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**CAP1914: Economic Regulation of Heathrow Airport Ltd ("HAL")**

**British Airways response**

1. The Covid-19 Crisis has had a significant impact on British Airways and IAG, and as noted in the IAG preliminary first quarter results and update, "IAG has reduced passenger capacity in April and May by 94 per cent compared to last year, only operating flights for essential travel and repatriation."
2. "Passenger capacity from June will depend on the timing of the easing of lockdowns and travel restrictions by governments around the world. In light of the impact of Covid-19 on current operations...the expectation {is} that the recovery of passenger demand to 2019 levels will take several years"
3. British Airways and IAG support HAL's decision to suspend all work on the expansion programme in light of the Court of Appeal judgment that the Airports National Policy Statement ("NPS") had not been lawfully produced. Noting leave to appeal has been recently granted, until such time that there is clarity over the NPS either through a successful appeal to the Supreme Court or a review by HM Government of the policy set out in the NPS, no further work should take place, and any spend must be at HAL's own sole risk.
4. Furthermore, and considering the Covid-19 Crisis, we believe it would be imprudent to re-start any work on an expansion programme due to the high degree of uncertainty over the future of many airlines, and the recovery profile and plans of surviving airlines. Until such time as greater clarity over the economic future exists, our position remains that no expansion work should take place and that no expansion costs be included in core H7 plan. Furthermore, we require certainty on the charging structure of approved Cat B costs in light of the JR ruling on Heathrow.
5. We therefore support the CAA in focussing plans for the new price control from 1<sup>st</sup> January 2022 on the existing two-runway airport, and believe HAL, airlines and the CAA should work collaboratively to find mechanisms to deal with the issues raised by low and/or uncertain future traffic volumes on the price control outcome.
6. British Airways and IAG are open to exploring the regulatory framework for the airport, considering the unprecedented nature of the present Crisis on demand for air travel, though any changes to the regulatory structure must not inhibit airlines

from growing in future by resulting in excessive costs. This should not however be viewed as a desire to lighten the regulatory regime in a manner seen at other airports, and it remains important in our view to focus on fully resetting the regulatory building blocks for H7.

7. It is critical in the recovery from this Crisis that airlines are able to meet any passenger demand that might arise: excessive airport user charges arising from any price control may inhibit growth, reduce the opportunity for wider economic benefits generated by business and leisure travel, and is not in the interests of the consumer were future connectivity to be reduced as a result.
8. Whilst it would seem prudent to ensure there remains a mechanism for the re-activation of the expansion programme, we believe the focus for the forthcoming price control must remain on the existing two-runway, four-terminal airport. This price control period will require such complexity that it should remain in place whilst demand uncertainty remains and recovery is still in progress.
9. Expansion presents significant additional complexity to any price control period, and we believe that should it – however unlikely it seems at present – need revisiting during the new price control period, it should remain distinct and separate from the core two-runway airport, and could be handled separately through further consultations at that time.
10. Additionally, the future financial stability of the wider airline community to bear any charges related to expansion must be considered carefully in light of recovery from Covid-19. Increased marginal costs affect any airline's ability to re-open routes with the reduced connectivity clearly not beneficial to the consumer, undermining any case for expansion. Previous IAG submissions to CAA consultations remain applicable in this case, with affordability remaining a key criterion.
11. In the absence of expansion, we expect user charges to decrease significantly from the level at which they are presently set, a level that presently makes Heathrow one of the most expensive airports globally at which to operate.
12. We further welcome the CAA's position that Heathrow Airport has substantial market power for the purposes of CAA12, and agree with the CAA that a regulatory regime must continue to operate at Heathrow Airport. For the avoidance of doubt, we are firmly of the view that lower traffic levels do not translate into a reduction in the substantial market power that is exercised by Heathrow, which exists by virtue of its location.
13. We welcome the suggestion from the CAA to find creative solutions to dealing with the uncertainty in the present economic environment and agree that it is appropriate that this might require some modest adjustment of length of a typical price control period.

14. We are open to exploring different structures that could provide a better balance between risk and reward for any price control, ensuring only appropriate rewards flow to a regulated infrastructure monopoly business and risks are shared in a balanced manner. For the best interests of the consumer to be upheld in all scenarios, all building blocks must be appropriate under those different scenarios to ensure that Heathrow remains in all cases affordable to airline customers.
15. Stakeholder engagement is critical to an effective regulatory process, and we agree that it is clearly beneficial to hold more workshop-based discussions to gather necessary evidence for key building blocks of the price control. We would suggest that a style of workshop on those key topics used for consultations such as NERL is beneficial, with greater CAA involvement that enables the process to be as swift as possible.
16. As demonstrated by decisions made by many airlines to operate from Heathrow in future in preference to elsewhere, robust regulation of Heathrow needs to remain in place. Other airports have seen a relaxation of the regulatory regime that we do not believe is appropriate at Heathrow.
17. We believe some form of scenario-based approach is probably the most appropriate way to manage the uncertainty following Covid-19, although it is unlikely that specifics on any such numbers could be defined until much later when the economic landscape becomes clearer.
18. The value in developing the framework for such scenarios is in ensuring key building block elements are logically tied together. Operating costs, commercial revenues, capital plans and other areas all need to be linked to a form of scenario, and an appropriate price control outcome needs to result from each.
19. Constructive engagement in the near term therefore needs to focus initially on completion of any areas unrelated to expansion, thereafter followed by the remaining elements of the building blocks, working effectively through topics in forums described above.
20. Where there is insufficient time, clarity or information available to reach a conclusion on any topics, there should be flexibility in timetable and approach to continue to work through those topics into 2021, therefore we welcome the proposal to maintain a more active involvement in the process following the publication of the RBP.
21. For the avoidance of doubt, our expectation is that an RBP must be delivered no later than September 2020 to allow sufficient time for the necessary engagement required, and for airline feedback to fully inform the CAA's "way forward" document in January 2021. We maintain the view that updated detailed numbers should be delivered prior to the RBP in July 2020.

22. We envisage that the period following RBP in autumn 2020 will allow for far further and meaningful engagement in many areas, and the conversations will be better-informed as we all begin to understand how aviation has been reshaped by Covid-19. It may be that the CAA should view this as a second period of Constructive Engagement, though continuing the proposed workshop format and responding to any new economic information at that time.
23. We look forward to the more substantial consultation in June to ensure the process for H7 continues to move forward, and hope to work collaboratively with the CAA and HAL to ensure the H7 price control can remain on track for implementation in January 2022.

British Airways Plc