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

February 2019

Re: Independent Planning Costs Review on costs relating to the Heathrow Expansion Programme covering the period 2016 and 2017 (CAP 1752)

Dear Anna,

Virgin Atlantic Airways (VAA) welcomes the opportunity to respond to the publication of the Independent Planning Cost Reviewer's (IPCR) assessment of Category B costs incurred by Heathrow Airport Limited (HAL) during 2016 and 2017 (CAP 1750 and 1751), and the opportunity to respond to the CAA's initial views on the level of Category B costs, in those years, that HAL should be allowed to recover (CAP 1752).

In summary;

1. VAA have repeatedly raised our concerns to both HAL and the CAA about the absence of a baseline plan including; schedule, costs, and risks as well as the lack of governance in HAL's management of its Category B costs. It is clear that, as IPCR, PwC faced the same issues.
2. The lack of a baseline plan means that all Category B costs to date have been dealt with retrospectively and this is not acceptable.
3. We note with significant concern that HAL do not appear to have taken the PwC review seriously in the first instance and in a key area of focus for the review (evidence¹) provided poor quality information and subsequently refused to offer further clarity. Unfortunately we recognise this behaviour from our experience working on Expansion so far.
4. In another key area of focus (categorisation²) PwC were unable to verify a large percentage of the costs submitted by HAL as correctly categorised as Category B due to a lack of evidence provided.
5. This lack of due diligence on HAL's part and our experience of Category B to date leaves us increasingly concerned about HAL's ability to control cost and manage efficiency for the rest of the Expansion programme. The risks of this trend continuing are significant and already evident in relation to early Category C costs.

¹ CAP1750, p.6 – Are the costs included within the Statement and Opex Schedules provided by HAL supported by appropriate evidence?

² CAP1750, p.6 – Are the costs presented in the Statement and Opex Schedules correctly categorised as Category B?

6. We understand that the CAA intends to consult on its Category B policy in the spring of 2019, and we urge the CAA to make this consultation a priority.

Assessment of efficiently incurred costs

In CAP 1750 PwC's approach to assessing whether work undertaken has been delivered in an efficient manner focused on four areas; baseline, governance, progress and performance and provision of information, we consider each in turn;

7. **Baseline**; is there a clear and consistent baseline that sets out the scope, cost, schedule and risk up to approval of the DCO?

In their key findings PwC state *'it appears that HAL does not have a clear and singular integrated baseline plan to approval of the DCO that aligns requirements and scope with the associated time, cost and risk'* and *'HAL has not provided evidence which definitively sets out the baseline scope and deliverables required in 2016, 2017 or up to DCO approval. Whilst HAL does have a number of documents containing varying levels of scope detail, these do not establish a robust baseline.'*

In our view, given the evidence provided by the IPCR, it is clear that this requirement has not been met.

8. **Governance**; is there an established and appropriate governance process in place to manage the baseline?

During their review PwC found that *'a number of core programme controls processes were not in place'* this included change control and PwC noted that *'HAL does not operate a programme level change process for the Expansion Programme to manage the baseline scope, cost, schedule and risk'*.

In our view, given the evidence provided by the IPCR, it is clear that this requirement has not been met.

9. **Progress and performance**; is progress and performance clearly and consistently reported, including the consequential impact of delay?

With *'no clear and singular reference point (baseline) to measure against'* PwC state that they found it challenging to review progress and performance. In their key findings they say that there is evidence that some activities in 2017 were delivered late, and that the programme was underspent in 2017 but that the *'consequential impact of these factors on the overall schedule and cost forecast to DCO approval is unclear.'*

The absence of a baseline means it is not possible to tell whether the under-spend is due to the delays to activity or as a result of efficiency gains made by HAL. It is also not possible to assess whether the costs incurred were more or less than anticipated for the progress made.

In our view, given the evidence provided by the IPCR, it is clear that this requirement has not been met.

10. **Provision of information;** was information provided relevant, complete and in a timely manner?

The review by PwC (CAP1750 and 1751) took place between May 2018 and August 2018 and in CAP 1752 the CAA states it 'has concerns over the quality of the information initially provided'. Indeed it highlights key findings of the report as;

- although HAL provided a statement of Category B costs it was unable to provide supporting information,
- only after a further request from PwC did HAL provide information in the form of invoices and other accounting records, and
- this information only reconciled to 60% of the total costs and included incorrectly referenced and duplicate invoices

In CAP 1513³ the CAA state that '*HAL must provide an annual statement of the planning costs that it has incurred within four months of the end of each Regulatory Year in sufficient detail to allow effective scrutiny by the IPCR and/or the CAA.*'

It is apparent from the PwC report that the initial information provided by HAL was not timely, complete, or fully relevant and that as a result the CAA decided to extend the review period to November 2018.

Given the evidence provided by the IPCR, it is clear that this requirement has not been met.

11. In our view HAL has failed to meet all of the efficiency requirements as set out by PwC in its assessment of Category B costs and we note that PwC were also unable to assure the efficiency of that spend in the absence of a baseline plan. However we are not convinced that the requirements are an effective assessment of efficiency, they appear wholly evidential and do not include any evaluation of whether the costs incurred in 2016 and 2017 were necessary or that the output represents value for money.

12. It is for the CAA to determine what level of Category B costs HAL should be allowed to recover. Nevertheless we are genuinely concerned that the CAA proposes to allow HAL to recover 94% of its Category B spend given the evidence presented by PwC of HAL's inadequate management of Category B costs to date and their behaviour during the extended review. We encourage the CAA to carefully consider the evidence PwC have provided, along with the implications that its decision will have for the affordability of the programme in the future. We believe careful consideration by the CAA is particularly important in light of the significant increase in HAL's forecast for Category B costs for future years.

13. We support the Heathrow airline community view that these matters now need urgent attention and that the CAA consider;

- prioritising its consultation on its Category B policy in the spring of 2019,

³ The recovery of costs associated with obtaining planning permission for a new northwest runway at Heathrow Airport: Policy statement

- deferring its decision on the level of allowable Category B spend for 2016 and 2017 until it has completed its review of Category B policy and;
- ensuring HAL brings full monthly reporting of Category B, and Category C, costs to the airlines and the CAA for review

In addition, given HAL's behaviour in this matter, we suggest the CAA introduce enhanced efficiency tests into its policy for Category B costs.

We welcome any further discussion of the points made in this response.

Yours Sincerely,

Claire Lambert

Regulatory Affairs

Virgin Atlantic Airways