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### **British Airways Response to CAP1967: NATS (En Route) plc licence modifications**

Thank you for the opportunity to respond to your latest consultation on the Economic Regulation of NATS (En Route) plc ("NERL"); we set out our views on the issues raised by you as requested as well as providing further comments on both this consultation and implications for the wider policy environment.

#### **Executive Summary**

British Airways is generally supportive of the proposed amendments to the NERL Licence and the required changes for RP3 following the determination by the Competition and Markets Authority ("CMA"):

- We particularly welcome the enhanced role of the Independent Reviewer of NERL's capital expenditure, along with quarterly updates on NERL's Service and Investment Plans
- In addition, the new capital efficiency incentive proposals appear appropriate. We encourage the CAA to draw on experiences from other regulated businesses both in aviation and other UK regulated sectors to ensure best practice is implemented to create clear efficiency incentives for NERL.
- The proposed engagement incentive appears well-formed and based on practical experience of a framework implements by Ofgem, though project selection criteria and weighting need to be carefully considered to ensure appropriate assessment of value to stakeholders.
- Oceanic conditions should ensure greater clarity over definition of full-operational status of space-based ADS-B), and would benefit from stronger definition of the independent review relating to value for money.

#### **Comments on licence modification provisions**

##### **Condition 10 – Business Plans, Service and Investment Plans and Periodic Reports**



1. We note the “Plan Renewal Date” means 1 January 2015 and every fifth anniversary thereof”, which does not appear to dovetail with the need for a new price review commencing 1 January 2023.

#### Condition 21 – Control of Eurocontrol Service Charges

2. No additional comments.

#### Condition 21a – Control of London Approach Charges

3. No additional comments.

#### Condition 22 – Oceanic Charges

4. Paragraph 8 of this Condition, which relates the determination of whether NERL is fully supplying an ADS-B service seems to lack a certain level of clarity.
  - a. Over what period is the 99% measured: periodic or over the whole duration of the licence?
  - b. Is there any independent assessment of whether the service was being provided, as opposed to NERL self-certification?
  - c. What does “being provided with an ADS-B enabled service” mean? (It should not include any compromised or degraded service level, which does not enable full application of the reduced separation standards ADS-B enables. It should also include the filing of user preferred routes when that capability is delivered.)
  - d. If there is a lack of “regulatory approval” (for instance if ICAO withdrew approval) to use ADS-B then can it really be considered fully available and surely, in such circumstances, NERL should not be entitled to charge for the service?
5. Paragraph 9 of this Condition does not appear to be a particularly strong incentive, as it only requires NERL to commission an independent review of whether the benefits of providing a fully ADS-B based service outweigh the costs of providing the service no later than two years and six months after they have certified they are operating a fully ADS-B based service.
  - a. By when must that report referred to within the condition be delivered?
  - b. Airlines should be consulted prior to any agreement by the CAA to delay the timeframe for delivery of the report.



- c. Can the 'scope, form and level of detail' (at least), if not the full terms of reference for this review not be specified more tightly in the license?
6. We further note that the CMA final decision, in paragraphs 12.34 and 12.35 said:
  - a. The CMA agree with the need for an independent review to be concluded earlier than the end of RP3.
  - b. They were satisfied that further detail on the scope and approach, including the potential outcomes of the independent review would be provided in the near future, and that the CAA would consult on the scope of the review in advance of its implementation.
  - c. They recommended that the CAA, NERL and stakeholders should define more precisely the approach that would be taken, and that there should be a clear understanding of how the review will operate before it starts. Furthermore, it was stated that it was important that airlines will be able to participate by providing reliable information on the flight efficiency changes that have occurred in practice.
7. These points do not appear to be clearly addressed in the proposed changes within CAP1967.

#### New 'Condition 10a – Airspace modernisation

8. We are supportive of the new licence condition in respect of airspace modernisation, with an obligation on NERL to set-up and manage an Airspace Change Organising Group ("ACOG") and develop an airspace change masterplan in support of UK Airspace Modernisation Strategy. This is critical to the future of UK aviation, and airspace modernisation needs to be ready for pre-Covid-19 traffic levels.
9. However, as recognised by the CAA in the guidance notes, we need to ensure that ACOG maintains its independence from NERL, allowing independence and impartiality of ACOG's Steering Committee to continue, and providing the best possible assurance that the masterplan is being delivered.

#### Minor licence modifications to improve clarity

10. No additional comments.

#### **Ex-post efficiency assessment of capital expenditure**



11. We note the CMA's view on the implementation of ex-post efficiency reviews and welcome the CAA's draft policy statement on the topic. We also note that such a consultation is presently ongoing relating to an ex-post assessment of Heathrow's Q6 expenditure, which is also regulated by the CAA (albeit a very different regulated entity).
12. We encourage the CAA to draw on learnings both from the Heathrow experience, where applicable, in implementing ex-post efficiency reviews of NERL, or any other entity that might become regulated by the CAA in the future.
13. Ex-post assessments of capital efficiency in other regulated sectors typically incorporate a used-and-useful test, or some form of assessment of open market asset value to the asset. The DIWE model developed by the Utilities Regulatory in Northern Ireland appears a useful model for application in this context, although the actual definition of efficiency is not specified beyond a dictionary definition, which in the context of capital expenditure leaves it open to interpretation.
14. We particularly welcome the strengthened role of the Independent Reviewer, especially where that will enable airline customers to gain greater visibility and oversight of capital expenditure projects, their progress, and their output.
15. Noting the potential information asymmetries, we agree that the engagement incentive should provide some form of incentive to ensure good governance of capital programmes continues.
16. We stress that delivery of agreed outcomes to the quality expected, on a timely basis and to an agreed cost are all important features to any capital expenditure programme. Timely delivery is as important as cost and quality in project delivery.
17. We also note that any such DIWE assessment may not take place for many years after the commencement of projects. As a result, it is critical to ensure the ex-post framework proposed can make informed assessments based on quality information, as the potential exists for inefficiencies to be hard to identify many years after decisions and processes have been undertaken.

### **Capital Expenditure Engagement incentive**

18. The implementation of the CMA's engagement incentive requirement appears broadly sensible.
19. The proposal to weight the incentive of the project to the level of the capital expenditure might diminish the impact of this incentive on relatively low-capital projects; in considering the capital spend as the baseline, the incentive will be less

effective in disincentivising a lower level of engagement on a capital project with a lower spend but disproportionately high outcome for stakeholders.

20. A relatively low capex project could be expected to deliver a disproportionately high user benefits (e.g. in terms of a financial return on investment, or an improved environmental or safety performance) and the weighting should be amplified to reflect outcomes delivery.
21. However, the assessment criteria do not appear unreasonable, and in broad terms appear to address how the incentive can be best implemented to ensure maximum engagement can be continued by implementing the incentive. We note the CAA may develop this incentive in the future and wish to fully engage in the process at this takes place.
22. The basis of the scoring system, borrowed from Ofgem's ESO framework also appear sensible on initial assessment, however we caution that such a system forms part of a greater whole of RII0-2, and outcomes-based regulatory system that has a fully-defined outcomes basis upon which to mark performance.
23. It appears that the project selection criteria could create future acrimony if not based upon all projects within the capital portfolio, but also recognise significant regulatory burden may result if this encompasses many small projects alongside several larger projects. Implementation should consider best use of time in considering projects, which must be representative of performance throughout the entire portfolio during the price control period.
24. In implementation, we also stress the importance of always taking into account view of stakeholders: the suggestion that this only occurs "where appropriate" is inconsistent with the fact that those stakeholders pay for all expenditure through charges, and it seems inconceivable stakeholders would not have a view on engagement on a particularly project.
25. It would also be useful to clarify whether the reference to RP4 simply means the next period of price control, or the EC regulatory period commencing 2025. To the extent that the quality of the engagement on any capital projects could be assessed in time for the regulatory price control period starting in 2023 it would be good to do that.
26. In paragraph 27 of the consultation, you say "If during the period the value of projects is changed, new projects are added, or projects are discontinued or deferred, it may be appropriate to adjust the weighting of projects in the overall score."
27. We recognise the need for this mechanism to ensure in those cases, where it is felt to be important, that NERL is incentivised on engaging well with stakeholders on why the decision to defer or delay was made, and that there is no perverse incentive on NERL to deliberately descope or delay projects, on which it could be seen that they



were failing to engage well on, in order for them to reduce the weighting on this project and consequently reduce any penalty that they may have faced.

28. We therefore support the adjustment of project weighting in the overall score if it serves to ensure the incentive remains effective in case of capex plan changes.

29. In calculation of the incentive (per illustrative figure 1), it would be useful to clarify the rounding mechanism to ensure absolute clarity in implementation.

Thank you for the opportunity to comment on the proposed changes to the licence.

Yours sincerely,



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