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Civil Aviation Authority

Sent by email to: economicregulation@caa.co.uk

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Re: Response to Economic Regulation of Heathrow – H7 Draft License Modifications (CAP2275)

Thank you for the opportunity to respond to the CAA's consultation, setting out further details on the CAA's proposed license modifications to HAL's license for H7 ("License").

This submission is made jointly by the LACC and Heathrow AOC (the "Airline Community") and sets out agreed principles and outcomes that we believe the CAA's policy and drafting should aim to address. Individual airlines, groups and alliances may make their own submissions detailing their specific views on the CAA's proposals.

In making this submission the Airline Community also retain the right to submit subsequent comments and evidence subject to further developments and evidence. This submission also incorporates by reference previous bodies of evidence and comment submitted to the CAA on this issue, in particular the Airline Community's response to CAA CAP2265 (H7 Initial Proposals), CAP2265E (2022 Holding Cap) and CAP2274 (H7 OBR Working Paper).

In responding, we have set out comments and, where relevant, proposed drafting against specific topics that are set out within the consultation. Drafting references set out within this response relate to those within the consultation unless stated otherwise.

1. General Comments

Whilst noting the CAA are seeking to begin finalising aspects of the License prior to its publication of the Final Proposals, we note there are a number of areas where either general policy positions are still to be finalised, for example Traffic Risk Sharing, or where specific details pertinent to the License need further discussion between the Airline Community, HAL and the CAA, for example particular measurements under OBR or capital timing incentives. Clearly the License should be in response to these matters.

In addition to the above, throughout this response there are a number of areas the Airline Community have highlighted would benefit from further discussion both in terms of what we have proposed as well as seeking a greater understanding on the rationale and / or mechanics of some of what the CAA are proposing, particularly those of a technical nature.

As such we very much see this as initial feedback to the CAA. We also formally request time with the CAA in order to go through these in further detail with an opportunity to provide further feedback for consideration as part of the CAA's development towards Final Proposals. We would also recommend that, where engagement is continuing on the development of policy matters, that such engagement could include specific discussion on implications for the H7 License.

2. 2022 Price Cap

The Airline Community note the comments within both the consultation, as well as those more detailed in the CAA's CAP2035 publication, particularly with regards to the mechanism for the 'true up / down' of the 2022 holding cap. Whilst we acknowledge that further engagement is planned by the CAA on this issue, the Airline Community note that where there is a 'truing down' this should not rely on the k-factor but instead be returned as soon as possible, and most preferably within year, subject to CAA timings. The CAA acknowledge the "challenges the level of the holding cap will create in the short term for consumers..."¹ and it would not be appropriate for HAL to further benefit at the expense of consumers.

With regards to the calculations themselves, the Airline Community would strongly encourage the CAA to use 'actuals' where possible, as proposed under C1.1.

The Airline Community would also welcome particularly clarity on how the Terminal Drop Off Charge will be dealt within as part of the 'true up / down'

3. Outcome Based Regulation (Schedule 1)

Given the Airline Community views on the CAA's proposals for Outcome Based Regulation ("OBR"), as set out in our recent response to CAA CAP2274 where we have highlighted a number of fundamental matters we believe need to be re-considered, the Airline Community have not commented in full on the associated proposals set out within this consultation. Instead, we strongly believe these matters are best dealt with as part of our proposed wider review with changes to the License made thereafter and in response to such further developments.

Notwithstanding and without prejudice to those comments above, we would make the following comments on some specific points raised within the consultation:

3.1 Schedule 1 – Part 2(a) - Quality of Service Monitor.

We note that this survey-based measure is to be measured as a monthly moving annual average. We would urge the CAA to move to a purely monthly based measure. The use of a moving annual average is serving to "smooth" any drops in performance. It is in the consumers' best interests that HAL's performance is measured at as granular level as possible so that all consumers get excellent levels of service on a consistent basis.

3.2 Schedule 1 – Part 3.7 - Surface Access Customer Satisfaction Survey.

We note that this survey-based measure is to be measured as a Quarterly moving annual average. We would urge the CAA to move to a purely quarterly based measure. The use of a moving annual

¹ Paragraph 1.50, CAA CAP2305



average is serving to “smooth” any drops in performance. It is in the consumers’ best interests that HAL’s performance is measured at as granular level as possible so that all consumers get excellent levels of service on a consistent basis.

3.3 Schedule 1 – Part 3.9 - Special Assistance Quality of Service Monitor.

We note that this survey-based measure is to be measured as a Monthly moving annual average. We would urge the CAA to move to a purely monthly based measure. The use of a moving annual average is serving to “smooth” any drops in performance. It is in the consumers’ best interests that HAL’s performance is measured at as granular level as possible so that all consumers get excellent levels of service on a consistent basis.

3.4 Schedule 1- part 3.28 - Provision of stand facilities.

We do not agree with the method proposed in the Licence for measuring the availability of these assets. The method takes each of the four assets % availability in a particular month and adds all the availability together before dividing by four (or three in the case of T4). This results in an average availability across all four (or three) assets, so the airport could for example have poor availability for FEGP for that month, but as an average still pass the target. In its current form this measure has reduced the target standard when compared to Q6. To address this we would recommend that the CAA adopt a standard that states no measure of availability for FEGP, PCS, Jetty or Stand Entry Guidance can be below 99% for the overall availability standard to be met.

3.5 Schedule 1 – Annex 2 F2 A2.6 Wayfinding.

We do not agree with the revised question text proposed. It does not provide a clear enough indication of how well the consumer is managing to navigate LHR. We would instead urge the CAA to adopt the following questions (as already proposed by the airlines in our “Way forward” response.

The question being asked of Heathrow customers should be designed to be an outcome of successful wayfinding and journey management. The outcome is essentially to be able to find your way in a ‘right first time’ manner. We feel it is necessary to ensure that all customers are asked a similar question whether departing, arriving and/or transferring.

Measure:

- Departure - On a scale of 1 to 5, I was able to go to the right place to check-in and catch my flight, first time.
- Transfers - On a scale of 1 to 5, I was able to go to the right place to catch my flight, first time?
- Arrival: On a scale of 1 to 5, I was able get to immigration and through the baggage hall, first time?

Schedule 1 – Annex 3 A3.4 Where the Licensee cannot reach agreement with the AOC

We would repeat again our statement made in the OBR Consultation response:

The Airline Community feels that it continues to be a necessity to ensure that any alleviation of service standards is only through the Airline Community. This is particularly important as in all cases of potential alleviation there is a service impact on the airline customers, with whom there is a contract of service and expectation of standards being met. Where these standards are not met, there may be consequences to the airline in terms of financial recompense, such as with under



performance in PRS, baggage, or prolonged delay; with others there may be reputational damage and future choices made not to fly from Heathrow. Currently this provides healthy challenge to HAL in delivering standards and where there is failure and HAL seeks alleviation, work is done to outline the operational reasons for such alleviation to be requested. Where appropriate alleviation is never withheld, and in a few examples each year it may be challenged, which appears to be a healthy reflection of the process.

The CAA have not demonstrated a requirement it to be the ultimate arbiter, as proposed within the consultation. The existing process has served the consumer well and on the rare occasion counsel from the CAA has been agreed by HAL and airlines, this has been agreed to. We are deeply concerned that any changes will lead to a continued escalation of issues by HAL and used to by-pass airlines. Given other concerns with OBR, if there is no opportunity for the community to represent the consumer in a very direct challenge of standards delivery through alleviation oversight, then we would likely recommend to CAA that SQRB is maintained until the whole OBR structure is in a more appropriate configuration.

Schedule 1 – Queuing Times and Measurements

We would highlight our comments in particular with regards to the Airline Community's proposals for queue measurements and monitoring, as set out in our response to CAP2274, including those on requirements for per passenger and daily measurements, which would require changes to the License and the CAA's proposed draft text.

4. ORCs – Charges for other services (Part C)

The Airline Community support the introduction of clauses C2.2 and C2.3 as this provides greater clarity to the annual pricing process allowing greater time for airlines and other users of the services to plan ahead for their forthcoming financial years.

Additionally, the Airline Community welcomes the introduction of C2.9 to C2.13 as this was clearly an area requiring addressing. The new drafting should be sufficient in allowing the CAA to make any determination if airlines and HAL are not able to agree on certain aspects of the development and treatment of ORCs.

Although, we welcome these changes, the CAA have so far inadequately dealt with the extent to which HAL are required to provide transparency in the provision of data that supports the delivery of ORCs. For the past 2 years, airlines have been requesting, not unreasonably, for HAL to facilitate an independent audit of ORCs to ensure each service is being delivered in a cost-effective manner. The CAA will be aware that HAL have made it very difficult for airlines and any independent 3rd party to access the relevant key data in order to carry out an effective audit. We expect the CAA to be able to write into the License the requirement for HAL to be completely transparent in its provision of data in this area and to support a 3rd party audit on request by users. Airlines would be satisfied with the ability to carry out a detailed forensic audit once per year, with any request to audit cannot be unreasonably withheld by HAL.

We would also like to take this opportunity to highlight that users of ORC services, namely airlines, are given the opportunity to be involved in the decision making of future ORC service provision. HAL currently say that we are through current governance processes, however, in 2 recent major decisions involving ORCs, airlines have been marginalised. The prime examples of this are the key decisions for [REDACTED]. In both

instances, airlines were told that we were being heavily consulted on the process and yet decisions were made solely by HAL without our involvement. As ORC charges are at a pass through, with HAL effectively the steward in their monopoly position, airlines need to have the ability to be involved in the decision-making process to ensure the costs and quality are in line with our expectations as customers of those services. The CAA must reflect the necessity for airlines to be involved in the process in the new License and if they aren't involved, there must be consequences, such as an ability for airlines to request the decisions are overturned and that a new process is conducted with airlines involvement.

5. Financial Resilience (Part E)

The Airline Community welcome the intent of the CAA in further strengthening requirements on HAL in relation to financial and operational assurances. We do not have specific comments on the drafting proposed by the CAA however would point to comments made within the Airline Community and airlines' responses on these aspects, particularly with regards to transparency and assurances.

6. Governance and Consultation (Part F)

In general, the Airline Community are welcoming of the enhancements within the License that improve the governance and consultation arrangements within the License – where we have specific comments on arrangements for certain areas, Terminal Drop Off Charge or OBR for example, we have addressed these under the relevant Sections within this response.

The Airline Community are unclear however as to the CAA's reasoning for removing the reference to "Charges that are subject to Condition C2¹". As such its removal cannot be supported at this point in time.

Whilst the CAA have sought to clarify, and in some instances enhance, its ability to intervene in certain matters, the past 18 – 24 months have highlighted such gaps in governance are often only brought to light when unforeseen issues arise and where the CAA's role has either been unclear or the CAA has felt unable to make a determination. For example, where HAL chose to close Terminal 4 which had subsequent costs and particular challenges for users of the airport and therefore ultimately consumers.

Whilst welcoming the proposed changes to Section F1.1 and F1.2 this still is primarily focussed on the 'consultation' of any proposed changes.

We believe therefore that the CAA should have a clearer ability to intervene on any matter raised in the interest of consumers – including material decisions taken by HAL post finalisation of the H7 settlement that were reasonably, or ought to have been, known at the time of submitting evidence, and result in a favourable outcome to HAL at the expense of airport users and consumers. Noting the License is aimed at the Licensee, this should include wider drafting compelling HAL to respond to specific requests, including specific reference within the License to meeting any requirements, provision of data and timetable set out by the CAA, including future processes for H8. With regards to the timetable to respond, we would suggest this should be within two working weeks unless otherwise stated by the CAA. Alongside this build within the License and without prejudice to

comments elsewhere within this response, we would encourage a review by the CAA on its ability to intervene and make such determinations as it ultimately sees fit.

In terms of the governance consultation arrangements themselves, we note many elements of these will be best addressed in respective protocols, handbooks and terms of references; however, we strongly encourage the CAA's engagement alongside those reviews as set out in the (proposed) F1.3 and F1.7. The Airline Community also retain our position that, subject to the development of these arrangements, further enhancements within the License may be required, for example requiring HAL's compliance with such protocols or provision of appropriate information to Relevant Parties.

7. Capital Arrangements (Draft changes incorporated throughout Table 1.1)

7.1 Approach to Capital Envelope [Paragraph 11]

The Airline Community have, and continue to be, supportive of an approach to the overall capital plan that allowed for an 'in-Q' upwards adjustment to reflect an improved outlook on overall performance (notably on passenger volumes) and / or any exceptional situations collectively agreed between the Airline Community, HAL and the CAA which would require additional capital expenditure above the CAA's initial allocation. We note the CAA's intention to keep this under review and look forward to engaging on the details in due course though would reiterate our previous position that such an increase must be with the 'agreement' of the Airline Community, as per the existing governance arrangements. In the meantime, specific reference under F1.1(b) would seem appropriate.

7.2 Development Capex [C1.9 and C1.10]

The Airline Community believe that under the proposed drafting for the 'annual development capex adjustment' that the wording is amended as follows:

'the **[undisputed]** actual capital spending incurred during the development stages of projects prior to transitioning through Gateway 3....'

Formal governance relating to the capital interplay with the aeronautical charges is enacted at Gateway 3 however there are occasional instances where HAL, having presented information at an earlier Gateway stage has not received airline endorsement but HAL still progresses 'at risk'. The addition of 'undisputed' is necessary as:

- (i) as set out within our response to CAA CAP1996 it is clear that HAL's 'at risk' is not actually true given they are still compensated for the expenditure as part of the calculations on the aeronautical charge; and
- (ii) the explicit reference to "...in accordance with the governance arrangements" shows a clear expectation that such development spend is subject to a level of engagement and approval pre Gateway 3, as evidenced by the current arrangements which were introduced following the CEPA capital efficiency recommendations to the CAA as part of the mid-Q6 review.

By including 'undisputed' within the text this not only reaffirms existing practices but also ensures that when there are genuine areas of disagreement pre-Gateway 3, there is meaning to HAL continuing 'at risk'

7.3 Transition Arrangements

The Airline Community are cognizant that for capital expenditure in particular there will be a number of 'transition' projects across the Q's that, as currently proposed, will continue to be treated as per the current License arrangements. We would highlight that due diligence that is required in particular on these elements to ensure there are no unintended losses or amendments, for example that the proposed changes from "Regulatory Period to Regulatory Year" under the trigger calculation is applicable to both current and any future trigger arrangements.

8. Other Matters for Consideration

8.1 CPI and RPI [Paragraph 12; Draft changes incorporated throughout Table 1.1]

The Airline Community note and welcome the movement to CPI as previously raised with the CAA, not least given the proposed reforms to RPI. In doing so within the context of the License however we would ask the CAA assures itself that such proposed changes within the license for H7 does not lose or distort any current incentives and arrangements.

By way of example, under C1.6 (Capital Trigger) the reference to "CHAW Retail Price Index" has been replaced by "ONS". A principle foundation of the capital trigger is HAL does not earn a return on such expenditure between the agreed trigger completion date and the actual trigger completion date. Should such a change distort the linkage between the rate of return i.e. HAL are still earning some return due to CPI / RPI variation, then this will need to be re-considered.

The Airline Community would welcome the opportunity to understand further from the CAA the implications of the CPI / RPI changes being proposed.

8.2 Commercial Arrangements [C1.14 and C1.15]

As notified to the CAA at the time, the commercial arrangements introduced in C1.14 and C1.15 were to address a specific matter, whereby a number of airlines reached an agreement with HAL to address the transition between Q6 and H7 (2020 and 2021 being referred to as iH7)

Whilst noting the removal of the specific details of the iH7 arrangements, continuing with such provisions, particularly given efforts elsewhere in the document to remove superfluous text, is unnecessary and suggests an approach of lightening regulation on HAL. We would propose its removal in its entirety.

Whilst not envisaged, should any such similar events materialise again in the future the CAA has the appropriate powers to introduce such a change to the License, as it did so previously.

8.3 Terminal Drop Off Charge [Draft changes incorporated throughout Table 1.1]

The Airline Community note that the Terminal Drop Off Charge ("TDOC") is still to be finalised . As such, whilst noting specific proposals within the consultation, and strongly supporting the specific reference under the Part F (Governance and Consultation), we believe this is an area to addressed as part of the ongoing development and finalisation of the TDOC proposals.



8.4 S-Factor [Draft changes incorporated throughout Table 1.1]

The Airline Community welcome the clarification that the S-Factor incorporates 'health and safety' measures as well.

During Q6 / iH7 the issue of the S-Factor arose on occasions (for example the extent it should be applied to particular Covid measures). During such discussions between airlines, HAL and the CAA it became apparent a difference of views and unclear guidance as to when and how it should be applied. The Airline Community would welcome greater documented guidance from the CAA in order to minimise potential disputes in the future.

We remain available and welcome the opportunity to discuss further the points and questions raised within.

Yours sincerely,

A handwritten signature in black ink, appearing to read 'Gavin Molloy'.

Gavin Molloy
Chair – LACC
London (Heathrow) Airline Consultative Committee

A handwritten signature in black ink, appearing to read 'Nigel Wicking'.

Nigel Wicking
Chief Executive – AOC
Heathrow AOC Limited