

JSB members

[shared via email]

19 April 2024

CAA consultation on H7 Final Issues (CAP2980): Other Outstanding Issues

Dear JSB colleagues,

I am writing to you regarding Heathrow Airport's response to the Civil Aviation Authority's (CAA) consultation on 'H7 Final Issues' (CAP2980).

In the spirit of transparency and collaboration as we work together to improve the delivery and implementation of price controls, this letter is to inform you that, in addition to the issues included by the CAA in CAP2980, we have identified three other outstanding elements connected to the H7 Final Decision that we believe require addressing (as further detailed below).

Heathrow is seeking resolve all H7 pending matters under CAP2980 and considering that these elements will require adjustments to our licence, we wanted to ensure you and the airline community had both the background to them and enough time to consider and respond to them as part of this process.

Please do not hesitate to contact us should you have questions or wish to discuss these issues in further detail.

Yours sincerely,

Mike King

Director of Regulation and Economics

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Background and Heathrow Position - other H7 outstanding issues:

1. Queuing times for vehicles (security):

Starting in 2017, Heathrow and the Airline Community have engaged extensively on the definition of the service quality framework for H7, including discussions on performance targets for vehicles queuing times in control posts.

As a result of this long engagement, Heathrow and the Airline Community have agreed that moving the target to a per-vehicle measure was likely to be the best way forward for H7. Heathrow and the Airline Community have also agreed on retaining the Q6 methodology for measuring the performance concerning this indicator. This is, by measuring the average percentage of vehicles at each control post group which have a waiting time of less than 15 minutes in every 15-minutes period (i.e., retaining the Q6 '15-minute time slice methodology', also consistent with other performance targets in the framework).

While Heathrow and Airline Community have communicated this agreement to the CAA (update provided by email in August 2021), such measurement methodology is not reflected in Heathrow's economic licence effective May 2023 (Licence). The actual wording used in the Licence is ambiguous as it refers to the '*Percentage of vehicles at each control post group which have a waiting time of less than 15 minutes*'. There is a risk that this may be incorrectly interpreted as the average across the month as opposed to every 15-minute period, which is not the intent of the measure.

We raised this inconsistency with the CAA in March 2024. The CAA has confirmed the metric is based on the average wait time every 15-minute period rather than the average across the month. Accordingly, Heathrow's response to CAP2980 will address this issue and propose the Licence (both paragraph 3.20 and item F8 of Table 2, in Schedule 1) is amended to include the following wording, which is consistent with other Licence measures:

*'Percentage of vehicles at each control post group **measured once every 15 minutes** which have a waiting time of less than 15 minutes.'*

2. Application of the Terminal Drop-off Charge (TDOC) recovery mechanism:

The H7 settlement related to the TDOC (Table C.5 in Heathrow's Licence) is clear. The differential between the total TDOC revenue forecast by the CAA and Heathrow's actuals/forecast TDOC revenue is subject to a risk sharing factor, with 65% of any profit or loss being shared with the airline community through the aeronautical charges. The policy takes effect from the regulatory year 2022.

However, the Licence implementation only starts from 2024 and does not include a mechanism for addressing differences in 2022 and 2023. This creates an inconsistency between the policy set in H7 Final Decision and the Licence that implements it, as there is no formal mechanism to recover this through the charging process.

In addition, the formula to calculate the yearly TDOC amounts as set in the Licence considers 2020 prices as a baseline (as per CAA's Final Decision) but does not include a respective mechanism for inflation adjustment.

To resolve these issues, we propose that (i) the equivalent of the amounts for 2022 and 2023 should be included in the K factor calculation for 2024 and (ii) to clarify that the calculation of the TDOC needs to consider the necessary adjustment by CPI. We will recommend to the CAA to amend Table C.5 in the Licence as below:

Table C.5: Calculation of the Terminal drop-off charge

For TDOC in Regulatory Year	Adjustment for revenue requirement in Regulatory Year (t)		
	2024	2025	2026
2022	$L_t \times (OTDO_{2022} - FTDO_{2022}) \times (1 + CPI_{2022} + CPI_{2023})$	0	0
2023	$L_t \times (OTDO_{2023} - FTDO_{2023}) \times (1 + CPI_{2023})$	0	0
2024	$L_t \times (OTDO_{2024} - FTDO_{2024})$	0	0
2025	0	$L_t \times (OTDO_{2025} - FTDO_{2025})$	0
2026	0	0	$L_t \times (OTDO_{2026} - FTDO_{2026})$
TDO_t	Sum Rows	Sum Rows	Sum Rows

where:

- (a) $L_t = -1.00$ if a change to legislation comes into force in Regulatory Year t that prevents the Licensee from recovering the full amount of the Forecast, and
 $L_t = -0.65$ otherwise;
- (b) $OTDO_t$ is the outturn revenue collected by the Licensee from Terminal drop-off charges in Regulatory Year t **uplifted by CPI inflation from the CAA price base (2020) to regulatory year t**; and
- (c) $FTDO_t$ is CAA's forecast of the revenue that the Licensee is expected to collect from Terminal drop-off charges in Regulatory Year t, **uplifted by CPI inflation from the CAA price base (2020) to regulatory year t**, and is set out in the CAA's final decision setting the price control applicable to the Licensee for H7.

3. Operational certificate of adequate resources:

Heathrow's Licence contains a specific obligation that requires an annual Certificate of Adequacy of Resources in relation to financial resources (CAR-F) and Certificate of Adequacy of Resources in relation to operational resources (CAR-O) to be produced, approved by a resolution of the Board, and submitted to the CAA by the end of April each year. The CAR-F and CAR-O have historically been a single certificate, but the CAA has now separated this into two certificates as part of the H7 Licence.

Both certificates must be accompanied by a report from Heathrow's statutory auditors, which states whether the auditors are aware of any inconsistencies between the certificate and any information they obtained during their audit of the year end accounts. While the auditors' report on the CAR-F has not highlighted any inconsistencies, they have set out that they cannot provide a report for the CAR-O certificate. This is due to the CAR-O now being a standalone certificate, and providing an opinion on Heathrow's operational resources and day to day management would lie outside the scope of their audit.

The CAA has been informed of this situation and has accepted that a certificate from PwC would not be possible. As such, they have agreed that they would not take any action as a result of non-provision. In substitute of this, Heathrow has agreed for 2024 to provide further assurance signed by

our Chief Operating Officer and a nominated Board member confirming that we have reviewed the requirement and confirm Heathrow has available sufficient operational resources to provide airport operations in accordance with the Licence for the next two years.

As such the current wording of the Licence needs to be modified. We will propose alternative wording to be included in Condition E2.5 of the Licence to clarify the mechanism agreed with the CAA in 2024:

E2.5. The Licensee shall obtain and submit to the CAA with ~~each-the~~ certificate provided under Condition E2.2 ~~and Condition E2.3~~ a report prepared by its Auditors stating whether or not the Auditors are aware of any inconsistencies between, on the one hand, those certificates and the statement submitted with them and, on the other hand, any information which they obtained during their audit of the relevant year end accounts of the Licensee. In relation to the certificate provided under Condition E2.3, the Licensee will provide assurance by producing a signed declaration from the Chief Operating Officer and a nominated Board member confirming that they have reviewed the Licence requirement, and that the Licensee has available sufficient operational resources to provide airport operations.