

Decision on modifications to NATS (En Route) plc licence in respect of Governance and Ring- fencing

CAP 1380

A large, abstract graphic occupies the bottom half of the page. It features a gradient of blue and teal colors, with a prominent diagonal line separating a darker teal area on the left from a lighter blue area on the right. The overall shape is a large, irregular polygon.

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Chapter 1

Introduction

Purpose of this document

- 1.1 This document sets out the CAA's decision on modifications to the NATS (En Route) plc ("NERL") licence in respect of Governance and Ring-fencing with the object of ensuring that users are adequately protected from risks which arise outside the regulated business.
- 1.2 The modifications affect NERL's licence with effect from 1 April 2016 in the following manner:
- 1) modify Condition 1 – Interpretation and construction to require that compliance certificates are approved either at a board meeting at which all the directors of NERL present, or that the Certificates are issued under a written resolution signed by all NERL's directors;
 - 2) modify Condition 5 – Availability of Resources and Financial Ring-Fencing to:
 - a) re-focus the annual directors' resources certificate to separate NERL's certification that it has sufficient operational resources from its certificate of sufficient financial resources;
 - b) include new statements from the directors setting out the processes used and factors considered in issuing the certificates;
 - c) require new annual certificates from NERL's directors that the licensee has complied with specific elements of the ring-fence;
 - d) require certificates of compliance with the ring-fence conditions to be issued each time the licensee declares or recommends a dividend;
 - 3) introduce a new licence Condition 7 requiring NERL to maintain an intervention plan to assist a special administrator in the event of insolvency;

- 4) introduce a new licence Condition 8 which will ensure the independence of the NERL board's decisions and contain a requirement that at least two 'Mandated Independent Directors' (MIDs) must sit on the NERL board unless the CAA consents otherwise; and
- 5) modify Condition 9: Prohibition of cross-subsidies to clarify and simplify the prohibition against cross subsidies and ensure it aligns clearly with the parallel requirements of European law.

The CAA's proposals and representations

- 1.3 With NERL's consent under section 11(1) of the Transport Act 2000 ("the Act"), we published, on 9 February 2016, final proposals by notice under section 11(2) of the Act¹ to modify Condition 1, Condition 5 and Condition 9, and to introduce Condition 7 and Condition 8 in NERL's licence.
- 1.4 We invited representations on these proposals by Wednesday 9 March 2016. A representation was received from NERL which confirmed acceptance of the CAA's proposed modifications.
- 1.5 In addition to accepting the proposed modifications, NERL formally requested the CAA's consent not to comply with the obligations contained in Condition 8, and thus to not appoint two mandated independent directors (MIDs). This consent was requested on the grounds that NERL considers that it has sufficient corporate governance arrangements in place to provide equivalent assurance that the appointment of MIDs would provide.
- 1.6 No other representations were submitted and the Secretary of State gave no directions to the CAA under section 11(4) of the Act requiring it not to make the proposed modifications.

¹ [CAP 1368: Proposal to modify the NATS \(En Route\) plc licence in respect of Governance and Ring-fencing: Notice under section 11\(2\) of the Transport Act 2000](#)

Chapter 2

The CAA's decision

- 3.1 In the absence of any adverse comments on our proposal, we have decided to modify NERL's licence with effect from 1 April 2016, as proposed in our notice of 9 February 2016 and consistent with our duties under section 2 of the Act.
- 3.2 The modifications to Condition 1, Condition 5 and Condition 9, and the new Conditions 7 and 8 are set out in Appendix A.
- 3.3 We have also consented to NERL's request to not comply in relation to certain provisions of new Condition 8 of its Licence. The request for consent from NERL is set out in Appendix B, and our consent, which includes the reasons for granting it, is set out in Appendix C.
- 3.4 Our position in respect to these licence conditions is based on the CAA's current risk assessment. Should the risk assessment change and warrant a different approach, the approach taken in this document will not fetter our discretion and we reserve the right to consider alternative actions, including revised licence conditions.
- 3.5 This decision was made by Mr Richard Moriarty, Director, Consumers and Markets Group, and a member of the CAA.

Civil Aviation Authority

22 March 2016

Appendix A

Modification to the Air Traffic Services Licence for NATS (En Route) plc

This Appendix sets out the modifications to the Air Traffic Services Licence for NATS (En Route) plc (“NERL”) air traffic services licence (the “Licence”) with effect from 1 April 2016 in relation to:

- Condition 1: Interpretation and construction - to include a new definition of “Compliance Certificate”;
- Condition 5: Availability of Resources and Financial Ring-Fencing - to implement the additional certification obligations described in the main body of this document; and
- Condition 9: Prohibition on cross subsidies - to clarify and simplify the obligation contained in it.

The changes to Conditions 5 and 9 are marked against the existing text of those conditions.

This Appendix also sets out the text of the following new conditions that also take effect on 1 April 2016:

- Condition 7: introducing a requirement to maintain an intervention plan; and
- Condition 8: introducing requirements for NERL to appoint mandated independent directors and in relation to NERL’s corporate governance.

For the avoidance of doubt, the existing obligations set out in paragraphs 9 to 30 of Condition 5 are retained without modification. Those paragraphs set out the obligations of NERL in relation to:

- Restriction on Activity and Financial Ring-Fencing;
- Amendments to the Finance Documents;
- Disposal of Relevant Assets and Indebtedness;
- Ultimate Holding Company Undertaking;
- Credit rating of Licensee; and

- Financial Indebtedness.

The text of the modifications is set out on the following pages. The text of paragraphs of the relevant Licence conditions that is not the subject matter of the modifications is not reproduced.

PART II THE GENERAL CONDITIONS

Condition 1: Interpretation and construction

Insert after the definition of “Auditors”:

- “Compliance Certificate” means a certificate that is addressed to the CAA and:
- (a) approved by a resolution of the board of directors of the Licensee either:
 - (i) at a meeting of the board of directors of the Licensee at which all directors of the Licensee are present; or
 - (ii) by a written resolution of the board of directors of the Licensee signed by all the directors of the Licensee; and
 - (b) signed by a director of the Licensee.

Condition 5: Availability of Resources and Financial Ring-Fencing

Summary

1. The objectives of this Condition are to set out measures which, inter alia:-
 - (a) require the Licensee to act in a manner calculated to secure that it has available to it sufficient resources to perform its Licence obligations and that it informs the CAA about the resources available to it and its compliance with certain conditions of this Licence;
 - (b) limit the scope of activities which the Licensee undertakes which are outside the En route (UK) Business and the En route (Oceanic) Business;
 - (c) create an effective financial ring-fence around the En route (UK) Business and the En route (Oceanic) Business and promote transparency;
 - (d) require the Licensee to make the CAA aware of any material steps proposed to be taken under the Finance Documents;
 - (e) require the Licensee to notify the CAA on the occurrence of certain events which might prejudice the Licensees' financial stability;
 - (f) control the disposal of relevant assets, and place certain restrictions on the ability of the Licensee to incur debt;
 - (g) require the ultimate holding company to undertake not to act, or cause any subsidiary to act, in such a way as to cause the Licensee to breach the Licence;
 - (h) prohibit the Licensee from entering into any agreement or arrangement with any affiliate or related undertaking except on an arm's length basis and on normal commercial terms unless otherwise permitted;
 - (i) require the Licensee to use all reasonable endeavours to maintain at all times an investment grade issuer credit rating; and
 - (j) establish a financial gearing target and cap.

This paragraph 1 provides a descriptive summary of the provisions which follow in this Condition. This paragraph 1 is not part of the Condition nor is it intended to add to the provisions which follow, and, for the purposes of interpretation, it is the detailed provisions which prevail.

Availability of Resources

2. The Licensee shall at all times act in a manner calculated to secure that it has available to it sufficient resources including (without limitation) financial, management and staff resources, fixed and moveable assets, rights, licences, consents and facilities, on such terms and with all such rights as shall ensure that at all times~~to enable it to~~ able it to:
- (a) carry out its Permitted Purpose activities; and
- (b) comply in all respects with its obligations under the Act and this Licence including, without limitation, its duties under section 8 of the Act.

Compliance Certificates in relation to financial resources

3. ~~With effect from 1 April 2016, the~~ The Licensee shall submit a Compliance Certificate ~~certificate addressed to the CAA, approved by a resolution of the board of directors of the Licensee and signed by a director of the Licensee pursuant to that resolution. Such certificate shall be submitted within four months of the end of the Licensee's financial year. Each certificate shall be~~ in one of the following forms:

(a) Certificate 1F

"After making enquiries based on systems and processes established by the Licensee appropriate to the purpose, the directors of the Licensee have a reasonable expectation that the Licensee will have available to it self, after taking into account in particular (but without limitation) any dividend or other distribution which might reasonably be expected to be declared or paid by the Licensee, any amounts of principal and interest due under any loan facilities and any actual or contingent risks which could reasonably be material to their consideration, sufficient financial resources and other resources and financial and operational facilities to enable the Licensee to carry on the Permitted Purpose activities and to comply with its obligations under the Act and under this~~its~~ Licence to which the Licensee is aware or could reasonably be expected to make itself aware it is or will be subject (as amended from time to time) for a period of two years from the date of this certificate."

or

(b) Certificate 2F

"After making enquiries based on systems and processes established by the Licensee appropriate to the purpose, the directors of the Licensee have a reasonable expectation, subject to what is said below, that the Licensee will have available to it self, after taking into account in particular (but without limitation) any dividend or other distribution which might reasonably be expected to be declared or paid by the Licensee, any

amounts of principal and interest due under any loan facilities, and any actual or contingent risks which could reasonably be material to their consideration, sufficient financial ~~and other~~ resources and financial ~~and operational~~ facilities to enable the Licensee to carry on the Permitted Purpose activities and to comply with its obligations under the Act and under ~~this~~its Licence ~~to which the Licensee is aware or could reasonably be expected to make itself aware it is or will be subject~~(as amended from time to time) for a period of two years from the date of this certificate. However, they would like to draw attention to the following factors which may cast doubt on the ability of the Licensee to carry on the Permitted Purpose activities and to comply with its obligations under the Act and under such Licence for that period.....”

or

(c) Certificate 3F

“In the opinion of the directors of the Licensee, the Licensee will not have available to it~~self~~ sufficient financial ~~or other~~ resources and financial ~~and operational~~ facilities to enable the Licensee to carry on the Permitted Purpose activities and to comply with its obligations under the Act and under ~~this~~its Licence ~~to which the Licensee is aware or could reasonably be expected to make itself aware it is or will be subject~~(as amended from time to time) for a period of two years from the date of this certificate.”

4. ~~[Paragraph deleted]~~The Licensee shall ensure that the Compliance Certificate given to the CAA under paragraph 3 is accompanied by a statement of the main factors that the Licensee’s directors have taken into account in giving that certificate including reference to:
- (a) the systems and processes established by the Licensee to support the giving of the certificate by the directors;
 - (b) the main financial resources and financial facilities available to the Licensee; and
 - (c) the most recent management projected cash flows of the Licensee together with a report prepared by its Auditors stating whether or not the Auditors are aware of any inconsistencies between, on the one hand, that certificate and the statement submitted with it and, on the other hand, any information which they obtained during their audit of the relevant year end accounts of the Licensee.
5. ~~The Licensee shall inform the CAA in writing as soon as practicable if the directors of the Licensee become aware of any circumstance which causes them no longer to have the reasonable expectation expressed in the then most recent certificate given under paragraph 3(a) or 3(b).~~

Compliance Certificate in relation to operational resources

6. ~~The Licensee shall obtain and submit to the CAA with each certificate provided for in paragraph 3 a report prepared by its Auditors stating whether or not the Auditors are aware of any inconsistencies between, on~~

~~the one hand, that certificate and the statement submitted with it and, on the other hand, any information which they obtained during their audit of the relevant year end accounts of the Licensee~~

5. With effect from 1 April 2016, the Licensee shall submit a Compliance Certificate to the CAA within four months of the end of the Licensee's financial year in one of the following forms:

(a) **Certificate 1R**

"After making enquiries, the Licensee's directors have a reasonable expectation that the Licensee will have sufficient operational resources available to itself, including management, personnel, fixed and moveable assets, rights, licences, consents, and facilities to enable the Licensee to carry on the Permitted Purpose activities and to comply with its obligations under the Act and under this Licence (as amended from time to time) for a period of two years from the date of this certificate."

or

(b) **Certificate 2R**

"After making enquiries, the Licensee's directors have a reasonable expectation, subject to what is explained below, that the Licensee will have sufficient operational resources available to itself, including management, personnel, fixed and moveable assets, rights, licences, consents, and facilities to enable the Licensee to carry on the Permitted Purpose activities and to comply with its obligations under the Act and under this Licence (as amended from time to time) for a period of two years from the date of this certificate."

However, the directors of the Licensee would like to draw attention to the following factors, which may cast doubt on the Licensee's ability to carry on the Permitted Purpose activities and to comply with its obligations under the Act and under this Licence [followed by a description of the factors concerned]."

or

(c) **Certificate 3R**

"In the opinion of the Licensee's directors, the Licensee will not have available to itself sufficient operational resources including management, personnel, fixed and moveable assets, rights, licences, consents, and facilities to enable the Licensee to carry on the Permitted Purpose activities and to comply with its obligations under the Act and under this Licence (as amended from time to time) for a period of two years from the date of this certificate."

6. ~~[Paragraph deleted]~~ The Licensee shall ensure that the Compliance Certificate given to the CAA under paragraph 5 is accompanied by a statement of the systems and processes established by the Licensee to support the giving of the certificate by the directors and the main factors

that the Licensee's directors have taken into account in giving that certificate.

Compliance Certificate in relation to certain Conditions

7. With effect from 1 April 2016, the Licensee shall submit a Compliance Certificate to the CAA within four months of the end of the Licensee's financial year in one of the following forms:

(a) Certificate 1C

"After making enquiries, the Licensee's directors consider that, at the time of their approval of this certificate, the Licensee is in compliance in all material respects with all of the obligations imposed on it by Condition 17 (Provision of information to the CAA for regulatory purposes), Condition 5 (Availability of resources and Financial Ring Fencing) and Condition 9 (Prohibition of cross-subsidies)."

or

(b) Certificate 2C

"In the opinion of the Licensee's directors, the Licensee is not at the time of their approval of this certificate in compliance in all material respects with all of the obligations imposed on it by Condition 17 (Provision of information to the CAA for regulatory purposes), Condition 5 (Availability of resources and Financial Ring Fencing) and Condition 9 (Prohibition of cross-subsidies) [followed by a description of the way in which the Licensee is not complying]."

8. The Licensee shall inform the CAA in writing as soon as reasonably practicable if:

- (a) the directors of the Licensee become aware of any circumstance that causes them no longer to have the reasonable expectations expressed in the most recent certificate given under paragraph 3(a), 3(b), 5(a) or 5(b); or
- (b) the directors of the Licensee consider that any adverse factors that caused them to give the CAA a Compliance Certificate in the form of under paragraph 3(b), 3(c), 5(b) or 5(c) and referred to in that certificate have materially worsened.

Certificates for the CAA in relation to dividends

- 8A. Subject to paragraph 8D, the directors of the Licensee shall not declare or recommend a dividend, and the Licensee shall not make any other form of distribution within the meaning of sections 829, 830, 849 and 850 of the Companies Act 2006, or redeem or repurchase any share capital of the Licensee, unless before declaring, recommending, or making the distribution, redemption, or repurchase (as the case may be) the

Licensee has given the CAA a Compliance Certificate that complies in all respects with the two requirements set out in paragraphs 8B and 8C.

8B. The first requirement is that the Compliance Certificate shall be in the following form:

“After making enquiries, the directors of the Licensee are satisfied:

(a) that, at the time of their approval of this certificate, the Licensee is in compliance in all material respects with all of the obligations imposed on it by Condition 17 (Provision of information to the CAA for regulatory purposes), Condition 5 (Availability of resources and Financial Ring Fencing) and Condition 9 (Prohibition of cross-subsidies);

and

(b) that the making of a distribution, redemption, or repurchase of [value] on [date] will not, either alone or when taken together with other circumstances reasonably foreseeable at the date of this certificate, cause the Licensee to be in breach to a material extent of any of those obligations in the future.”

8C. The second requirement is that the Compliance Certificate shall have been approved by the Licensee’s board of directors not more than 14 days before the date on which the declaration, recommendation, or payment is to be made.

8D. The Licensee need not give the CAA a Compliance Certificate of the type required by paragraph 8A in circumstances where:

(a) during the six months preceding the declaration or recommendation of a dividend, the making of any other form of distribution or the redemption or repurchase of share capital, it has given the CAA a Compliance Certificate in the form of Certificate 1C under the requirement set out in paragraph 7 of this Condition; and

(b) that certificate includes an appropriate addendum using the wording given at paragraph 8B(b) of this Condition.

8E. Where the Compliance Certificate given under paragraph 8A, or relied upon under paragraph 8D, relates to the declaration or recommendation of a dividend, the Licensee is under no obligation to issue a further Compliance Certificate before paying that dividend so long as such payment is made within six months of the date on which the Compliance Certificate was given.

Condition 7: Requirement to maintain an intervention plan [Currently “[NOT USED]”]

1. The Licensee shall prepare by 1 April 2016, or within 6 months of this condition coming into effect in this Licence, whichever is the later and, thereafter, maintain an intervention plan fulfilling the criteria set out in paragraph 3.
2. The requirement for the information described in paragraph 3 will be satisfied if the plan provides details of other documents or records (including electronic records) where that information can readily be obtained and those documents or records are either maintained by the Licensee itself or are available to the Licensee at all times under a legal or contractual right.
3. For the purposes of this condition, an intervention plan shall be a document or set of documents (which may be in a suitably secure electronic format) containing information that would be sufficient to allow any person appointed under an air traffic administration order (within the meaning in Chapter I of the Act) in respect of the Licensee readily to obtain the information they could reasonably be expected to require in order for that person efficiently to carry out his functions and to remain compliant with the Act and this Licence. The form of the intervention plan shall, as a minimum, contain information on:
 - (a) the financial assets, resources and facilities of the Licensee;
 - (b) the non-financial assets, rights and resources of the Licensee, including information on key management and operational personnel and information technology systems;
 - (c) the liabilities of the Licensee, including contingent and contractual liabilities with counterparty and maturity information;
 - (d) the tax affairs of the Licensee;
 - (e) the personnel of the Licensee and any personnel employed by any affiliate or related undertaking of the Licensee who are engaged in operating any aspect of the Permitted Purpose activities of the Licensee;
 - (f) any pension schemes of which those personnel referred to in subparagraph (e) are members and which are sponsored or administered by the Licensee or any affiliate or related company of the Licensee;
 - (g) any mortgages, charges, or other forms of security over the Licensee's assets; the systems and processes by which the Licensee carries on the En route Businesses with information on any

significant contractual arrangements, including those that impose obligations on the Licensee;

- (h) any arrangements under which the Licensee has delegated any part of the En route Businesses to any affiliate of the Licensee;
 - (i) any contractual rights to receive cash or other financial assets from any affiliate of the Licensee or any other person;
 - (j) any contractual obligations to deliver cash or other financial assets to any affiliate of the Licensee; and
 - (k) the Licensee's arrangements and procedures for ensuring compliance with legislative requirements relating to the provision of air traffic services and with its obligations under this Licence, including the conditions set out in Part III of this Licence.
4. The form, scope and level of detail of the intervention plan prepared in accordance with paragraph 1 shall be approved by the CAA (such approval not to be unreasonably withheld or delayed).
5. The Licensee shall keep the intervention plan under review at all times and, at least annually, shall review the appropriateness of the intervention plan and submit to the CAA a Compliance Certificate within four months of the end of the Licensee's financial year in the following form:

"The Licensee has reviewed its intervention plan as required by condition 7 of its Licence. In the opinion of the directors of the Licensee, the intervention plan is fit for purpose and complies with the Licensee's obligations under that condition."

Condition 8: Requirement for mandated independent directors and corporate governance [Currently “[NOT USED]”]

1. Where potential conflicts exist between the interests of the Licensee and those of any affiliates or related undertakings of the Licensee, the directors of the Licensee, in discharging their responsibilities as directors of the Licensee shall act independently of the interests of any affiliate or related undertaking of the Licensee and ensure that they have regard exclusively to the interests of the Licensee.
2. Subject to paragraph 13, the Licensee shall ensure that at all times after a date which is 12 months after this condition comes into effect, it has at least two non-executive directors who meet the criteria set out in paragraphs 3, 4 and 5. In this condition such directors are referred to as “mandated independent directors”.
3. A mandated independent director shall:
 - (a) be a natural person;
 - (b) in the reasonable opinion of the Licensee, have the skills, knowledge, experience, and personal qualities necessary to perform effectively as a non-executive director of the Licensee and participate fully in the decision making of the board of directors of the Licensee;
 - (c) not have any executive duties within the Licensee’s business; and
 - (d) be of sufficient standing to ensure that directors of the Licensee, in discharging their responsibilities as directors of the Licensee, act independently of the interests of any affiliate or related undertaking of the Licensee and ensure that they have regard exclusively to the interests of the Licensee.
4. A mandated independent director shall not be, and shall not have been during the 12 months before his appointment as a director of the Licensee or the coming into force of this condition (whichever is the later):
 - (a) an employee of the Licensee; or
 - (b) a director or employee of an associate of the Licensee.
5. A mandated independent director shall not:
 - (a) have, or have had during the 12 months before his appointment as a director or the coming into force of this condition (whichever is the later), any material business relationship with the Licensee or any associate of the Licensee;
 - (b) hold a remit to represent the interests of any particular shareholder or group of shareholders of the Licensee or the interests of any associate or the interests of any particular shareholder or group of shareholders of any associate of the Licensee; or
 - (c) receive remuneration from the Licensee or any associate of the Licensee apart from a director’s fee and reasonable expenses.

6. For the purposes of sub-paragraphs 5(a) and 5(c) respectively:
 - (a) the holding of a small number of shares or associated rights in the Licensee or any associate of the Licensee shall not, of itself, be considered a material business relationship; and
 - (b) the receipt or retention of any benefit accrued as a result of prior employment by or service with the Licensee or any associate of the Licensee shall not be considered to be remuneration.
7. The Licensee shall notify the CAA of the names of its mandated independent directors appointed pursuant to paragraph 2 within 14 days of the date on which they are appointed.
8. The terms of appointment of each mandated independent director shall include a condition stipulating that both the Licensee and the appointee will use their best endeavours to ensure that the appointee remains independent during his term of office, having particular regard to the criteria set out in paragraphs 3, 4 and 5.
9. A term of appointment for a mandated independent director may not be for longer than eight years, but an individual may be reappointed thereafter provided that he continues to meet the criteria set out in paragraphs 3, 4 and 5.
10. The Licensee shall notify the CAA in writing within 14 days if any mandated independent director is removed from office or resigns, giving reasons for the removal or (to the extent that they are known to the Licensee) the resignation. For the purposes of this requirement, the reasons for a resignation may, if applicable, be stated to be personal reasons.
11. If at any time the Licensee has fewer than two mandated independent directors because of a removal or resignation or other reason (including death or incapacity), the Licensee shall use reasonable endeavours to ensure that a new director is, or new directors are, appointed to fulfil the obligation in paragraph 2 as soon as is reasonably practicable to bring the number of mandated independent directors up to at least two.
12. Where mandated independent directors have been appointed to fulfil the obligation in paragraph 2, the Licensee shall ensure that (save where necessary to meet urgent safety or operational matters of the Licensee) meetings of its board of directors are:
 - (a) quorate only if attended by at least one of those mandated independent directors; and
 - (b) clearly distinct, and held at a separate time, from any meeting of the board of directors of any associate of the Licensee.
13. Paragraph 2 shall not have effect where and to the extent that the CAA consents otherwise. The CAA may grant such consent where it considers that the corporate governance arrangements applicable to the Licensee provide equivalent assurance to the CAA in relation to any potential conflicts between the interests of the Licensee and those of any affiliates or related undertakings of the Licensee as if the mandated independent

directors required by paragraph 2 had been appointed. Any consent granted by the CAA pursuant to this condition may be on such terms as the CAA considers appropriate in all the circumstances.

14. Nothing in this condition shall be construed as requiring any director of the Licensee to act in a manner that is not consistent with that director's legal obligations as a director.

Interpretation

15. In this condition:

“associate” means:

- (a) an affiliate or related undertaking of the Licensee;
- (b) an ultimate holding company of the Licensee;
- (c) a participating owner of the Licensee; or
- (d) a common control company;

“common control company” means any company, any of whose ultimate holding companies (applying the definition set out in Condition 1 (Interpretation and construction) but substituting that company for the Licensee) is also an ultimate holding company of the Licensee;

“participating owner”: for the purposes of the definition of “associate”, a person is subject to a participating interest by another person (a “participating owner”) if:

- (a) that other person holds a participating interest in the person; or
- (b) the person is subject to a participating interest by a person who is himself subject to a participating interest by that other person; and
- (c) “participating interest” has the meaning given in section 421A of the Financial Services and Markets Act 2000.

Condition 9: Prohibition of cross-subsidies

1. Without prejudice to the provisions of Article 15(2)(e) of Regulation (EC) No 550/2004 on the provision of air navigation services in the single European sky (the "Service Provision Regulation"), ~~the~~ The Licensee shall procure that no Separate Business or part of a Separate Business gives any cross-subsidy (whether in money or money's worth) to, or receives any cross-subsidy from, any other business or part of any other business of the Licensee or any affiliate or related undertaking of the Licensee (whether or not a Separate Business) ~~where such cross-subsidy has or is intended to have or is likely to have the effect of preventing, restricting or distorting competition in any market for the provision of air traffic services.~~
2. Where, on or after 1 April 2016:
 - (a) the Licensee enters into any new cross subsidy arrangement; or
 - (b) any cross subsidy arrangement which has been entered into prior to 1 April 2016 but which has not been implemented or has not come into effect prior to that date, is implemented or comes into effectand any such arrangement, in the Licensee's opinion, is justified for objective reasons and so would be permitted under the Service Provision Regulation, the Licensee shall submit in writing to the CAA a clear identification and explanation of those objective reasons.
3. Where the CAA is satisfied the Licensee is giving or receiving, or has given or received, any cross-subsidy prohibited by paragraph 1 above or the Service Provision Regulation, the Licensee shall take such steps, set out in any directions that may be issued by the CAA, as are necessary to ensure that it complies with paragraph 1 and the Service Provision Regulation.

Appendix B

NERL consultation response and request for consent to not comply with Condition 8 of the Licence

This appendix sets out the response we received from NERL on our final proposals to modify its licence with respect to governance and ring-fencing. Included in the response was a request from NERL to not comply with certain provisions of new Condition 8 of the Licence.

**PROPOSAL TO MODIFY NATS (EN ROUTE) PLC (NERL) LICENCE IN
RESPECT OF REPORTING OF GOVERNANCE AND RING-FENCING: NOTICE
UNDER SECTION 11(2) OF THE TRANSPORT ACT 2000 (CAP 1368)**

NERL RESPONSE

1. Summary

- 1.1 On 9 February 2016, the CAA published CAP 1368, which invited views on a proposal to modify the NERL Licence in respect of governance and ring-fencing.
- 1.2 This response document confirms NERL's acceptance of the proposed Licence modifications and also contains a formal request for consent from the CAA not to appoint two mandated independent directors (MIDs).

2. Licence modification proposals

- 2.1 NERL understands that the Licence modifications proposed are as follows:
- Separate annual certificates on the availability of financial and operational resources, in both cases accompanied by supporting statements on the processes used and factors considered in issuing the certificates;
 - New annual certificates confirming compliance with specific elements of the ring-fence;
 - New certificates of compliance with the ring-fence conditions before declaring or recommending a dividend;
 - Production and maintenance of an intervention plan to assist a special administrator in the event of insolvency;
 - All non-executive directors of NATS to be appointed to the NERL Board;
 - Where there are potential conflicts between the interests of NERL and those of any other group company, NERL directors must focus exclusively on the interests of NERL; and
 - Two MIDs to be appointed to the NERL Board unless the CAA consents otherwise.

2.2 NERL can confirm that it accepts the proposals listed above. With respect to the final point, NERL considers that it has sufficient arrangements in place that provide equivalent assurance in relation to corporate governance as the appointment of MIDs would provide. Therefore, and as provided in the proposed new Condition 8(13), a formal request for consent from the CAA not to appoint two MIDs is attached in the annex to this document.

Peter Tullett

9 March 2016

**ANNEX - NERL REQUEST FOR CAA CONSENT NOT TO APPOINT TWO
MANDATED INDEPENDENT DIRECTORS (MIDs)**

1. NERL has confirmed its acceptance of the proposed changes to its Licence in CAP 1368.
2. At its January 2016 meeting the NATS Holdings Limited Board resolved that all non-executive directors of NATS Holdings Limited (being the independent Partnership Directors appointed by HM Government and those appointed by Airline Group and LHR Airports) will be appointed to the NERL Board with effect from 1 April 2016.
3. Given the current membership of the NATS Holdings Limited and NERL Boards, all of the existing directors of NATS Holdings Limited will therefore also be members of the NERL Board. These directors, including the Partnership Directors, will therefore bring their responsibilities to be expressly independent directly on to the NERL Board.
4. No executive director who may be appointed to the NATS Holdings Limited Board who is predominantly responsible for operating the NSL business will be a member of the NERL Board. For the avoidance of doubt, no executive director currently holds such responsibility.
5. NERL considers that the governance arrangements in place through the Public Private Partnership (PPP) are sufficient without the need for the appointment of MIDs. The Partnership Directors appointed by HM Government have special powers not available to MIDs, through access to information concerning all NATS group companies and the power to veto material decisions affecting NERL on a wide range of issues. In contrast, MIDs' only recourse if they objected to such material decisions would be to resign.
6. The en route services operated by NERL account for around 75 per cent of overall NATS Holdings Limited group turnover and therefore the turnover of NATS (Services) Limited does not exceed the 45 per cent threshold proposed by the CAA.
7. On this basis, NERL requests formal consent from the CAA not to appoint two independent non-executive directors, pursuant to paragraph 13 of Condition 8 of the Licence from the date it becomes effective in the Licence. NERL acknowledges that any such consent would be subject to revocation upon any of the following:
 - a. HM Government losing its right to appoint at least two Partnership Directors to the board of NATS Holdings Limited;
 - b. HM Government failing to appoint (or reappoint) at least two Partnership Directors to the board of NATS Holdings Limited; and
 - c. the turnover of NATS (Services) Limited exceeding 45 per cent of the overall NATS Holdings Limited group turnover, each as assessed in and on the date of publication of the relevant Annual Report and Accounts.

Appendix C

CAA consent for NERL to not comply in relation to Condition 8 of the Licence

This appendix sets out our consent for NERL to not comply in relation to certain provisions of the new Condition 8 of the Licence, due to the current governance arrangements at NERL. In granting consent, we also describe the circumstances under which our consent would be terminated.

NATS (En Route) plc (“NERL”)**Consent granted to NERL in relation to Condition 8 of its Air Traffic Services Licence****Introduction: Requirement for NERL to appoint mandated independent directors**

On 28 March 2001, the Secretary of State for Transport granted a licence to NERL under section 6 of the Transport Act 2000 (the Act) authorising it to provide en route air traffic services in the UK (the Licence).

Pursuant to section 2 of the Act, the Civil Aviation Authority (CAA) has a primary duty to maintain a high standard of safety in the provision of air traffic services. Under section 11(1) of the Act, the CAA may modify the conditions of a licence granted under the Act if the licence holder consents to the modifications.

In 2012 and 2013, the CAA carried out an Ad-Hoc review of NATS-related risks which found that the arrangements for NERL’s governance and ring-fencing contained in the Licence may need to be strengthened to ensure that users are adequately protected from risks which arise outside the regulated business of NERL (the Ad-Hoc Review). In the light of the Ad-Hoc review findings, the CAA undertook a thorough review of the ring-fencing conditions in the Licence and on 27 April 2015 published for consultation its initial proposals on modifications to the Licence in respect of Governance and Ring-Fencing (CAP 1287) (the Initial Proposals).

Among other things, the Initial Proposals proposed the introduction of a new condition (condition 8: Requirement for mandated independent directors and corporate governance) into the Licence to require NERL to appoint at least two “mandated independent directors” to its board to ensure the independence of the board’s decisions. This was aimed, in particular, at addressing the potential concerns that may arise as a result of the interrelationship between NERL and NATS Services Limited within NATS Holdings Limited and discussed in more detail in CAP 1287.

Alternative arrangements proposed by NERL

During and following the consultation period in respect of CAP 1287, the CAA and NERL engaged in a number of discussions regarding the CAA’s Initial Proposals.

As part of the discussions between NERL and the CAA in respect of CAP 1287, NERL wrote to the CAA proposing an alternative arrangement to address the CAA's concerns. These proposals were made in the context of the right of HM Government being able to appoint up to three "Partnership Directors" to the board of NATS Holdings Limited as a result of its shareholding and/or contractual rights in respect of NATS Holdings Limited, including, in particular, pursuant to the Partnership Agreement between the Secretary of State for Transport, the Airline Group Limited and BAA plc (as amended).²

NERL's alternative proposal was one under which "*all non-executive directors of NATS Holdings (being both the independent P[artnership] D[irector]s appointed by Government and the user representatives appointed by Airline Group, but with the exception of any executive director with predominantly responsibility for operating the NSL business) would join the NERL Board.*" NERL also proposed a trigger mechanism under which the requirement for NERL to appoint mandated independent directors would be triggered by:

- HM Government losing its right to appoint Partnership Directors to the NATS Holdings Limited board;
- HM Government failing to appoint (or reappoint) a Partnership Director; or
- the turnover of NATS Services Limited exceeding a set proportion of the overall NATS Holdings (group) turnover.

Formal licence modification proposals made by the CAA and NERL's response

On 9 February 2016 the CAA made a formal proposal to introduce a new Condition 8. Taking the alternative proposals made by NERL into account, the new Condition 8 formally proposed by the CAA included a new Paragraph 13 which provided that the requirement to appoint mandated independent directors set out in paragraph 2 of that condition should not have effect where and to the extent that the CAA consents otherwise. The CAA may grant such consent where it considers that the corporate governance arrangements applicable to NERL provide equivalent assurance to the CAA in relation to any potential conflicts between the interests of NERL and those of any affiliates or related undertakings of NERL as if the mandated independent directors required by paragraph 2 of condition 8 had been appointed.

² The directors appointed to the board of NATS Holdings Limited are referred to throughout this letter and consent as "Partnership Directors".

In NERL's letter to the CAA of 9 March 2016, NERL confirmed its acceptance of the proposed changes to the Licence. NERL also confirmed that the January 2016 meeting of the NATS Holdings Limited Board had resolved that all non-executive directors of NATS Holdings Limited (being the independent Partnership Directors appointed by HM Government and those appointed by Airline Group and LHR Airports) would be appointed to the NERL Board with effect from 1 April 2016. Given the current membership of the NATS Holdings Limited and NERL Boards, this would mean that all of the existing directors of NATS Holdings Limited would also be members of the NERL board. These directors, including the Partnership Directors would therefore bring their responsibilities to be expressly independent directly on to the NERL Board. In addition no executive who may be appointed to the NATS Holdings Limited Board who is predominantly responsible for operating the NSL business would be a member of the NERL board. NERL's letter expressly confirmed that no executive director currently held such responsibility.

On this basis, NERL requested formal consent from the CAA pursuant to paragraph 13 of condition 8 of the Licence from the date it became effective in the Licence subject to:

- HM Government losing its right to appoint at least two Partnership Directors to the board of NATS Holdings Limited;
- HM Government failing to appoint (or reappoint) at least two Partnership Directors to the board of NATS Holdings Limited; or
- the turnover of NATS Services Limited exceeding 45 percent of the overall NATS Holdings Limited group turnover, each as assessed in and on the date of publication of the relevant Annual Report and Accounts.

CAA Assessment

Having considered the letter of 9 March 2016 and the issues raised by NERL in its response to CAP 1287, we consider that the appointment of all non-executive directors of NATS Holdings Limited to the NERL board as described above would have important benefits such as encouraging higher standards of corporate governance and increased focus on the activity of the NERL business. As a result, the CAA is satisfied that, if these arrangements are put into place, NERL would have corporate governance arrangements in place that would provide equivalent assurance to the CAA in relation to any potential conflicts between the interests of

NERL and those of any affiliates or related undertakings of NERL as if the mandated independent directors required by paragraph 2 of condition 8 of the Licence had been appointed. For these reasons, the CAA considers that the requirements set out in paragraph 13 of condition 8 of the Licence for the grant of a consent by the CAA are met. The CAA considers that this will be the case for so long as requirements listed below continue to be fulfilled.

Confirmation and Consent

The CAA hereby acknowledges the receipt of NERL's letter of 9 March 2016 and grants consent to the NERL with effect from 1 April 2016 and pursuant to paragraph 13 of condition 8 of the Licence for it not to appoint two mandated independent directors, subject to the following conditions (being, for the purposes of this consent, referred to as "requirements"):

1. all non-executive directors of NATS Holdings Limited from time to time being appointed to, and remaining members of, the board of NERL;
2. HM Government retaining the right to appoint at least two Partnership Directors to the board of NATS Holdings Limited;
3. no director of NATS Holdings Limited with predominant responsibility for operating the business of NATS Services Limited being, at the same time, a director of NERL; and
4. the turnover of NATS Services Limited (and its subsidiaries), as set out in the latest statutory accounts of NATS Holdings Limited from time to time not exceeding 45% of the total turnover of NATS Holdings Limited.

Term and termination of consent

This consent shall continue in force for so long as the requirements listed above are met. Where particular requirements are no longer met, this consent shall terminate in accordance with the following provisions:

- A) this consent shall terminate immediately in the event that either requirement 1 or requirement 2 is not met, save that where the rights of HM Government to appoint Partnership Directors referred to in requirement 2 are amended, restated or changed (for whatever reason) so that HM Government has the right to appoint only one Partnership Director to the board of NATS Holdings Limited this consent shall continue to apply, but shall be deemed to amended so NERL is required to comply with the requirements of condition 8 of the

Licence to ensure that the total number of mandated independent directors and Partnership Directors on the board of NERL is at least two;

- B) in the event that HM Government does not exercise the right referred to in requirement 2 to appoint (or reappoint) one or more Partnership Directors to the board of NATS Holdings Limited for a period of 3 months after the departure of a Partnership Director from the board of NATS Holdings Limited (for for whatever reason), this consent will terminate after a period to be directed by the CAA (after consultation with NERL) which allows NERL a reasonable period within which to recruit and appoint mandated independent directors to satisfy the requirements of condition 8 of the Licence. The CAA shall not make any such direction unless it has consulted with HM Government to confirm that it is not intending to exercise its right appoint one or more Partnership Directors to the board of NATS Holdings Limited in order to increase the number of Partnership Directors to a total of two within six months after the departure of a Partnership Director from the board of NATS Holdings Limited; and
- C) in the event that the turnover of NATS Services Limited (and its subsidiaries), as set out in the latest statutory accounts of NATS Holdings Limited from time to time exceeds 45% of the total turnover of NATS Holdings Limited, this consent shall terminate on the date which is 12 months after the end of the financial year to which those statutory accounts relate.

The provisions in this letter shall not be deemed to constitute any derogation from the terms of the Licence but shall constitute consent only pursuant to condition 8 of the Licence.

Richard Moriarty
Director, Consumers and Markets Group
Civil Aviation Authority