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Re. Economic regulation of capacity expansion at Heathrow: policy update and consultation (CAP 1722)

Introduction

1. This submission is made by International Consolidated Airlines Group SA (IAG) in response to the CAA's consultation of October 2018 on core elements of the regulatory framework to support capacity expansion at Heathrow (CAP 1722). It represents the views of IAG and its subsidiary airlines: British Airways, Iberia Airways, Vueling, Aer Lingus and LEVEL.
2. This submission will set out IAG's responses to the key issues raised by the CAA in CAP 1722 regarding capacity expansion at LHR and will also address other points arising from the consultation.
3. Submitted with this response is an RBB Economics paper on the effect of congestion at Heathrow Airport, commissioned by IAG.
 - a) IAG supports expansion at Heathrow, but it is imperative that it is constructed in an affordable manner, with airport charges no higher than flat in real terms. Consumers at Heathrow already pay the highest airport charges in the world, so an increase will further constrain demand and severely limit the number of airlines willing to take up new capacity at Heathrow, undermining the case for expansion.
 - b) IAG understands the need for limited expansion related expenditure pre-DCO approval to help maintain the timelines for the third runway. However, the risk of these costs should be borne solely by HAL, not consumers. It is also important that HAL does not use the 'cost of delay' argument to rush through designs that have not been fully evaluated by relevant stakeholders, especially given the fact that there has been a complete lack of cost information and poor programme management.

Executive Summary

4. IAG's key messages are:
 - Discussions around a "commercial deal" between HAL and IAG for the iH7 period are better characterised as an "agreed compromise" in the context of the absent regulatory certainty that the extension to Q6 and the iH7 period has fostered.

- IAG has no appetite for any moves to a commitments framework as at Gatwick when HAL starts its next regulatory period – its monopoly position will simply be stronger and will require full regulation.
- The CAA must require HAL to produce an initial and revised business plan to ensure decisions for H7 are based on the latest information. HAL must justify their plan in the round and ensure full transparency due to the scale and complexity of H7.
- Absent a “commercial deal” the CAA should do a full reset of the Weighted Average Cost of Capital (WACC) for the whole iH7 period including a likely third interim extension year.
- IAG supports the proposal for a new licence condition to promote economy, efficiency and effectiveness in relation to HAL’s operation and development of the airport
- IAG agrees with the CAA’s assessment that HAL has only made “limited progress in providing convincing information on costs and efficiency”.
- The CAA must give due focus to the Arora Group proposals for its development plans at Heathrow as these offer a genuine alternative that can be designed, built and operated and not simply extend HAL’s monopoly.
- However, the CAA should be careful that assessment of the Arora Group plans takes account of their relative competitive position versus HAL and ensure that the benefits of competition are not lost to the consumer.
- The CAA’s confirmation of support for the “user pays” principle for surface access costs is welcomed.
- However, IAG is concerned that the CAA is open to scope creep on surface access schemes that will increase costs for aviation consumers and threaten affordability. Surface access schemes should therefore be evaluated for the value that they bring to the consumer.

The overall timetable and the interim price control

5. IAG’s responses to these issues are made assuming that the eventual regulatory arrangements are based on a CAA “mini” review of the regulatory building blocks as proposed in CAP 1658 absent of any bilateral agreed compromise between HAL and airlines that could potentially supersede this. The following responses are therefore predicated on a CAA-led interim price control.
6. Before addressing these issues IAG wants to clarify our position relating to the interim price control alternatives discussed by HAL with some airlines. IAG does not view this as a “commercial deal”, rather it is an “agreed compromise”. As outlined in our CAP1658 response: *“the fullest protection that consumers and airlines have from HAL’s monopoly power is for an effective regulator to conduct a full review at regular intervals to ensure that consumers are not being taken advantage of”*¹.
7. IAG’s position on this is unchanged. The “agreed compromise” position that IAG has discussed with HAL to date is a pragmatic position taken for a short-term, limited period only in the absence of the CAA proposing to conduct either an effective interim review or a full regulatory review of HAL which would have offered the greatest protection to consumers and airlines who are subject to HAL’s substantial market power. This position and our appetite to explore such an agreed compromise is not indicative of any desire for HAL to face a lesser level of regulatory scrutiny and/or reduce the need for the economic regulation of Heathrow Airport. Rather it is a logical response to the alternative of the CAA’s regulatory proposals for iH7 that would not have adequately addressed HAL’s market power in that period.

¹ IAG CAP 1658 response, para 36

8. The CAA notes that such arrangements have “emerged at Gatwick airport” and HAL itself has recently encouraged the CAA to move towards the type of Gatwick commitments framework in the next regulatory period at Heathrow². IAG strongly disagrees with such moves – Gatwick Airport is not a proxy for Heathrow Airport whose monopoly position will only grow with Expansion. Full economic regulation will continue to be required at Heathrow conducted by an accountable regulator that ensures this monopoly provider is subject to a proxy for the same commercial pressures that are experienced by HAL’s customers.
9. IAG stated in its CAP 1658 response that it was likely a third interim extension year would be required, in addition to the Q6+1 extension year put in place for 2019. The H7 period should have run from 2019 onwards rather than HAL benefiting from a continuation of the regulatory settlement, determined in 2013, running up until 2022 and potentially beyond. In the absence of a fully regulatory review which has generated regulatory uncertainty we have taken a pragmatic approach to consider an “agreed compromise” in bilateral discussions with HAL to cover the 2021-22 period. The basis for this is that we have a good degree of understanding of how HAL is out-performing the Q6 regulatory settlement and a relatively high-level of certainty of the likely capital plan over this period. Therefore prior to HAL securing its Expansion DCO we are in a position to take a view on a compromise position in the short-run. IAG would not be able to do this for a full 5-year regulatory period and not for a new regulatory settlement with the scale of investment that the eventual H7 period will entail for Expansion.
10. If an “agreed compromise” arrangement is agreed between HAL and airlines, then the arrangements for this should be incorporated into the HAL licence issued by the CAA. This would mean that any arrangements can then be enforced by the CAA through the licence and maintain accountable regulatory oversight through the licence breach and enforcement tools the CAA has.
11. IAG believes that there is an opportunity to review the overall structure and mechanics of airport regulation prior to heading into the H7 period and the huge costs and challenges that Expansion will present. The challenge of Heathrow Expansion makes it imperative that the system of airport regulation is fit for purpose going forward and delivers the most efficient and demonstrably fair outcomes for the consumer, whilst ensuring that HAL face the right incentives and are not over-rewarded at the consumers expense. As part of a review of how airport regulation should be updated IAG would contend that the following areas should be considered. A key objective for airport regulation and expansion and is ensuring that risk is borne by those parties best-placed to manage it.
12. At a structural level, current airport regulation is based on a per passenger charge basis which sees HAL rewarded for volume risk that airlines bear and translate into yield risk. A review of how suitable the current mechanisms are would be appropriate as the CAA considers the regulatory framework for expansion. The regulated rate of return and how that compares to market estimates and HAL’s assessed Weighted Average Cost of Capital should also be reviewed to ensure that consumers are funding the most optimal financing arrangements.
13. Below the structural level airport regulation should also provide for a range of incentives for HAL to ensure that cost efficiencies for CAPEX and OPEX, and maximum commercial revenues are

² HAL response to CAA CAP 1684 Gatwick future economic regulation

achieved both within the current regulatory period and beyond to ensure that consumers only pay what they need to, both now and in the future. The appropriateness of other regulatory incentives such as service quality bonuses should also be reviewed to establish whether they are needed in future and, if so, how they are best applied. IAG raise these issues as areas for further discussion with the CAA to ensure that airport regulation continues to deliver the most optimal outcomes for consumers in the future.

H7 regulatory framework timetable and business plan

14. HAL must produce and work to a timeline for Expansion that allows airlines to clearly understand what activity is happening when. The key challenge for airlines is to be able to have clear visibility of HAL's expansion plans and for these to be robust and reliable enough for us to be able to effectively plan our engagement and analyse and evaluate. HAL's performance in this regard has been very poor to date and must improve for us to be able to challenge those plans and get confidence in them. Failing to do this risks Expansion and puts at risk our capability to represent consumers in the Expansion process.
15. IAG supports the CAA's confirmation that HAL should produce a business plan for H7 by the end of December 2019. However, IAG does not agree with the CAA's proposal that HAL should only produce "one high quality business plan with information updated on a flexible basis"³.
16. This position is informed by our experience of engaging with HAL on master-planning issues since 2016 and the scope required of the H7 plan itself. Expansion master-planning has proven to be complex, fluid and challenging for HAL and for airlines to be consulted upon. It is inevitable that beyond the publication of an initial business plan in December 2019 that there would be changes, especially as the scale of Expansion work planned ahead of a DCO decision is significant and will lead to a greater understanding of these costs. IAG is concerned that allowing HAL to update a business plan submitted in December 2019 "on a flexible basis" risks a lack of transparency and accountability for change and may result in a core plan drafted in 2019 being used as the basis for the H7 period starting in 2022 or even 2023. A revised business plan will require HAL to re-justify their plan in light of the latest available information and ensure the H7 plan is based on an up-to-date understanding of Expansion and airport operational requirements.
17. Likewise, the challenge of identifying and balancing the investment and operational needs of the existing airport infrastructure will need to be balanced against proposed Expansion costs within the plan. A revised business plan at a later date will allow for future Expansion master-planning development and existing airport operation requirements to be reflected at a more mature level. It will also require HAL to fully justify the content of revised business plan at a later date which they ought to have to do bearing in mind the scale of investment planned over this period will be more than at any point in the airport's history. As such a requirement to produce two business plans is wholly proportionate and reflects the need for a greater level of scrutiny and oversight for the upcoming H7 period.
18. Therefore, the CAA should require HAL to produce an initial business plan (by December 2019) and a revised business plan(s) dependent on the eventual end date for the iH7 period, i.e. whether a third extension year is required or not. This could be at the conclusion of the HAL-airline

³ CAP 1722 para 1.19

“Constructive Engagement” period in late 2020 or it could be in late 2021 if a third extension year is required and the regulatory process becomes stretched further.

19. IAG agrees with the CAA’s statement that “we expect HAL to consult carefully with airlines throughout the masterplanning and business plan processes to ensure that these plans appropriately reflect the views of airlines”⁴.

Arrangements for the three-year interim price control period

20. IAG is not surprised by the delay to the HAL Expansion process and the 6-month delay to the second consultation (CON2). We stated in our CAP 1658 response that a third extension year was likely, and we agree with the CAA’s assessment that, despite HAL’s assurances that it will maintain the current DCO timescales, that a 6-month delay and a third interim extension year will be likely and should be planned for.
21. IAG supports the CAA’s position that a full Weighted Average Cost of Capital reset is required. Whereas the CAA proposes this if a third extension year is needed this should be done for the whole of iH7 period. A reset drawing upon the WACC work done to date across both airport and ANSP regulation should be possible during 2019 and should be implemented alongside a full update of the other key regulatory building blocks, including passenger forecast numbers, operating costs and commercial revenues for the iH7 period as a whole.
22. If the CAA were to retain a full WACC reset for a third iH7 extension year only this should not be carried over to iH7 itself as the WACC for that regulatory period. Any iH7 WACC reset should be distinct from the H7 WACC itself so as to most accurately reflect the market conditions at that point in time and not bring forward a debate on WACC outside of the formal regulatory process.

Other interim price control points

23. In IAG’s CAP 1658 response we outlined our opposition to the CAA’s proposed policy of allowing early Category C expenditure to be admitted to the Regulatory Asset Base (RAB) prior to DCO. Whilst the CAA acknowledge this point was made⁵ CAP 1722 does not make clear what the CAA’s position is on this nor does it update on the feedback received on arrangements for early Category C costs including the CAA appointed expert to determine expenditure efficiency.
24. Early Expansion costs must be a key area of focus for the CAA, whether Category A, B or C, and IAG is concerned that the required level of rigour necessary for the CAA to achieve this is not in place. There are numerous issues including the significant growth in Category B costs from £285m to over £500m, re-classification of Category C to Category B costs, the growth in exposure to early costs ahead of DCO as HAL’s plans are delayed, and the absence of a clear CAA policy on early Category C costs pending your last substantive update in April 2018. Additionally, the anticipated CAA working paper on early Category C costs due in November has now been postponed until February 2019 – 10-months since views were invited back in CAP 1658. The CAA needs to clearly

⁴ CAP 1722 para 1.20

⁵ CAP 1722 para 1.9

outline its position in relation to early Category C costs and we look forward to receiving the proposed working paper in due course⁶.

25. IAG would like the CAA to fully outline the process for updates to the regulatory settlement for the iH7 period and for activity that is pending at the end of Q6+1. For instance, we expect that at the end of Q6+1 the CAA will commence its end of Q6 reviews of capital expenditure efficiency. Likewise, at the start of the iH7 period we expect the CAA to update the range of capital triggers for the period and specify new service quality performance stretch targets to ensure that performance is improving rather than remaining static and allowing bonuses to be earned without challenge.
26. Any pre-payment towards Expansion Costs should take account of the fact that new entrants at the point of opening new capacity will not have contributed towards it and any regulation should ensure that incumbents are not put at a competitive disadvantage through paying for facilities that will ultimately benefit new entrants at no cost to themselves.

Promoting economy and efficiency

Merits of a licence condition

27. IAG supports the CAA's proposal to introduce a specific licence condition promoting the economical and efficient operation and maintenance and timely development of Heathrow airport. We agree with the CAA's assessment that such a condition, with a behavioural focus, could be an additional tool for the CAA and would also allow the regulator to intervene during a regulatory period if that were required. Such a licence condition is present in many other UK regulatory regimes and with the scale and complexity of the upcoming iH7 and H7 periods as Expansion is progressed it could well prove to be a necessary safeguard for consumers and airlines.
28. IAG disagrees with HAL's assertions to the CAA that such a condition is not required. HAL note that its behaviour adapts and responds to other CAA priorities and this shows it acts in the consumers interest. IAG would note that all of HAL's comments are based on how it responds to the regulators priorities and incentives rather than responding to consumer needs directly. If HAL has shown that it does respond to such regulatory priorities then simply extending the regulator's capacity to potentially intervene if required during a regulatory period should only further advance the consumers interest.
29. In the current Q6 period IAG have concerns with HAL's management of capital projects (e.g. T3 Integrated Baggage system, T3 Flight Connections Centre, and Heathrow CTA tunnels refurbishment) and in the provision of information to airlines throughout the Expansion (as highlighted by the CAA to the DfT in your Section 16 advice). Both of these concerns could have been addressed by such a licence condition if that had been open to the CAA.
30. IAG would not agree that such a condition would require a set of balanced incentives. The entire regulatory system is predicated on incentivising HAL. If such a licence condition were used then penalties should be sufficient to incentivise HAL. Offering a positive incentive for behaviour HAL ought to be displaying anyway is simply rewarding poor behaviour in the first place.

⁶ CAP 1722 para 1.21, fig 3

31. Ultimately any licence condition will only be effective if the CAA is willing to use it and enforce it. Without a willingness to use the proposed licence condition it is of no value to consumers and airlines. Clearly having the ability to take action during the regulatory period will result in the CAA taking a more active role in monitoring HAL behaviour and performance which IAG would welcome and consumers would benefit from.

Drafting of the licence condition, introduction and iH7 areas of focus

32. IAG would suggest that the draft working be extended to include effectiveness as well as economy and efficiency, and make clear that it refers specifically to HAL rather than the wider definition here of Heathrow Airport as a location itself where more companies than just HAL operate. As well as actions undertaken by HAL being done economically and efficiently those need to be done in a way that delivers effective outcomes to complete the behaviour needed to ensure consumer interests are met. IAG would support the following draft text:

“The Licensee shall conduct its business in an economical, efficient and effective manner so as to secure the:

(a) operation and maintenance; and

(b) timely enhancement and development of facilities and services provided by Heathrow Airport Limited.”

33. IAG supports the CAA’s concept of revising sub-conditions as circumstances change to allow the CAA to adapt its focus. This will allow the CAA to focus on issues as different circumstances arise at Heathrow. The suggested iH7 areas of focus (does the DCO meet the NPS requirements; incurring only efficient costs now and ongoing; providing timely information to airlines and stakeholders) are supported by IAG.
34. None of the above should be seen as “too onerous” by HAL and IAG would strongly object to any HAL claim that the introduction of any such licence condition would introduce any additional significant regulatory risk. It is all behaviour that HAL ought to be doing anyway through its various business assurance process and is clearly a standard feature of other UK regulatory structures.
35. The introduction of such a condition by the end of 2019 in time for the iH7 period is supported. As the CAA has concluded IAG does not see a compelling need for a further licence condition for “Constructive Engagement” especially if the proposed economy and efficiency condition covers HAL during this phase of the regulatory period.

Alternative delivery arrangements

36. IAG view alternative delivery arrangements as a key element to ensuring that Expansion is delivered effectively and affordably for all stakeholders. HAL’s performance to date in sharing information to allow airlines to engage, understand and assess the developing masterplan has fallen well short of what we require to be able to have the assurances that Expansion is being progressed effectively or affordably. We agree with the CAA’s assessment that “HAL has made only limited progress in providing convincing information on costs and efficiency”⁷.

⁷ CAP 1722 para 3.12

37. As opposed to using the Innovation Partners process to allow competition to be introduced to the Expansion design process HAL's intent is rather to protect their own position and convert any potential competition into a secure supply chain. HAL achieve this by effectively making it more profitable for a competitor to become a HAL supplier rather than risk competing and potentially being excluded from Expansion as a whole. As opposed to benefiting from the competitive dynamic such alternative schemes should bring airlines and consumers are paying for the scheme and the dilution of those benefits. Despite this whilst Innovation Partners has a role to play (and IAG has submitted a number of proposals to the scheme itself) it clearly does not fulfil the objectives set by the CAA earlier this year to advance alternative commercial and delivery arrangements.
38. The Arora Group scheme offers a genuine alternative to HAL's proposal that could be built, delivered and operated and has brought competitive pressure to bear on HAL. This is of huge importance to the Expansion process as a whole highlighting that there are alternatives to the continued HAL monopoly of airport services and the design and build of Expansion at Heathrow. The consumer interest in the Arora Group scheme going forward is clear.
39. It is telling that whereas the CAA is with-holding judgment on the Arora Group proposals that include separate terminal delivery operation and/or delivery that HAL has already rejected these. IAG's view is that the introduction of even limited competition to the provision of terminal and airport services at Heathrow would provide a better outcome than the sole regulation of HAL itself. Arguments based on concerns over operational co-ordination and safety risks are clearly undermined by the fact that this type of separate terminal operation form the basis of many airport operations throughout the world and so can demonstrably be delivered. Furthermore, the competitive pressure that would be introduced would also spur an improved commercial proposition as well.
40. IAG supports the CAA's approach to focus on the proposals from the Arora Group. These clearly offer the greatest benefits to consumers by introducing competitive tension to the masterplan development process and ensuring HAL take account of other methods of delivery whilst also offering a genuine alternative to sole HAL ownership and operations. Full and fair consideration of this by the CAA is clearly in the consumer interest.

Developing the regulatory framework for alternative delivery providers

41. In focusing on the Arora Group proposals the CAA should make an accommodation for their competitive position in relation to HAL as the incumbent. HAL have a significant informational advantage over the Arora Group. Whilst we agree with the CAA that there is now a "competitive context" between HAL and the Arora Group⁸ some allowance for the basis of that competition should be made to ensure that it is given the opportunity to work and potentially generate benefits for the consumer and airlines.
42. In light of this the CAA's position regarding the justification of information requests that the Arora Group makes of HAL may set an unnecessarily high barrier and simply allow HAL to stall and

⁸ CAP 1722 para 3.21

ultimately reject the Arora Group proposals. Ultimately the CAA will need to judge whether the Arora Group requests and the HAL response to those requests is fair and advances the consumer interest.

43. IAG strongly supports Arora Group engaging with the Arcadis review of their proposals in order to achieve a better understanding of their plans potential. However whilst we want “substantive progress in a timely manner”⁹ a failure to achieve this may not be solely down to a lack of engagement, especially when the informational advantages HAL hold over Arora Group and the delays to Arora Group – HAL engagement over the past year are taken into account. IAG would caution the CAA against taking a “knife-edge” assessment of the Arora Group proposals following the Arcadis review. The competition that Arora Group has brought to Expansion remains at a nascent stage of development and there is a danger in it being strangled before it has the potential to deliver real benefits. It would also be hard to justify not progressing the Arora Group proposals on the basis of a failure to supply information on the detail of its plans when the same accusation could be made of HAL who have made “only limited progress in providing convincing information on costs and efficiency”¹⁰ themselves.
44. As part of its assessment of the Arora Group’s proposals the CAA invites the submission of views on “the commercial and regulatory arrangements that might support its proposals”. Whilst the Arora Group is best placed to comment on the commercial arrangements it envisages ultimately the regulatory arrangements will be determined by the CAA as the regulator. The onus should not be wholly placed on the Arora Group in this regard and the CAA should outline its thinking when it is appropriate to do so.

Surface access

45. IAG supports the CAA continuing its policy of the “user pays” principle in relation to determining the costs that aviation consumers should pay towards surface access scheme on and around the airport. This principle was outlined in CAP 1658:

“The ‘user pays’ principle means that all users of the surface access scheme should pay for it to the greatest extent practicable and any residual costs should be split between airport users and non-airport users in proportion to the benefit each receives.”¹¹

This policy has been long-held by the CAA and we believe has been used successfully to determine the costs aviation pays to wider surface access projects, Crossrail being a notable recent example.

46. However, we are concerned that whilst on the one hand the CAA confirms its support for the “user pays” principle it may on the other hand take a looser view on the range of schemes that may make a claim for costs from aviation consumers. This risks opening the consumers up to more costs on a greater scale at a time when aviation consumers themselves are funding one of the largest investments in the UK’s transport infrastructure. Making expansion affordable is fundamental to delivering expansion and placing too great a burden of surface access costs on

⁹ CAP 1722 para 3.23

¹⁰ CAP 1722 para 3.12

¹¹ CAP 1658 footnote 46

aviation consumers beyond that needed for the immediate operation of the airport itself threatens the viability of expansion itself.

47. IAG is concerned that the CAA's statement that "we do not consider it is our role to determine whether the [HAL] surface access strategy will meet the targets set out in the NPS as this is a decision for the planning process"¹² as being at odds with the proposed area of focus under the new licence condition that would determine if HAL "is preparing a DCO application with due regard for the requirements of the NPS"¹³. IAG would take the view that part of assessing the costs that aviation consumers should bear is also assessing the need for that cost in the first instance. The CAA position could currently be seen as being more open and simply making a judgment on what aviation consumers should pay for any scheme that is brought forward.
48. Furthermore whilst we understand the CAA's position that "we do not consider it is our role to oversee the design and delivery of third party projects...as these are matters for the Office of Rail and Road (ORR) and the DfT"¹⁴ there is surely a strong case for CAA oversight of HAL involvement and guidance on what quantum of costs will likely be acceptable to the regulator at as early a stage as possible and throughout the development of such schemes. The alternative would be to allow HAL's surface access strategy and associated to develop over time and effectively become a fait accompli for aviation consumers to pay for. Throughout the Airports Commission and NPS process HAL has repeatedly made unilateral surface access commitments without consultation with airline stakeholders or the CAA. IAG will take an active role as encouraged by the CAA in this area but the CAA also needs to take a more active role to prevent even more costs being added to the bill and threatening the viability of Expansion.
49. Unlike the opening of new runway capacity at Heathrow that is not likely to open until midway through the H7 regulatory period airport staff will be impacted by HAL's expansion surface access strategy much sooner in and around the time of DCO approval when construction begins and, it is proposed, airport parking facilities are removed without replacement. Engagement on these issues needs to happen now and in particular on staff modal shift pre-DCO. IAG's assessment is that HAL's strategy is neither robust nor realistic and will lead to significant costs and potential threats to the operational resilience and the retention of staff. IAG would like to understand what the CAA's views are on this subject.
50. More detailed comments on the proposed updated surface access policy are included in Appendix A of this response. IAG would note that the CAA must ensure that any future HAL public surface access commitments must be first consulted on by HAL with airlines. Throughout the Airports Commission and National Policy Statement process HAL has made unilateral commitments with significant affordability and deliverability implications without any prior consultation. The CAA should ensure this does not happen around the CON2, preferred masterplan and the subsequent DCO process.

END

¹² CAP 1722 para 4.12

¹³ CAP 1722 para 2.17

¹⁴ CAP 1722 para 4.23

Appendix A – Detailed comments on the CAA’s proposed updated surface access policy¹⁵

All update references are based on CAP 1722 Appendix D.

	Proposed update reference	IAG comments/questions
1.	Para 4 (a) “surface access projects, (considered individually, or as part of a surface access strategy...)”	Notwithstanding whether a project forms part of a wider surface access strategy or not a project should have a positive business case to as with any airport development project.
2.	Para 4 (a) bullet 3 “bring the investments forward to enable them to meet the timescales for the anticipated increase in demand for surface access brought about by expansion of the airport”	Propose amendment to reflect whether a surface access project is needed or not rather than basing an assessment on “an increase in demand”: “bring the investments forward to enable them to meet the timescales for the anticipated increase in demand for surface access brought about by <u>needed for</u> expansion of the airport”
3.	Para 4 (a) bullet 4 “take into account journeys made by airport staff”	Agree this should be linked to staff working at the airport, i.e. terminal, ramp, engineering.
4.	Para 4 (a) bullet 4 “made in relation to cargo operations”	Amend to specify cargo operations at the airport: “made in relation to cargo operations <u>at the airport</u> ”
5.	Para 4 (b) “Cost minimisation: the airport operator can <u>should demonstrate</u> that there is a need for the surface access investment”	Amend to require need for investment: “Cost minimisation: the airport operator can <u>should must demonstrate</u> that there is a need for the surface access investment”
6.	Para 4 (b) “the likely requirements to secure planning approval for expansion”	If this determination of requirements is being done pre-DCO then they should remain designated as “likely”: “the <u>likely</u> requirements to secure planning approval for expansion”
7.	Para 4 (b) “The costs of airport access projects should be measured against a base case which includes planned future upgrades by Government to road and rail infrastructure which would be made absent any further airport growth <u>assuming that the surface access demand arising from the airport is at a level which arises from its current capability.</u> ”	The CAA should outline when the Government base case will be determined. Will it be informed by statements of Government planned future upgrades prior to the intent to expand Heathrow or will it be done in the future, i.e. a statement made in the context of planned airport expansion?

¹⁵ CAP 1722 Appendix D

	Proposed update reference	IAG comments/questions
8.	Para 4 (c) “Direct users’ contributions attribution ”	Can the CAA further clarify the rationale behind the change from attribution to contribution? This appears to assume a contribution directly follows attribution which may not always be the case.
9.	Para 4 (c) “the airport operator should take reasonable steps”	In the context of the significant affordability challenge that Heathrow Expansion has HAL must consider all steps rather to ensure and demonstrate that everything possible has been done to defray costs: “the airport operator <u>must consider all steps and then should take reasonable steps</u> ”
10.	Para 4 (d) “infrastructure that has the sole purpose of connecting the airport to the wider transport network”	Can the CAA clarify that “the airport” is defined as the infrastructure within the airport boundary only?
11.	Para 5 “capital elements of the airport operator’s residual efficient costs would be added to the Regulatory Asset Base (RAB)”	IAG’s position is that the only capital expenditure that should be added to the RAB is for projects built by HAL within the airport boundary, i.e. not for a contribution made by HAL to a non-HAL project.
12.	Para 5 “any ongoing operating cost and revenues from the surface access projects <u>would be taken into account in the single till calculations used to set the airport operators price control.</u> ” added to the airport operator’s operating expenditure in subsequent price controls.”	The clear link between airport operating costs and the CAA’s determination of those opex costs for the subsequent price control period should be maintained as is. “Taking into account” could mean that operating cost and revenue efficiencies are not fully reflected and returned to consumers in any subsequent price control determination. “any ongoing operating cost and revenues from the surface access projects would be taken into account in the single till calculations used to set the airport operators price control. ” added to the airport operator’s operating expenditure in subsequent price controls.”
13.	Para 6 bullet 5 “it would not, however, be appropriate for <u>airlines</u> to have a veto over surface access projects...”	Can the CAA clarify if this update is correct as the addition of “airlines” does not appear to make sense in the context of the original text?