official forecasts incorporating economy-wide productivity assumptions could be a straightforward way to generate a reasonable cost building block.

- **Align regulatory finance parameters with UK consensus**: the CAA's initial proposals in the NR28 review will be issued in summer 2027, after the conclusions of the current CMA appeals in water, the Ofgem RIIO-3 decision (and any appeals arising), and the CAA's final H8 decision in spring 2027. It should therefore be possible to import a wide range of consensus items (both method and parameters) from these reviews, leaving the key empirical question for NR28 cost of capital being the NERL-specific company risk as measured using best available data and comparator group. Issues such as inflation index to replace RPI and the move to nominal cost of debt will have been well settled through the prior reviews.

This streamlining of some of the 'business as usual' aspects of the NR28 review would allow CAA, NERL and its customers to focus on: (a) the critical areas of the price control which require judgement, including revising aspects of the current incentive framework and assessing resources to support a resilient service, and (b) developing new and appropriately designed regulatory approaches for emerging services, such as UKADS.

On the former, we consider that full regulatory consideration will continue to be needed in several areas including:

- **Traffic forecasting**: in our view, this remains an unavoidably important area which would benefit from ongoing engagement with customers and the CAA throughout the review, so that the price control is set using the best available data and analysis thereof.

- **Risk and reward**: the allowed return on equity will continue to need to be carefully calibrated, considering the overall financial risks to the business, the strength of the incentive regimes and the various mitigations for cost variance.

On the latter, we consider that the NR28 review will need to allow space for consideration of new issues:

- **Regulatory innovation**: there are several areas of potential innovation which would benefit from engagement during the review, including a new flight efficiency metric, developing the regulatory regime for the enduring UK Airspace Design Service, and evolving the current incentives for investment engagement and efficiency so that they are better targeted and support value-adding engagement.

- **New airspace users**: we anticipate that part of the NR28 review could be productively devoted to joint working between NERL and the CAA to explore the most appropriate regulatory model for NERL's proposed new user services.

These thoughts are not comprehensive, but are offered as suggestions to stimulate further thinking.

4. Price control length

We understand that the CAA is currently considering potentially extending the NR28 price control period from 5 to 6 years, in the hope of deconflicting the start of the subsequent control period for NERL (which would be NR34 in January 2034, with a 6 year price control), and the comparable period for Heathrow (H9, currently scheduled to start January 2032). We understand that the purpose of such an extension would be two-fold:

- Reduce the peak loading on CAA's economic regulation resources, including analytical, programme management and board-level decision-making
- Reduce the peak loading on those airlines and their representatives (notably IATA and British Airways) which are actively engaged customers of both Heathrow and NERL and choosing to engage fully with both price control review processes.

As previously discussed with the CAA, we have a strong preference for a 5-year control period. The current model provides some stability for the business to focus on delivering the outcomes expressed in NERL's regulatory plan for the period and endorsed by the CAA's final decisions on price control parameters. It also provides several clear years between the end of one regulatory cycle and the start of the next in which NERL can plan and execute material changes with the aim of securing cost efficiencies and/or productivity gains. The benefits of these established arrangements flow directly to customers in the form of cost-efficient services, reflected in charges and service targets when the price control is subsequently reset after its full term.

NERL is sympathetic to the CAA's aim to deconflict the workload involved in running multiple price control review processes in parallel. However, an extended length of the price control period would make it materially more difficult for NERL to predict (and stakeholders and the CAA properly to consider) operating costs, technology delivery and traffic volumes (up to nine years in advance) as part of its business plan for the upcoming period, thus introducing significant additional risk and uncertainty. This is particularly true at a time, as noted above, of significant change.

The CAA will no doubt be mindful of its duties under the Transport Act 2000 to promote economy and efficiency on the part of NERL and to secure that NERL does not find it unduly difficult to finance its licensed activities, as well as the current government's 'regulating for growth' agenda[1], with its emphasis on tackling regulatory complexity, reducing the burden of regulation and promoting proportionate regulation, removing uncertainty and increasing regulatory predictability for businesses. For the reasons set out in this response, in our view, the CAA's proposed 6-year control period would risk cutting across both its own statutory duties and the government's wider regulatory agenda.

We also note that, given prior precedents of Heathrow price controls being extended, there is no guarantee that a 1-year extension would deconflict NERL's price control from Heathrow's. To the contrary, there is a significant possibility that, despite introducing additional

[1] New approach to ensure regulators and regulation support growth (HTML) - GOV.UK

complexity and uncertainty, the extended price control period would ultimately drive greater conflict if H8 were to be extended, particularly in light of the significant demands of the Heathrow expansion project.

If the CAA were to go ahead with a 6-year control period, this additional uncertainty would need to be addressed appropriately in NERL's cost of capital and/or in risk-sharing mechanisms to protect NERL's ability properly to finance its licensed operations in the face of such uncertainty.

We understand that the CAA is considering including within its proposed 6-year price control period a mid-period review (MPR) after three years. We recognise that a MPR would be intended by the CAA to mitigate the additional uncertainty inherent in a longer control period, by allowing progress to be assessed part-way through the period, and we welcome this recognition of the issue. However, we believe that an MPR would introduce further adverse impacts on NERL's ability to operate effectively during the extended price control period.

- **NERL engaging with a MPR will result in less capacity to focus on improving the service NERL provides**: Achieving cost efficiencies and productivity gains during the price control period would inevitably be much harder if NERL and its customers were focused after only 1-2 years of the NR28 period on a mid-period review. This would tend to put NERL on the defensive with respect to improvement initiatives in train but whose benefits are not yet confirmed. Such an approach is also liable to introduce duplication, as time is spent reopening and debating issues at the MPR stage that were settled at the outset of the price control period. This more frequent change in NERL's regulatory settlement could also have an impact on its financeability, as investors could find it more difficult to understand and assess the regulatory environment in which NERL operates.

- **The scope of any MPR is likely to widen under pressure from other stakeholders, increasing its tendency to distract from, rather than improve, performance**: There is a real risk, notwithstanding any prior guidance from the CAA to define the scope of the MPR narrowly, that pressure will grow from NERL customers to widen the scope. The net effect of this would be that, even if the CAA intended in advance to conduct a 'narrow' MPR, for example focused only on traffic forecasts, in practice the MPR would likely be widened, further reducing focus for NERL's management on running the business and implementing the NR28 plan for the benefit of customers.

We also encourage the CAA to consider carefully the experience in this area from the energy sector, which illustrates many of the concerns expressed above. In 2018, Ofgem decided that its RIIO-2 price control for GB gas and electricity networks should be for five years, shorter than the previous 8-year period for RIIO-1 controls, and re-aligning this energy sector with the control period applying to most other UK economically regulated utilities. Ofgem's rationale[2] is reproduced below. The same dynamics identified by Ofgem (namely, an overly long control period exacerbating the uncertainty inherent in ex ante regulation, with things turning out differently from core assumptions given the passage of time, and the risk of an expanding scope of MPR frustrating the ability of regulated companies to plan for and deliver innovations and investments, ultimately to customer benefit) will inevitably be replicated in a 6-year NR28 period with MPR.

[2] Ofgem, RIIO-2 Framework Decision, July 2018

We strongly believe that a standard 5-year control period for NR28 is likely to be in users' best interests. The CAA's concerns of peak workloads for CAA and for those airlines engaged in both Heathrow and NERL price controls could be dealt with better at source, through carefully designed plans which interleave activities for the respective price controls, thereby enabling airlines to participate in both effectively. We are pleased that the CAA has stated its intention to appoint a delivery partner professional services firm, to complement its own permanent staff and to provide peak resources to deliver price control outputs to time and quality.

Finally, we reiterate the observations in section 2 of our March 2024 response to CAA consultation, **CAP2618 Setting future price controls – review of approach**, regarding the process and governance around price controls. Focusing on materiality of issues under active consideration will help manage the volume of work for each price control review. Creating mechanisms for ongoing oversight and incentives for performance through the period, as is the case with capital investment, can also reduce the need to reach definitive judgements on certain topics within the price control settlement itself, thereby reducing peak workload.

Annex

Ofgem RIIO-2 Framework

This annex reproduces the relevant extracts from Ofgem's RIIO-2 Framework document in which it sets out its decision and reasoning on the length of the RIIO-2 price control period.

Decision

3.6 Our decision is to set the default length of price control at five years.

3.7 We will consider proposals we receive from companies in their business plans to set allowances for certain activities for a longer-term. For these to be justified, we will need to see evidence of significant net benefits to consumers relative to a five-year period.

Reasons for decision

3.8 In RIIO-1, we have already observed that things have turned out differently from the assumptions made at the time of setting the price control. Some cost allowances were set too high in hindsight, and some performance targets were set too low. This forecast risk is inherent in ex ante regulation. However, extending the price control to eight years with only a limited scope for an MPR, limits our ability to reset certain cost allowances and output targets.

3.9 The uncertainty surrounding network activity in the future, even within the next 5-10 years, means it is extremely difficult to predict the allowances necessary for a range of different activities. Forecasts could be wrong to a significant degree and this could harm consumers, or investors. Our experience with RIIO-1 suggests that it may not be possible to anticipate all of the areas where this will arise. As a result, we may not be able to put in place a complete set of uncertainty mechanisms.

3.10 We think that this risk is too high to justify retaining the current arrangements.

3.11 A significant majority of stakeholders that commented on this topic have confirmed our view that shortening the period over which we set allowances/targets is a sensible way to manage this risk over RIIO-2.

3.12 We believe that setting allowances over a five-year period, still provides incentives on companies to plan and develop their networks to meet future demands, and to find innovative ways to reduce cost and improve performance. We do not believe that five-year price controls will necessarily affect schemes (such as undergrounding) that may take longer to progress through the planning process. There are many examples of projects that have been initiated in one price control and completed in another. It is also possible – within the framework of a five-year control – for us to set allowances for certain projects over a longer period.

3.13 We believe that the option to retain an eight-year price control period with an extended MPR is not likely to drive more long-term thinking and greater innovation than a five-year control. Stakeholders agreed with our concern that a wide-ranging MPR will instead create two mini price control periods. A number of network companies identified risks with moving to a control period shorter than five years, particularly around certainty of investment and ability to innovate effectively.