

Transport for London's response to the CAA's Discussion paper on the regulatory treatment of issues associated with airport capacity expansion.

Background

1. Transport for London is working on behalf of the Mayor of London to deliver the Mayor's aviation programme. As well as being Londoners' elected representative, the Mayor has specific statutory duties that are highly pertinent to the question of where to locate new runway capacity, including planning and development, housing, economic development and regeneration, transport, environmental issues and health inequalities.
2. TfL, working with its advisors, has developed specific proposals for construction of a new hub airport in the Inner Thames Estuary (ITE). In its Interim Report, the Airports Commission acknowledge that construction of a new airport in the ITE is in a different category to options involving the incremental expansion of existing airports, noting that 'the scale of the benefits ... is potentially greater than for any of the other options that the Commission has considered'. A detailed paper, prepared by Ernst & Young, sets out a proposed 'base case' funding and delivery model for a new hub airport¹ - although alternative approaches may be possible. EY assess the new airport as commercially viable, on the assumptions set out.
3. The Airports Commission is expected to make a decision on whether to shortlist the ITE option this autumn, and is undertaking feasibility studies in four areas. TfL therefore considers a CAA discussion paper or consultation exercise that looks at only three of the four options under consideration by the Commission to be premature, and by furthering the debate on those options to the exclusion of the ITE, potentially prejudicial to a fair consideration of the latter.
4. If the ITE option is shortlisted, TfL expects the CAA to change its approach to ensure that the regulatory issues associated with the ITE are considered alongside the incremental expansion of existing airports, and not through a standalone process.

Specific responses (where relevant to the mayor's statutory duties)

Regulation, competition and market power

Q2.1 Do you consider that new runway capacity in the south-east of England would change the competitive conditions in the south-east of England? If so, what are the likely changes in those conditions?

TfL believes that construction of a new hub airport, with a significant increase in capacity, together with closure of Heathrow, would promote greater competition between airlines, with resulting downward pressure on fares and wider choice of international and domestic destinations available to passengers.

¹ <https://www.tfl.gov.uk/cdn/static/cms/documents/financial-and-commercial-considerations.pdf>

Conversely, Airports Commission figures show that a 3-runway Heathrow would effectively be full shortly after opening, operating at 80 – 90% runway utilisation – with little hope for any competition benefits for consumers. An expansion of Gatwick would do nothing for the competitive dynamic at the main hub, which would become even less competitive as demand outstripped supply, forcing prices up further. Despite Gatwick’s transformation since it was sold, it has not served as an effective competitor to the hub.

Freight operators would also benefit from the competition offered by a 4-runway ITE hub, particularly in allowing access for more freighter operators who are almost completely excluded from Heathrow today.

TfL submitted a paper on “Competition and Airline Needs” to the Airports Commission on 23 May² examining these issues in detail.

Risk, Regulation and Financing

Q4.6 Do you consider that the Government has a role in the mitigation of risk, particularly political risk?

Q4.8 Do you consider that Government involvement would assist an airport operator gaining the necessary finance for capacity expansion?

TfL believes that the environmental, public health and noise impacts associated with the expansion of Heathrow mean that the political risk is not only very significant, but unavoidable given the need under a democratic political system to go through due process before a decision is taken and binding contracts are awarded. The Mayor has been clear in his view that a 3rd runway at Heathrow is not deliverable.

Historically (and frequently today in other countries), the majority of large airports globally were initially developed and operated by Governments prior to privatisation or increased involvement by the private sector. TfL’s proposal for a new airport in the ITE envisaged Government acquiring the land and letting contracts for construction of a new airport, as well as acquiring Heathrow and operating it prior to its closure (with income from Heathrow operations being used in part to pre-fund construction of the new airport). The new airport, once operational, could then be sold (or a concession to operate awarded) in order to recover the construction costs. A recently constructed, modern airport with the ability to meet long term growth in demand would attract huge interest from infrastructure investors.

This approach was designed to ensure that political and delivery risk was retained by Government during the crucial pre-construction and construction phase. The scale of investment and challenging timescale, combined with the level of risk, make it likely that Government is best placed to play the key role in delivering a new airport and surface access links.

² <https://www.tfl.gov.uk/cdn/static/cms/documents/q-extract-ac-discussion-paper-four-airport-op-models.pdf>

Q4.13 Do you consider there are other case studies that could provide useful insights?

If the Isle of Grain option is shortlisted, TfL urges the CAA to conduct case studies on the financing and delivery models of new airports internationally (for example Istanbul) to inform consideration of the appropriate regulatory regime for a new hub airport.

Q4.14 Do you consider that there is a role for Government in providing financial assistance for any capacity development?

As described above (and set out in detail in Ernst & Young's September 2013 paper), TfL's proposal to the Commission envisages a significant role for Government in financing and delivering a new hub airport on the ITE – in relation to:

- Acquiring and preparing the land;
- Letting a contract or contracts for the construction of the airport (prior to a recovery through a sale or concession once operational)
- Funding and letting contracts for the surface access measures required (except where PPP options exist, such as for a new access road).

The justification for this level of government involvement is in the public goods that would flow: the environmental, economic and socio-economic, regeneration and housing benefits that would accrue to current and future generations.

TfL believes the case for government financial assistance in respect of shortlisted options to be much weaker given the environmental, public health and noise consequences of Heathrow expansion.

Inter-generational issues

Q5.1 Do you consider that the generation that is demanding a particular piece of infrastructure should pay for it?

TfL believes that the benefits of a new hub airport with capacity to grow to meet rising demand will accrue as much if not more to future generations as the current generation, and that the regulation and financing approach should reflect this. For example, the Airports Commission's assumption in their Interim Report that debt should be repaid by 2050, some 20 – 25 years after the opening of the new capacity, seems wholly inappropriate.

The CAA's Statutory Duties

Q9.1 Do you consider that any part of the Act presents barriers to investment, including with respect to any potential capacity expansion?

TfL believes that resilience should be at the heart of the CAA's primary duty to users of air transport services, and that improved resilience can only come through the

spare capacity (and hence ability to absorb shocks) offered by a 4 runway airport. Runway utilisation of 70-75%, in line with international best practice, can ensure an airport is resilient and optimised for transfers.

Even based on the lower demand forecasts the Commission has adopted, the Interim Report identified that a three runway Heathrow would be at 80-90% runway utilisation shortly after opening, in 2030. This means the airport will be effectively be full, with significant impacts on resilience and slot availability, particularly during peak periods.

On a relatively broad interpretation, the CAA's statutory duties – specifically the duty to 'further the interests of users of air transport services regarding the range, availability, continuity, cost and quality of airport operation services', could be taken as supporting the provision of spare capacity for the purposes of improving operational resilience, promoting competition between airlines and meeting future demand growth. However, the current regulatory approach, with its focus on incremental additions to the RAB over a 5 year control period, does not contain a mechanism or incentives to provide such spare capacity, which will benefit future generations as much as current.

These issues will need to be clearly addressed following the Airport's Commission's decision on the ITE this autumn.

Transport for London
10 July 2014