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Re: CAP3238 – Draft decision on the regulatory treatment of early costs of capacity expansion at Heathrow Airport

Virgin Atlantic ("VAA") welcomes the opportunity to respond to the CAA's draft decision ("the draft decision") on the regulatory treatment of early costs associated with Heathrow expansion (CAP3238). This submission should be read in conjunction with our response to the CAA's November consultation (CAP3201).

Overview

We are pleased the CAA has substantially acknowledged concerns raised by stakeholders during the CAP3201 consultation process, including those regarding affordability and cost escalation, governance and ex ante review mechanisms, and uncertainty over the benefits case for expansion. We are, therefore, extremely disappointed that the CAA has chosen to both disregard the primary position – that Heathrow Airport Limited ("HAL") (or other Promoters of expansion) should not be permitted to recover pre-DCO costs from airlines and consumers – and electing to implement only limited aspects of stakeholder recommendations to address our concerns with its regulatory approach.

For the avoidance of doubt, VAA continues to believe that no early recovery of costs should be permitted by HAL for reasons set out in our earlier response. The CAA has largely accepted that some of the key assumptions underpinning the justification for early cost recovery remain unresolved – indeed in some key areas, the CAA's own assessment of stakeholder responses in CAP3238 would justify materially stronger intervention than is currently proposed. For example, the draft decision acknowledges conflicting evidence regarding scarcity rents and recognises that there are plausible scenarios in which consumers may not realise the scale of benefits asserted by HAL in its Frontier Economics analysis. Regardless, the CAA should not be relying on a HAL commissioned report, which contains several methodological flaws identified by the *Heathrow Reimagined* campaign, when making its decisions, and should instead commission its own independent analysis.[1]

The CAA has also accepted that Heathrow expansion is likely to result in airport charges increasing materially in real terms, recognising the potential for airline behavioural responses that will have an impact on competition at the airport – which is particularly likely when considering the impact of materially higher Heathrow charges on smaller scale carriers such as Virgin Atlantic, which remain highly exposed to airport charging. The impact of sustained increases in airport charges is the likely weakening of effective airline competition at Heathrow, reducing consumer choice and reinforcing the market power of the airport and incumbent carriers alike. Despite these conclusions, the CAA's draft decision continues to permit HAL – a monopoly airport operator with significant market power – to recover potentially irreversible pre-consent costs before development consent is secured, before a full business case has been independently validated, and before there is sufficient certainty over the total scale of expenditure that could ultimately be incurred.

Moreover, this issue has become even more significant following publication of CAP3251, in which the CAA explicitly identifies potential regulatory models, including those that may facilitate the introduction of competition between promoters and/or alternative delivery structures for Heathrow expansion. In that context, permitting HAL to undertake extensive land acquisition, enabling works or strategic asset control ahead of the conclusion of the Government's upcoming ANPS review and wider regulatory reform process risks materially prejudicing future competitive outcomes before the CAA or Government has determined the appropriate frameworks for expansion delivery. There is also a high degree of political uncertainty, which may have a bearing on the strength of support of Heathrow expansion and the timetable currently being pursued to deliver it.

We believe that the CAA's draft decision is therefore inconsistent with the CAA's statutory duties to further the interests of consumers, promote efficiency, and ensure that users are protected from the costs of inefficient or uncertain expenditure.

Evidence suggests greater cost uncertainty

Since the publication of the previous consultation in December 2025, additional evidence has emerged which materially increases concern regarding both the reliability of Heathrow's expansion cost estimates and the adequacy of the proposed regulatory framework for early cost recovery.

[1] Heathrow Reimagined: *Review of Frontier Economics' 2025 cost benefit analysis for HAL of Heathrow expansion*, April 2026

Independent report confirms HAL's estimates are optimistic
Most notably, the CAA has now published alongside CAP3238 an independent technical and cost-efficiency assessment by Steer into Heathrow expansion proposals[2]. The Steer report provides important independent evidence regarding the uncertainty, immaturity and potential cost exposure associated with expansion. While HAL publicly presents its scheme as affordable and deliverable, Steer concludes that the current cost estimates remain early-stage, optimistic and subject to material upside risk.

Steer benchmarks HAL's headline £33bn capex estimate (2024 CPI prices) at the very bottom of a plausible range extending to approximately £52bn – while also excluding major future surface access enhancements such as additional rail infrastructure. It should also be noted that this figure excludes the estimated £15bn investment planned for the Central Terminal Area (CTA) at Heathrow – this terminal capacity is essential to enable the full utilisation of a third runway and is core to the benefits case for expansion. The report also identifies reliance on dated assumptions, incomplete design development and significant uncertainty around terminals, tunnelling and enabling infrastructure. That these findings come from the CAA's own independent adviser clearly undermines any suggestion that HAL's current cost estimates are sufficiently mature or reliable to justify large-scale speculative pre-consent expenditure recovery, not least as HAL CEO Thomas Woldbye has also publicly suggested they expect a 'typical' cost overrun of around 20%.[3]

At the same time, HAL's own estimates of early-stage and pre-DCO costs continue to evolve materially upwards. While VAA welcomes the CAA's decision to reject HAL's proposal to increase the 2025/2026 allowance from £320m to £450m, Heathrow's broader estimates of pre-consent expenditure now appear substantially higher than earlier assumptions. This further reinforces the need for materially stronger controls than those currently proposed in CAP3238 – notwithstanding our primary objection to the principle of early cost recovery.

Continued lack of detail on cost breakdown
The Steer report also demonstrates that 'early costs' are not limited to relatively modest planning or advisory expenditure. Instead, it confirms that the programme envisages potentially very substantial pre-construction and enabling costs, including:

- land acquisition and compulsory purchase activity;
- demolition and temporary works;
- river diversions and utilities relocation;
- logistics compounds and enabling infrastructure;
- environmental mitigation; and
- Development Consent Order preparation activity.

Steer estimates for land acquisition and property compensation alone are in the range of approximately £4.0bn–£4.8bn. Airlines have not been provided with a clear or comprehensive view of the totality of expenditure that may ultimately fall within the definition of 'early costs' – indeed much of the underlying data used in the Steer report remains redacted. The lack of transparency is remains a serious concern. While the draft decision relates primarily to the proposed £320m cap for 2025–2026, this represents only a very small proportion of the potential early-stage cost exposure. The current allowance represents only the first stage of a substantially larger funding envelope and the CAA's draft decision risks establishing a regulatory precedent that may subsequently be relied upon to justify increasingly far larger categories of speculative pre-consent expenditure.

VAA believes a detailed and transparent breakdown of all anticipated pre-consent expenditure categories – and independent validation of consumer value – is urgently required before any further decisions on early cost recovery are taken. Expenditure should only be approved once the associated consumer benefits have been independently established and verified. The current approach reverses that logic by permitting substantial speculative expenditure to enter the RAB before the economic and consumer case for expansion has been conclusively demonstrated.

Permitting land take as 'early costs' would be prejudicial
Moreover, the issue is not merely financial. Allowing substantial land acquisition and enabling works to proceed on this basis risks materially prejudicing future competition and alternative development proposals before the planning process has properly concluded. This concern is directly recognised within the CAA's own analysis. CAP3238 explicitly acknowledges the need to disallow costs that *'reduce potential competition where HAL has not taken appropriate steps to avoid these costs'*. Despite recognising these risks, the draft decision would still permit HAL to undertake potentially extensive land and property acquisition activity – in addition to costs already recovered from pre-2019 – with limited ex ante scrutiny and no clearly defined restrictions on HAL's process for acquisition.

[2] https://www.caa.co.uk/publication/download/27605
[3] Thomas Woldbye at Aviation Club, 12 February

This is particularly problematic given the uncertainty that arises from an ongoing review of the Airports National Policy Statement (ANPS) and the CAA's CAP3251 *consultation on a shortlist of regulatory models*, which includes options to enable alternative Promoters to bring forward competing schemes[4].The CAA should simply not allow HAL to acquire land or otherwise take control of assets known to be required for the expansion project, since it is clear this would fundamentally undermine potential competition and foreclose alternative options before they can properly emerge.

CAA should assume control of independent assessor
VAA is disappointed that the CAA appears to have substantially discounted stronger independent assurance arrangements primarily on grounds of timing and practicality. The draft decision suggests that there is not the time available to appoint a truly independent assessor for spend between 2025/26, while leaving scope to *'retain the option of directly appointing an independent assessor…to maximise independence, accountability and scrutiny in the regulatory process*' from 2027.

This creates an obvious inconsistency – it's difficult to understand why maximising '*independence, accountability and scrutiny in the regulatory process*' should not be a standard CAA choose to apply immediately. Given the magnitude and strategic importance of these decisions, the CAA should be clearer that it *will* take direct ownership of assurance arrangements as soon as practicable ahead of further consideration of development costs post-2027. It is essential that HAL, as the regulated entity, is not permitted to lead procurement, appointment and management of any advisory structure going forward.

This view is consistent with the community views on the future of the Independent Fund Surveyor, its function and appointment for H8, where we would want to see:

- independent assessors directly appointed by and accountable to the CAA;
- terms of reference set by the regulator in consultation with airlines;
- access for airlines to equivalent technical expertise, funded by HAL and appointed by the CAA[5];
- transparent sharing of any assurance outputs; and
- stronger powers to approve/halt expenditure.

Stronger regulatory protections are required for 2027 and beyond
VAA remains concerned that many of the safeguards referenced throughout CAP3238 continue to rely primarily on policy statements and future regulatory discretion rather than binding licence-based obligations and proactive CAA-led oversight. While the CAA has indicated that it intends to apply a 'high bar' to future cost increases and strengthen aspects of the assurance framework, these protections remain insufficiently codified within the proposed regulatory structure.

Given the potential scale and duration of expansion-related expenditure, VAA considers it essential that key protections – including clawback mechanisms, cap controls, reporting obligations, duplication tests, value for money and need assessments in addition to assurance requirements – are embedded directly within enforceable licence conditions. This would provide materially greater transparency, accountability and certainty for airport users, while also reducing the risk of future regulatory ambiguity or discretionary drift as expenditure escalates over time.

Such safeguards are necessary to provide meaningful protection for consumers particularly in light of the CAA's continued reliance on ex post review mechanisms despite the CAA's own historic recognition that retrospective regulation is insufficient to drive efficient behaviour.[6] Fundamentally, once these costs are incurred, regulatory leverage is significantly reduced as the burden would fall on the CAA to demonstrate that costs are duplicative rather than on HAL to demonstrate that they are not.

Furthermore, we would note the CAA's own recent findings regarding the quality of HAL's H8 business planning submissions. In CAP3232, the CAA noted that HAL's plan represented a 'low-quality plan', which *'reflects concerns on consumer benefit, ambition (including baseline efficiency evidence and service quality enhancement), coherence across sections, and third-party assurance (particularly the absence of independent assurance over capex efficiency and limited transparency of assurance findings for consumer research)'*[7]. Against that backdrop, it is difficult to understand how the CAA can reasonably conclude that HAL's complex early expansion expenditure programmes can be appropriately governed by ex post reviews and under HAL-led assurance arrangements.

[4] https://www.caa.co.uk/media/sbhmpxlt/cap3251-consultation-on-short-list-of-regulatory-models.pdf
[5] We note that in H8, airlines' access to SME's to consider the multi-billion pound T2 baggage scheme cut due to lack of funding arising from HAL overspend.
[6] Highlighted in VAA's original submission, where the CAA concluded during its H7 framework review that:
'an ex-post regime does not offer any incentive to find efficiencies in the delivery of a project to outperform budget expectations. Nor does it provide appropriate incentives for HAL to manage capital risks effectively.'
[7] https://www.caa.co.uk/media/upcoupbx/economic-regulation-of-heathrow-airport-h8-initial-proposals-summary.pdf

Considering the potential scale of future development/pre-DCO costs beyond 2026 the CAA must demonstrate how it intends to ensure future business plans will be materially better, including:

- the standard of scrutiny that will apply;
- the extent of independent validation (see below);
- whether airlines will have a role in prior approval of expenditure;
- what benchmarking will occur;
- what cost categories may be excluded;
- how potential duplication will be assessed; and
- what binding clawback mechanisms will apply.

Without robust ex ante approval mechanisms, the framework risks becoming reactive rather than preventative – intervening only after expenditure has already been committed and regulatory leverage materially weakened. VAA therefore continues to strongly believe that:

- all early costs should require formal, ex ante approval by CAA;
- independent benchmarking, value for money and needs assessments should occur before expenditure is incurred;
- HAL should bear the burden of proof regarding efficiency and necessity;
- detailed cost breakdowns and programme scope should be transparently disclosed; and
- stronger licence-based clawback and enforcement mechanisms should be embedded from the outset to insure against consent not being granted.

Conclusion
VAA recognises that the CAA has sought to respond to stakeholder concerns and that aspects of the draft decision represent movement in the right direction. However, the current framework still fails to provide the level of protection we argued for in our response to CAP3201, particularly given the speculative nature of pre-consent expenditure and scale of potential costs. In many respects, the CAA's own analysis reinforces the case for materially stronger intervention than is currently proposed to ensure no precedent is set which allows potentially billions of pounds to be added to the RAB long before consent for expansion is secured.

VAA therefore strongly urges the CAA to reconsider the current approach and implement materially stronger protections before permitting further early cost recovery.