

Strategic themes for the review of Heathrow Airport Limited's charges ("H7")

A discussion document

CAP 1383



Published by the Civil Aviation Authority, March 2016

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Contents

Contents	3
Chapter 1	5
Introduction	5
Purpose of this document	5
H7 programme milestones	5
Views are invited on this document	7
Chapter 2	8
Key contexts for the H7 review	8
Interaction with potential new runway capacity	8
Market power assessment	10
The CAA's primary statutory duty	12
Regulatory best practice	12
Chapter 3	14
Overview of Heathrow	14
Passengers' characteristics	14
Passenger growth	15
Airline characteristics	16
Airport charges to airlines	17
Airport investment	18
Chapter 4	20
Strategic themes for H7	20
Empowering consumers and furthering their interests	20
Incentivising the right consumer outcomes	21
Increasing airport operational resilience	22
Promoting cost efficiency and financeability	23

Chapter 5	26
Constructive Engagement	26
Operating principles	26
CE Process	28
Chapter 6	30
H7 Timetable	30
Chapter 7	32
Key questions	32

CHAPTER 1

Introduction

Purpose of this document

- 1.1 The current regulatory controls on the charges and services that Heathrow Airport Limited (HAL) offers to airlines, and ultimately to consumers¹, are due to expire on 31 December 2018. The CAA has now launched a review (called 'H7')² of the appropriate regulatory arrangements that should be put in place after that date.
- 1.2 This discussion document seeks views from all interested parties on the process, strategic themes, and the relevant issues that should shape the CAA's methodology for the H7 review. We have published a number of Technical Appendices to support this discussion document, which are available from the CAA's website.³
- 1.3 Following our consideration of feedback to this discussion document, we intend to publish a Policy Update document in the autumn that sets out our latest thinking on the methodology for the H7 review.

H7 programme milestones

- 1.4 The periodic review of charges and services is a major programme of work. The CAA's decisions have significant implications for the consumers that use Heathrow, HAL, airlines, cargo owners and many other interested parties. It is important that the CAA's decisions are well supported and subject to appropriate consultation.
- 1.5 The CAA's current programme has a number of key milestones following the issue of this document (Figure 1). The broad aim of the process is to begin discussions with interested parties on the framework and strategic

¹ For the sake of simplicity we use the term 'consumers' to mean both present and future passengers and cargo owners.

² 'H7' where the 7 denotes it will be the 7th period for which Heathrow Airport is subject to price control arrangements since it was privatised in 1986.

³ Strategic themes for the review of Heathrow Airport Limited's charges ("H7") – Technical Appendices, CAP 1383A, available from: www.caa.co.uk/CAP1383a

themes that should govern H7 and then move over time to more detailed consideration of specific issues.

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Figure 1: Key milestones for the H7 review

Date	H7 Milestone
March 2016	Publication of strategic themes discussion document
April – June 2016	CAA led workshops with interested parties
Summer 2016	Establishment of H7 Consumer Challenge Forum
Autumn 2016	CAA Policy Update on H7 methodology
January 2017	HAL publishes its draft Business Plan
Jan – June 2017	Constructive Engagement process between HAL and airlines
September 2017	HAL submits revised Business Plan to the CAA
December 2017	CAA Initial Proposals
June 2018	CAA Final Proposals
1 January 2019	New regulatory arrangements come into effect the day after the present controls are due to expire

Views are invited on this document

- 1.6 If you have any views on this discussion document, and in particular on the key questions set out in chapter 7, please email them to economicregulation@caa.co.uk by **no later than noon on Friday 29 April 2016**. We cannot commit to take into account representations after this date.
- 1.7 If you would like to discuss the issues raised in this document before the deadline please contact Stephen Gifford (stephen.gifford@caa.co.uk) or Rob Toal (robert.toal@caa.co.uk).
- 1.8 Representations will be made available on the CAA's website. Any material considered confidential should be clearly marked as such. Please note that we have powers and duties with respect to disclosure of information under Section 59 of the Civil Aviation Act 2012 (the Act) and the Freedom of Information Act 2000.

Chapter 2

Key contexts for the H7 review

Interaction with potential new runway capacity⁴

- 2.1 The CAA has argued for some time that given present and likely future capacity constraints, without building another runway in the South East of England, consumers will suffer from higher prices, reduced choice and lower service quality.
- 2.2 The H7 review takes place against the backdrop of the Government developing its response to the work of the Airports Commission (the Commission) on new runway capacity in the South East of England.
- 2.3 The Commission reported in July 2015 recommending a new northwest runway at Heathrow, alongside a significant package of measures to address its environmental and community impacts. Since July 2015, the Government has been reviewing the work of the Commission and confirmed in December 2015 that:
- it agrees with the Commission that the South East needs more runway capacity by 2030;
 - it agrees with the Commission's shortlist of three options, all of which it concluded were viable; and
 - the location decision for new runway capacity is subject to further consideration on environmental impacts and the best possible mitigation measures. The Government indicated that the package of further work is expected to conclude over the summer 2016.
- 2.4 The CAA acknowledges that the H7 review will need to proceed, at least for a number of months, with a degree of uncertainty given the Government has not made a decision on the location of new runway capacity.
- 2.5 The CAA has designed the process for the H7 review to accommodate work on the regulation of new runway capacity. The CAA published in February 2016 a Policy Update on the regulatory treatment of the planning

⁴ See [Technical Appendix 4](#) for further background.

costs associated with new runway capacity.⁵ Assuming the Government makes a decision on location over the summer of 2016, the CAA presently intends to publish a decision on its approach to planning costs in the autumn of 2016, alongside a broader consultation on the regulatory framework for construction costs associated with new runway capacity. At the same time, the CAA expects to publish its Policy Update on its H7 methodology to ensure there is alignment between H7 and policy on new runway capacity. Given its financial and operational significance, a decision on a new runway may necessitate some changes to the emerging views on H7 contained in this document.

2.6 Despite the current uncertainty over new runway capacity, the CAA considers that it is important that all interested parties engage with it at an early stage on the appropriate methodology for H7 because:

- there are some strategic themes and priorities for the H7 review that may not change or be significantly altered by the Government's decision on new runway capacity;
- there is likely to be a significant period of time where regulation will be required between 31 December 2018, when the current regulatory controls on HAL's charges and services are due to expire, and the earliest date from which any new runway capacity becomes operational (not expected until at least 2025 if the Government adopts the Commission's recommended Heathrow option); and
- interested parties may have their own views on how the CAA best accommodates uncertainty over new runway capacity within its H7 programme.

2.7 We will keep our H7 process under review pending decisions by the Government on new runway capacity. If it proves necessary we can consult with interested parties with a view to extending the current regulatory settlement.⁶

⁵ Recovery of costs associated with obtaining planning permission for new runway capacity: policy update, CAP 1372, available from: www.caa.co.uk/CAP1372

⁶ Note that the CAA has the power under the Act to propose an extension to the current regulatory arrangements.

Market power assessment⁷

- 2.8 The Act requires the CAA to regulate an airport operator if we have made a determination that that operator has met the Market Power Test (MPT) in relation to an airport. The MPT has three limbs:
- Test A – the relevant operator has, or is likely to acquire, substantial market power (SMP) in a market.
 - Test B – competition law does not provide sufficient protection against the risk that the relevant operator may engage in conduct that amounts to an abuse of that SMP.
 - Test C – the benefits of regulating the relevant operator are likely to outweigh the adverse effects.
- 2.9 In 2014 we published a Market Power Determination (MPD), which concluded that HAL had met the MPT in relation to Heathrow Airport (see Box 1 overleaf).

⁷ See [Technical Appendix 2](#) for further background.