

Mr Stewart Carter
Civil Aviation Authority
Westferry Circus
Canary Wharf
London EH14 4HD

By email: economicregulation@caa.co.uk

13 December 2024

Dear Stewart,

**IAG response to the Civil Aviation Authority Draft Method Statement and
Business Plan Guidance for H8 (CAP3044)**

1 Introduction

- 1.1 Thank you for giving us the opportunity to provide our input to the H8 price control review process and the CAA's draft method statement and business plan guidance. As a key stakeholder, we are committed to participating in the overall Constructive Engagement process. However, as stated in section 2 below, while we fully endorse the fact that H8 should deliver fair, efficient, and consumer-focused outcomes to benefit of our passengers, we have significant concerns with the current outcomes of the economic regulation at Heathrow Airport Ltd ("HAL").
- 1.2 We fully endorse the response submitted by British Airways to this same consultation. This response is submitted by the International Airlines Group ("IAG") on behalf of our airlines Aer Lingus, British Airways, Iberia and Vueling which collectively carry some 43 million passengers to and from Heathrow every year, providing a wide choice to consumers and enhancing the UK's air connectivity.

2 Overall context: Commitment to the H8 process and regulatory reform

- 2.1 While we remain fully committed to engaging in the consultation as constructively as possible, we feel it will be remiss, at this early stage, not to reiterate our fundamental concerns with the current economic regulation at HAL. Passengers at Heathrow continue to receive poor value for money with poor consumer outcomes by having to pay the highest airport charges in the world, without the equivalent level of world class service, quality or resilience. We understand and appreciate that this is also a concern for the CAA. We believe that fundamental reforms are needed to the regulatory system for effectively regulating aviation infrastructure in the UK, particularly at the UK's only hub airport, to ensure it significantly improves consumer outcomes and delivers for the UK economy as a whole. Our comments further below are therefore made without prejudice to our underlying reservations about the suitability and appropriateness of the current regulatory model (including as reflected or amplified in H8).

Registered Office

International Consolidated Airlines Group, S.A.
El Caserío, Iberia Zona Industrial nº 2 (La Muñoza)
Camino de La Muñoza s/n, 28042 Madrid, Spain

Registro Mercantil de Madrid,
tomo 27312, folio 11, hoja M-492129
C.I.F. A85845535

UK Branch Registered Address

International Airlines Group
Waterside (HAA2), PO Box 365
Speedbird Way, Harmondsworth,
UB7 0GB, United Kingdom

Registered in England & Wales BR014868

3 Main submission

Impact of publication delays on the overall Constructive Engagement process

- 3.1 We note the ambitious timelines set by the CAA for H8 and remain concerned that the delay in the publication of the H7 Lessons Learnt exercise and draft method statement has had, and will continue to have, an adverse impact on the overall H8 CE process. Specifically, Round 1 kicked off before the method statement was finalised and Round 2 (building blocks consultation), due to start in January 2025, risks a similar approach. The CAA's price control approach for H8 is vital for stakeholders to have the full picture of the various elements and be able to meaningfully engage in this process. We therefore welcome the CAA's stated intention to keep the H8 timetable under review and look forward to an update on its feasibility in early 2025 and any necessary contingency measures.

Clarity on H8 Price Control priorities

- 3.2 We support the CAA's commitment to identifying and clarifying its main priorities for the H8 price control review. We agree with some of the priorities identified, such as HAL's need to optimise infrastructure and provide resilient services, improve environmental performance and manage costs efficiently, however, we do believe the CAA needs to clarify these objectives more clearly to enhance their effectiveness.

Alignment with the CAA's statutory duty hierarchy and focus on affordability

- 3.3 The sequencing of H8 priorities should mirror the priorities of the CAA's statutory duties, consumer protection being the primary focus. In this context, the CAA should include affordability as a key metric and make this a top priority to ensure airport charges are reduced to at the least a reasonable level for the benefit of the consumer, consistent with the CAA's primary duty. This is crucially important given charges at HAL are currently the highest in the world. Specifically, the CAA should:

- ensure cost efficiency by aligning the WACC with the H7 lessons learnt findings;
- address the extortionate size of the RAB at HAL which far exceeds the RAB at any other major European hub and given this drives the majority of the charge;
- ensure that investment projects are prioritised to maintain an affordable capital investment plan that supports resilience, capacity optimisation, and cost reduction while supporting progress towards net-zero targets. This is especially important as HAL embarks on its long-term investment plan, which includes initial phases of the 2R masterplan alongside the continuation of existing active H7 projects.

Risk on financeability

- 3.4 While recognising the CAA has a secondary duty towards HAL's financial resilience, this should not be given disproportionate weight and it must not override the primary focus of protecting the consumer. In this regard, the regulator's duty is not to eliminate all possible risk and to totally insulate HAL at the expense of the consumer, but to ensure a business faces the same challenges as if were operating in a competitive market. Regulatory incentives must strike a fair balance to avoid over-rewarding the licensee and to mitigate the risks of regulatory gaming.

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Concerns regarding business plan incentives (BPI)

- 3.5 While we welcome the exploration of a BPI mechanism, we strongly oppose awarding HAL a bonus for simply producing a “high-quality” business plan (BP). Producing a robust BP is a baseline expectation in a regulatory process and should not warrant additional financial rewards, particularly given HAL’s inadequate BP submission during H7. We therefore call for a penalty-only BP incentive instead.

Proportionality of BPI bonuses

- 3.6 The proposed bonus level for a “high-quality” BP is disproportionate, being significantly higher than service-level bonuses for 2025. Additionally, combining quality and ambition metrics risks undermining the incentive’s effectiveness. Quality metrics should be treated separately and subject to a set of minimum requirements which, if not met, would trigger penalties. In the event of a “low-quality” BP, penalties should be automatically triggered.

Stakeholder engagement in BP development

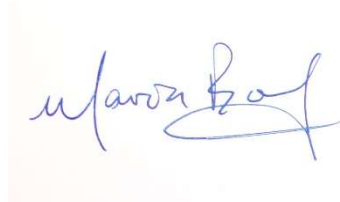
- 3.7 We urge that the assessment of the quality of the BP must include the extent that meaningful stakeholder engagement took place to ensure it reflects stakeholder input and consumer interests. Additionally, there must be full transparency in the information produced, ensuring stakeholders have access to all relevant data and analyses underpinning the business plan.

Conclusion

We recognise the complexity of the H8 process and the challenges involved in balancing consumer, airline, and HAL interests. However, we firmly believe that the priorities we have highlighted and regulatory measures outlined are essential to delivering fair and sustainable outcomes. In particular, we emphasise the need for a sharper focus on affordability, cost efficiency, and a prioritisation of investments that align with consumer interests.

We remain committed to supporting the CAA, notwithstanding our wider position on much needed regulatory reform for HAL, and we look forward to engaging further throughout this process.

Yours sincerely,



Maria Borg
Group Head Airport Regulation
International Airlines Group, S.A.

Registered Office

International Consolidated Airlines Group, S.A.
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