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Proposed modification to the Air Traffic Services Licence of NATS (En Route) PLC

The Civil Aviation Authority ("the CAA") hereby gives notice pursuant to section 11(2) of the Transport Act 2000 of a proposal to make modifications to the air traffic services licence held by NATS (En Route) PLC ("the Licensee"). The modifications are to the following conditions in the licence:

- Condition 2: General obligation to provide Core Services and Specified Services;
- Condition 5: Availability of Resources and Financial Ring-Fencing;
- Condition 6: Regulatory accounting requirements;
- Condition 10: Business Plans, Service and Investment Plans and Periodic Reports;
- Condition 11: Service Standards;
- Condition 15: Secondment of air traffic controllers to the CAA;
- Condition 16: Consultation and complaint handling;
- Condition 17: Provision of information to the CAA for regulatory purposes; and
- Condition 24: Information to be provided to the CAA in connection with the Charge Control Conditions

The CAA has published a document, in the economic regulation section of its website, setting out why it has proposed the modifications, including how it has taken into account representations on earlier consultation on the modifications. (This document is appended to this notice, except for appendices 2 and 3 which are available on the CAA website, at http://www.caa.co.uk/docs/5/ergdocs/natslicencereview_feb07_app2.pdf and http://www.caa.co.uk/docs/5/ergdocs/natslicencereview_feb07_app3.pdf respectively.)

Any comments should be sent, if possible by e-mail, to Susie Talbot at Susie.Talbot@caaerg.org.uk by Friday 30 March 2007. Alternatively, comments may be sent by post to:

Susie Talbot
Economic Regulation Group
CAA
4th Floor
CAA House
45-59 Kingsway
London WC2B 6TE

All responses will be treated as public information and the CAA will place copies on its website soon after the end of the consultation period.

If you have any questions on this document please contact either Paul Taylor on 020 7453 6232 (or, by e-mail, to paul.taylor@caaerg.org.uk) or Rodney Gander on 020 7453 6225 (e-mail to rod.gander@caaerg.org.uk)

Paul Taylor
Licence Manager
1 March 2007

**Review of conditions in the air traffic services licence
held by NATS En Route plc**

**CAA Formal Proposals under section 11(2) of the
Transport Act 2000**

February 2007

**Civil Aviation Authority
CAA House, 45-59 Kingsway, London WC2B 6TE**

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1. Introduction

Purpose of this document

- 1.1 This document invites comments on the CAA's formal proposals to modify conditions in the air traffic services licence held by NATS En Route plc (NERL) following a review of the conditions by the CAA. The review was announced in the CAA's decision of December 2005 on NERL's price controls for 2006-2010.^{1,2} The main purpose of the review has been to consider whether the conditions in NERL's Licence, other than those dealing with price controls, remain fit for purpose and do not impose unnecessary reporting burdens on NERL, and consequently, what modifications to the conditions might be appropriate.

Structure of this document

- 1.2 The document is structured as follows. Chapter 2 sets out the background to the review. Chapter 3 describes the modifications to conditions in the Licence where the CAA's view in its consultation of July 2006 was that modifications should be made, the responses to the July 2006 consultation and sets out the CAA's conclusions. The terms of reference for the review are at Appendix 1. Appendix 2 summarises the modifications the CAA proposes to make to the relevant conditions while Appendix 3 shows the specific modifications it proposes to each of the conditions on which the CAA is now inviting comments.

The review process to date

- 1.3 When it published the terms of reference for the review in December 2005, the CAA invited initial comments on the continuing need for, and the effectiveness of, the existing licence conditions. It allowed until 10 February 2006 for these. NATS was the sole respondent and the CAA published NATS' response on 17 February 2006³ along with an invitation for any comments on NATS' submission by 17 March 2006. Only bmi and British Airways responded with bmi indicating it had no comments to make. British Airways' comments were limited to the specific suggestions that NATS had submitted.⁴ The CAA took into account the comments made by NATS and by British Airways in developing the changes to the Licence proposed in the CAA's consultation paper of July 2006⁵. Only NATS and British Airways responded and the CAA published their responses on 12 October 2006⁶. The comments made by NATS and British Airways have been taken into account in the CAA's formal proposals set out in this document.

¹ The period 2006-2010 is that of the second price control on NERL. It is, therefore called Control Period 2 (CP2).

² "NATS Price Control Review 2006-2010, CAA Decision", CAA, December 2005.

³ Available at http://www.caa.co.uk/docs/5/ergdocs/nats_licencereview.pdf

⁴ Available at http://www.caa.co.uk/docs/5/ergdocs/ba_licencereview.pdf

⁵ "Review of conditions in the air traffic services licence held by NATS En Route plc, Consultation paper", CAA, July 2006

⁶ Available at http://www.caa.co.uk/docs/5/ergdocs/nats_nerlicence_oct06.pdf and http://www.caa.co.uk/docs/5/ergdocs/ba_nerlicence_oct06.pdf.

Views invited

- 1.4 Under section 11(1) of the Transport Act 2000 the CAA may modify the conditions of a licence if its holder consents to the modifications. NERL, as the licence holder, has given its consent to the modified conditions in Appendix 3.
- 1.5 Under section 11(2) of the Transport Act 2000, before making modifications to the Licence the CAA must publish a notice setting out the proposed modifications and state the period (of not less than 28 days) within which representations may be made regarding the proposed modifications. Accordingly, this document constitutes such a notice and the CAA would welcome comments on the proposed modifications. Any comments should be sent, if possible by e-mail, to Susie Talbot at Susie.Talbot@caaerg.org.uk by **Friday 30 March 2007**. Alternatively, comments may be sent by post to:

Susie Talbot
Economic Regulation Group
CAA
4th Floor
CAA House
45-59 Kingsway
London WC2B 6TE

- 1.6 The CAA would expect to make responses available on its website for other interested parties to read as soon as practicable after the period for written comments has expired. Any material that is regarded as confidential should be clearly marked as such.
- 1.7 If you have any questions on this document please contact either Paul Taylor on 020 7453 6232 (or, by e-mail, to paul.taylor@caaerg.org.uk) or Rodney Gander on 020 7453 6225 (e-mail to rod.gander@caaerg.org.uk)

Next steps

- 1.8 The CAA is allowing one month for comments on this document. Subject to the scale and nature of the responses received, the CAA is planning to publish its final decision modifying the conditions in the Licence by the end of April 2007.

2. Background

Introduction

- 2.1 When the CAA published its decision on the NATS price control for CP2 in December 2005 it published the terms of reference for a review of the conditions of the air traffic services Licence held by NERL.⁷ These terms of reference are repeated at **Appendix 1**. The main purpose of the review was to consider whether each of the conditions in NERL's Licence, other than those dealing with price controls, remain fit for purpose and do not impose unnecessary reporting burdens on NERL, and consequently, what modifications to the conditions might be appropriate.
- 2.2 The review has considered:
- whether the conditions are expressed in clear and unambiguous terms. There should be no doubt about the obligations placed on NERL by the conditions and they should be capable of effective and transparent application, monitoring and, where necessary, enforcement by the CAA; and
 - whether the degree of financial monitoring and oversight of NERL by the CAA remains necessary to meet the CAA's statutory objectives. The initial Licence granted by the Government included some conditions designed to ring-fence the regulated business. These were significantly expanded in March 2003 as part of the Composite Solution and reflected in a new consolidated Condition 5.
- 2.3 The CAA has also considered what changes, if any, should be made to Condition 6 of the Licence which sets the requirements for the Regulatory Accounting Guidelines (RAGS). The CAA is not, however, proposing to review the requirement for that part of the RAGS that sets out the mechanism for tracking NERL's Regulatory Asset Base (RAB), which was reviewed as part of the process of setting the price controls for 2006-2010 and set out in Appendix 3 of the December 2005 decision.
- 2.4 There are certain parts of the Licence that the review has been unable to consider. These are not capable of modification as they are expressed as terms rather than conditions. These include:
- NERL's authorisation to provide air traffic services in respect of the Licensed Areas as described in the Licence;
 - the period of the Licence;
 - the period of ten years of NERL's exclusivity to provide core services under the Licence; and

⁷ NATS Price Control Review 2006-2010, CAA Decision, Appendix 4, December 2005

- the circumstances in which the Secretary of State can revoke the Licence.

Equally, the review has not considered NATS Services Ltd (NSL) since NSL is exempt from the requirement to hold a licence, nor can the CAA consider the mechanism for enforcing NERL's Licence as this is governed by the Transport Act 2000.

Review Criteria

2.5 The CAA has reviewed the conditions against its statutory duties found in section 2 of the Transport Act 2000. Subject to an overriding duty to maintain a high standard of safety in the provision of air traffic services, these are:

- a. to further the interests of operators and owners of aircraft, owners and managers of aerodromes, persons travelling in aircraft and persons with rights in property carried in them;
- b. to promote efficiency and economy on the part of licence holders;
- c. to secure that licence holders will not find it unduly difficult to finance activities authorised by their licences;
- d. to take account of the UK's international obligations;
- e. to take account of any Government guidance on environmental objectives;
and
- f. to impose the minimum of restrictions on licence holders consistent with the exercise of the CAA's regulatory functions.

2.6 Subject to its statutory duties, the CAA has also reviewed the conditions against the criteria established by the Better Regulation Commission and its predecessors, namely that regulation should be proportionate, transparent, well targeted and applied consistently and that the regulator should be accountable for its decisions.

3. Review of conditions

- 3.1 The conditions where the CAA is proposing modifications and the reasons for the CAA's proposals are set out below. Further details are provided in **Appendices 2 and 3**. This chapter also discusses the comments made by NATS and British Airways on the CAA's proposals in the July 2006 consultation paper, although in broad terms both organisations were content with the CAA's proposals.

Condition 2: General obligation to provide Core Services and Specified Services

- 3.2 In meeting its obligation to develop and maintain its assets, personnel, systems, and other parts of its business the Licensee is currently under an obligation to have regard to the objective of permitting access to airspace on the part of all users while making the most efficient overall use of airspace. Since NERL has no powers over access to uncontrolled airspace the CAA proposes to modify the Licence to make it clear that NERL's obligation relates to access to controlled airspace alone.
- 3.3 The CAA included this proposal in its July 2006 consultation document and there were no objections to it.

Condition 5: Availability of Resources and Financial Ring-Fencing

- 3.4 The present condition was introduced in 2003 as part of the Composite Solution⁸ whose purpose was to improve the financial robustness of NERL. The CAA has reviewed this condition in the light of subsequent events, including the refinancing of NATS and the completion of the NERL price control review for CP2. The CAA has concluded that Condition 5 should be modified so as substantially to remove the obligation on the Licensee to provide financial information as a matter of routine, noting that the CAA is able to ask the Licensee for relevant information at any time under Condition 17, for example as part of a future price control review process. However, the Licensee should continue to be obliged to alert the CAA to any material change in the Licensee's financial circumstances. The CAA reflected these policy considerations in the July 2006 consultation paper and, subject to the two issues raised by NATS and discussed in paragraphs 3.6 and 3.7 below, they were broadly accepted by those who responded.
- 3.5 British Airways saw scope to reduce unnecessary reporting and consultation with the regulator but considered that the CAA should continue to have sufficient access to NATS data to conduct the quinquennial reviews and to be in a position to intervene to prevent a financial crisis. The CAA believes that NERL's general obligation under Condition 17 of the Licence to provide information to the CAA together with the safeguards being retained in Condition 5 should provide sufficient assurance.

⁸ Following the significant and unanticipated downturn in traffic after 11 September 2001, NATS applied for a number of amendments to the original price controls, including a relaxation of the caps on maximum allowed revenue. Revised caps took effect in January 2003 and revised financial conditions in the Licence took effect in March 2003. The overall package came to be known as the Composite Solution.

- 3.6 NATS invited the CAA to remove the present obligation on it to provide written notice to the CAA when it seeks any consent to a waiver or release of, or cancels, terminates, suspends or surrenders, or seeks any consents under any of, the finance documents (in each case referred to as a "Consent"), unless the Consent is administrative or procedural in nature. NATS pointed to the administrative burden on it of assessing whether or not a particular waiver (of which there are some 15 to 20 each year) falls within the administrative or procedural category. If the obligation were to be retained NATS would wish to see the exclusions broadened to include:
- i. consents in the ordinary course of business; and
 - ii. consents which will not cause a material increase in risk to the Licensee.

In the CAA's view, the general obligation to notify should be retained for the reasons given in the July 2006 consultation paper, namely that it provides a means of providing the CAA with advance warning of a change of circumstances. The CAA does, however, agree with NATS that the present limitation of the exceptions to "administrative and procedural" Consents could be open to uncertain interpretation and thereby imposes an unnecessary administrative burden on NATS in deciding which Consents to notify to the CAA. Some further clarification would therefore be useful. In the CAA's view, NERL should only be required to notify the CAA of those Consents, whether or not in the ordinary course of business, that are likely to cause a material increase in risk to the business. The CAA's formal proposal, therefore, is that NERL would not need to notify the CAA of any Consent which will not cause a material increase in risk to the Licensee.

- 3.7 The current Condition 5 requires NERL to notify the CAA if there is likely to be an increase in its gearing which is either material or likely to continue to have effect for more than six months. NATS proposed that notification should be given only where the increase is material, where it is likely to last more than six months and where it is forecast to occur within the following five years rather than within the lifetime of the financial arrangements. The CAA agrees that the change sought by NATS that it should only notify the CAA if the increase in gearing is both material and is likely to last more than six months is sensible and describes the set of circumstances that is most likely to raise issues of potential concern and where regulatory intervention might be appropriate. It has incorporated this change in its formal proposal. The CAA has also considered NATS' suggestion that it should only notify the CAA where an increase in gearing is expected over the following five years. NATS has explained that five years is the maximum period over which its lenders require it to perform gearing tests and it was difficult to assess what its borrowing requirements would be in future control periods. The CAA does not wish to impose unnecessary administrative burdens on NATS and considers that such a limitation within the context of Condition 5.14(h) would be reasonable given the wider reporting obligations that Condition 5 places on NERL, for example in the event of a major re-financing of the business. The CAA will also be able to consider future gearing levels at subsequent price control reviews. It has therefore included a five year limitation in its formal proposals.

- 3.8 The current Condition 5 also requires the Licensee to consult the CAA in certain circumstances. An important aim of the present review has been to ensure that the purpose and effect of the conditions is clear to all parties. In the CAA's view, the purpose and effect of consultation as expressed in Condition 5 is, in some respects, uncertain. The CAA therefore proposed in its July 2006 consultation to replace, where appropriate, the obligation on the Licensee to consult the CAA with an obligation promptly to notify the CAA if the defined circumstances arise. This would not prevent the CAA, on receipt of the notification, from seeking discussions with the Licensee in those circumstances where it saw a need to do so. There were no objections to this approach and the CAA has therefore adopted it in its formal proposals.

Condition 6: Regulatory accounting requirements

- 3.9 The CAA's view in its July 2006 consultation was that this condition should be aligned more closely with the regulatory determination for CP2, for example by requiring separate reporting of the financial performance of the UKATS and Oceanic businesses rather than on the basis of the "Separate Businesses" as currently defined in the Licence. This would allow NERL's performance to be more easily monitored against the regulatory projections for CP2. At the same time, the published regulatory accounting information should be presented on a single valuation basis in accordance with applicable law and International Financial Reporting Standards (IFRS) as adopted by the EU.
- 3.10 NATS proposed three changes to the CAA's July 2006 proposals. The first was to remove the reference to "and any other business of the Licensee" on the grounds that the CAA's proposed descriptions of the NERL business were already comprehensive. The second was that the CAA and the public should be able to "assess" rather than "monitor" NERL's performance. The third was that allowance should be made for any future changes in EU accounting standards. The CAA sees merit in each of these suggestions and its formal proposals confirm the proposals included in the July 2006 consultation, subject to the three changes suggested by NATS.

Condition 10: Business Plans, Service and Investment Plans and Periodic Reports

- 3.11 For the avoidance of doubt there is no suggestion that the ten year Business Plan or the annual Service and Investment Plan (SIP) that NERL has to produce under the Licence should be discontinued. In its response to the July 2006 consultation, NATS argued that in order to avoid the complexity of overlapping and divergent requirements under the Licence and under Single European Sky for the provision of an annual report of progress against NERL's plans, the Licence should be amended to remove the requirement for an annual business plan report. British Airways wanted business planning information to continue although it thought it would be sensible to combine the annual reporting requirements under the Licence and Single European Sky within a single document. In its July 2006 consultation paper

the CAA indicated that, while not strictly required by the SES legislation, NERL should continue to produce an annual report of progress against the latest SIP. The CAA continues to believe that it is important that users are able to track, on an annual basis, NERL's actual investment against what was planned for in the SIP. The CAA is not, as yet, wholly satisfied that the annual plan that NERL will have to produce to comply with the Single European Sky legislation is expected to include this information. Consequently, the CAA has not adopted NATS' suggestion to remove the obligation in Condition 10 to produce an annual business plan report. However, once NERL is producing annual plans and reports under the Single European Sky legislation the CAA will be ready to consider relaxing the requirements of Condition 10 should it become clear that the relevant information is available separately to users. In due course, it may be possible for a single document to meet the requirements of both the Licence and Single European Sky legislation.

- 3.12 The original condition assumed that NERL's plans and reports would only be available in hard copy. Now that NERL publishes its plans and reports on its website, the CAA proposes to modify the condition to reflect this wider availability as proposed in July 2006. However, NATS argued that it should expect reasonable reimbursement for providing hard copies of documents to those essentially non-direct users of NERL's services who do not have access to NATS' customer website. NATS also wanted the obligation to charge within a limit set by CAA direction to be deleted, accepting that the CAA would seek to intervene were a charge to be considered unreasonable. The CAA agrees that, provided all direct users of NERL's services have ready access to the plans on NATS' customer website, it is not unreasonable for NERL to be able to charge for hard copies if it chooses to do so. The CAA also agrees that it is not consistent with its duty in section 2 of the Transport Act 2000 to impose the minimum restrictions on licence holders for it to direct the maximum level of such a charge, provided this is set at a reasonable amount. The CAA has incorporated the changes suggested by NATS in its formal proposals.

Condition 11: Service Standards

- 3.13 The present condition does not require NERL to consult users on the annual revision to the service standards or to make its regular performance reports available to users. In practice, NERL does both and the CAA proposes to modify the Licence to reflect this position. There were no objections to these changes in the July 2006 consultation paper.
- 3.14 In its July 2006 consultation paper the CAA explained how the position under the Licence is currently unclear where it either delays or withholds its approval of an annual service standards statement, for example pending the submission of further information from NERL. The CAA therefore suggested that the Licence could be modified so that, if such circumstances arise, this should not place NERL in active breach of its Licence, so exposing it to enforcement action under the Transport Act. Instead, the CAA believed that the previous annual statement should remain in

effect until it had approved a subsequent statement. Both NATS and British Airways commented on this. NATS agreed with the principle of the change proposed by the CAA that would prevent NERL being in breach of its Licence were CAA approval not to be forthcoming before the end of the financial year. Its alternative suggestion was that the revised statement would take effect from the first day of the Licensee's financial year following that in which it was submitted to the CAA, notwithstanding that the CAA may not have approved the revised statement by that date. British Airways thought that in relation to service standards the requirement could be changed to one of notification, allowing for CAA intervention if the regulator believed the standards were inadequate or did not take account of the reasonable interests of users. In British Airways' view, the Licence should make it clear whether the standards in the relevant condition were intended to be minimum service standards or targets.

- 3.15 The CAA has considered the alternative approaches suggested by British Airways and NATS for dealing with a revised statement for the following year. While the suggestion made by British Airways could potentially result in the need for less regulatory intervention than under the present arrangements, it would also create a practical difficulty if any intervention by the CAA took place shortly before the new statement was due to take effect. Uncertainty would then remain about NERL's position under the Licence as from 1 April of the year in question. The CAA is proposing therefore to retain the substance of Condition 11(2) but to introduce a further requirement that, following consultation by NERL with users, the revised statement should be submitted to the CAA for approval not less than six weeks before the beginning of the financial year to which it relates. This should allow sufficient time for the CAA to inform NERL of its conclusions and for NERL, where required, to respond. In the event that the CAA had not granted approval before the end of the previous financial year, the revised statement would take effect on 1 April and NERL would not then be in breach of its Licence obligations. This is similar to procedures adopted elsewhere in the Licence, for example in Condition 25.3.
- 3.16 In relation to the nature of the service standards, as the CAA made clear when it first approved the annual statement in 2001, the standards set out in the statement constitute in its view the minimum standards that should be regarded as acceptable. They are, therefore, distinct from the service quality measures that the CAA has adopted in setting the NERL price controls for CP2.

Condition 15: Secondment of air traffic controllers to the CAA

- 3.17 This condition currently requires NERL to make available to the CAA on secondment up to two recently experienced and appropriately qualified air traffic controllers. In its July 2006 consultation the CAA considered that its needs could be satisfied by staff who are not necessarily fully qualified controllers and so proposed to amend this condition to allow for the secondment of any suitably qualified staff. There were no objections to this proposal and the CAA has therefore adopted it in its formal proposals.

Condition 16: Consultation and complaint handling

- 3.18 The present condition is unclear whether NERL's code of practice on consultation and complaint handling is subject to regular review and approval by the CAA. The CAA therefore proposed in its July 2006 consultation that NERL should re-apply to the CAA for approval of the statement every three years. There were no objections to this proposal and the CAA has included it in its formal proposals.

Condition 17: Provision of information to the CAA for regulatory purposes

- 3.19 This condition currently appears to place a limit on the CAA's scope of action to require information from the Licensee rather than set out the obligations of the Licensee. The July 2006 consultation paper proposed that this condition should be modified slightly to confirm that the Licensee is not obliged to provide information to the CAA that could not be obtained under the enforcement provisions of the Transport Act. There would be no change to the substance of the condition. There were no objections to this proposal and the CAA has included it in its formal proposals.

Condition 24: Information to be provided to the CAA in connection with the Charge Control Conditions.

- 3.20 This condition was consulted on and modified as part of the CP2 regulatory settlement in December 2005. However, NERL pointed out earlier in the review that the condition currently requires it to provide the same amount of detail on future proposed charges in both June and November preceding the charging year. Given that the information available in June will be that much more speculative than in November, the CAA proposed in July 2006 that the condition should be further modified so that the information that NERL provides on a provisional basis in June each year can be less detailed than the final information submitted in November. Furthermore, since the charges for London Approach normally take effect in April each year the CAA considered that NERL should not be required to provide information on the following year's London Approach charge before the previous November.
- 3.21 NATS suggested a further change, namely that references to Eurocontrol charges should be to the "average" charge per Chargeable Service Unit for consistency and to enable the possibility of a future multi-tariff charging system. British Airways wanted forecast information, including on the London Approach charge, to be available for consultation with users at a sufficient level of detail and in sufficient time to allow for any issues to be followed up before the charges come into effect.
- 3.22 There was no objection to the proposal that the information provided in June should be less detailed than in November and the CAA has reflected this in its formal proposals. The CAA also agrees with NATS' suggestion to refer to "average" charges and has included this modification. In relation to British Airways' comments

the CAA agrees that relevant information should be made available to users in a timely way. This is, however, a subject more appropriate for the Code of Practice on Consultation developed by NERL under Condition 16 than for Condition 24 which is based on the timing of the submission of information to Eurocontrol.

The specification of services provided by NERL

3.23 One of the purposes of the review was to remove doubts that may exist about the obligations that the Licence places on NERL. NERL's Licence currently does not specify in detail the whole range of services that NERL is expected to provide under the Licence. At various points in the Licence, and in particular for some of the Specified Services, the Licence simply refers to services described in the "Air Pilot" (the UK AIP) as it stood at the date of coming into effect of the Licence (29 July 2001). While this might have been the most suitable way to proceed at the time of PPP⁹ in 2001, during the intervening five years, and partly due to the changes that have taken place over this period, it has become increasingly difficult to identify unambiguously the scope of the services that NERL is required to provide. The CAA therefore considered whether the current Licence review provided a suitable opportunity for a more fundamental re-evaluation of NERL's services so that they could be specified more rigorously in the Licence. It decided against this for two reasons:

- the CAA's published timetable for the review, originally due to be completed by the end of 2006, was unlikely to allow sufficient time for the proper completion of such an exercise; and
- the regulatory settlement for CP2 was recently concluded on the basis of a common understanding of NERL's services and the CAA does not consider these should now be disturbed during CP2.

3.24 As part of the work programme to be conducted during the course of CP2 and designed to help establish the foundations for the CP3¹⁰ review, NERL intends to undertake further work to define more precisely what it is that users want in terms of a service from NERL and the appropriate financial incentives for CP3.¹¹ The CAA has also discussed with NERL a separate exercise, which would be conducted during the early part of CP2 and be designed to review the specification in the Licence of the services NERL would currently be expected to provide under the Licence.

3.25 NERL has pointed to the resource implications both for it and for the CAA of such a wide-ranging exercise. Instead, NERL has suggested that any review should focus on specific issues where there may be differences of view between the CAA and NERL about the scope of the services the latter provides. The CAA is taking these issues up with NERL, with a view to defining an appropriate scope of work.

⁹ NATS has operated as a Private Public Partnership since 2001.

¹⁰ CP3 is the third Control Period, which will run from 2011-2015.

¹¹ *NATS Price Control Review 2006-2010* CAA Decision, December 2005, Appendix 2, paragraph 57, third bullet.

Treatment of bad debts

3.26 NATS has separately raised with the CAA the issue of how bad debts should be measured for the purposes of the price control. The CAA therefore proposes to clarify this by augmenting the CAA's Statement of Regulatory Policy¹² as follows:

'The wording in the price control conditions in the Licence is intended to capture debts which have arisen from 1 January 2006 in respect of Eurocontrol charges and where those debts have been written off. The CAA recognises that waiting until debts have been written off means that some debts may arise in CP2 yet not become bad debts, as defined for the purposes of the price control, until CP3 or later. In these circumstances, the CAA would not expect NATS to be disadvantaged simply because of these timing differences. This is because, as a general rule, the CAA considers it desirable to maintain a consistent approach to regulatory policies across price control periods unless there are good arguments to the contrary. However, this should not prevent the CAA from considering during the next price control review, its approach towards debts that arise in CP3. In addition, to allow for the delay between the date of the debt going overdue and the date of write off, interest at the regulatory cost of capital on the debt should be included in the measure of Relevant Bad Debt.'

3.27 The CAA would welcome comments on this wording.

¹² *NATS Price Control Review 2006-2010* CAA Decision, December 2005, Appendix 2

Appendix 1: Terms of reference for the review of the conditions in NERL's licence

Purpose of review

1. To consider whether each of the conditions in the air traffic services licence held by NATS (En Route) plc (NERL), other than those dealing with price controls which are subject to separate review, remains fit for purpose and does not impose unnecessary reporting burdens on NERL, and consequently, what modifications to the conditions might be appropriate.

Scope of the review

2. The review will consider whether the licence conditions are expressed in clear and unambiguous terms. There should be no doubt about the obligations placed on NERL by the conditions and the conditions should be capable of effective and transparent application, monitoring and, where necessary, enforcement by the CAA.
3. The review will also consider whether the degree of financial monitoring and oversight of NERL by the CAA, supplemented in March 2003 as part of the Composite Solution, remains necessary to meet the CAA's statutory objectives.
4. The review will consider what changes, if any, should be made to the Regulatory Accounting Guidelines (RAGs) produced under condition 6 of the Licence, other than that part of the RAGs that sets out the mechanism for tracking NERL's Regulatory Asset Base (RAB) which is being reviewed as part of the process of setting the price controls for 2006-2010.
5. For the avoidance of doubt, the review cannot address the terms of the Licence set out in Part I of the Licence since these are not open to modification by the CAA. Consequently the review is unable to consider:
 - i. NERL's authorisation to provide air traffic services in respect of the Licensed Areas;
 - ii. the period of the licence; and
 - iii. the period of NERL's exclusivity to provide core services under the Licence.

Equally, the review cannot consider any conditions in relation to NSL since NSL is exempt from the requirement to hold a licence, nor can it consider the mechanism for enforcing NERL's Licence as this is a statutory procedure.

6. While developments in Single European Sky (SES) could, potentially, have a major impact on the Licence, for example in the creation of Functional Airspace Blocks, the extent and timing of this is as yet uncertain. Consequently, this review will not directly consider the impact of EU legislation that implements SES, which the CAA is addressing as a separate exercise. However, the CAA would be reluctant in this review to modify conditions to relax or remove obligations on NERL in areas where,

in order to comply with SES legislation, broadly similar obligations may need to be imposed subsequently on NERL.

Criteria

7. The CAA will review the licence conditions against the statutory objectives of section 2 of the Transport Act 2000. In particular, they will be tested against the CAA's duty to impose the minimum of restrictions on the licence holder subject to the CAA meeting its other statutory objectives.
8. Subject to the CAA's statutory objectives, the licence conditions will also be reviewed against the criteria established by the Better Regulation Task Force, namely that regulation should be proportionate, transparent and well targeted and that the regulator should be accountable for its decisions, and decisions should be consistent.

The Review Process

9. The CAA is publishing the final terms of reference for the review as part of its decision on NERL's price controls for 2006-2010. At the same time it is inviting initial comments on the continuing need for, and the effectiveness of, existing licence conditions. It is allowing until 10 February 2006 for these. The CAA expects to publish the responses and then allow a period of one month for interested party to express views on what others have said.
10. The CAA will then conduct an internal review during Spring 2006, taking into account the various responses, leading to the publication of its initial conclusions in around June 2006 on which it would invite comments. It would expect to allow 12 weeks for these. Once it has considered the responses to the consultation the CAA would expect to publish formal proposals, with modifications to NERL's Licence, during early Autumn 2006. It is planning to publish its final conclusions, with confirmed modifications to the Licence, in late Autumn 2006.
11. Under section 11 of the Transport Act 2000 the CAA may modify conditions with NERL's consent. In the event that NERL did not consent to any of the modifications being proposed by the CAA the CAA would consider whether this raised issues of sufficient importance that warranted it making a reference to the Competition Commission.
12. Once this review of licence conditions has been completed, and any changes implemented, the CAA will consider what changes should then be made to its policies towards the monitoring and enforcement of the Licence. At the same time the CAA would expect to consolidate in one document the following two CAA documents:
 - "Monitoring and Enforcement of the NATS En Route Ltd (NERL) Licence" (published in February 2001) that deals with the CAA's processes for monitoring and enforcement; and

- “The CAA’s Policies towards the Monitoring and Enforcement of the NATS En Route Ltd (NERL) Licence” (published in June 2002) that deals with the CAA’s policies for monitoring and enforcement.