The Civil Aviation Authority (CAA) has published its decisions for price controls for Heathrow and Gatwick airports for the five years from April 1 2008 to March 31 2013 - effectively increasing the maximum charge

by 23.5% or £2.44 ($4.91) at Heathrow Airport to £12.80 ($25.77) per passenger and increasing the charge at Gatwick Airport by £1.18 ($2.37) or 21% to £6.79 ($13.67).

The CAA says its package of price caps and incentives will enable and encourage BAA to deliver genuine service quality improvements and to invest to raise the level of facilities and service that can be delivered to passengers and airlines. ‘The outcome for passengers should be decently modern airports and consistently high service standards,’ said the CAA. These charges over and above the present price caps are hugely important if BAA is to be able to fund its future infrastructure and remain competitive.

The CAA said: ‘At both airports, the difference from the CAA’s November proposals is in the first year increase, which is £0.83 ($1.61) per passenger or 7 percentage points greater at Heathrow and £0.72 ($1.44) per passenger or 12 percentage points greater at Gatwick.

‘The main reasons for the differences since November are (i) additional investment, particularly at Heathrow, the need for which has largely been endorsed by the airlines operating at each airport; and (ii) additional security costs at both airports, but with greater impact at Gatwick, which, in the CAA’s view, are necessary both to reduce queues for passengers and to meet Department for Transport security requirements and the Government’s drive to restore more normal arrangements across the UK for passengers’ hand baggage.

‘Otherwise, these decisions are aligned with the recommendations made by the Competition Commission, updated for subsequent airport-airline agreements, information received since the Commission completed its report, and the final round of consultation on the CAA’s November 2007 proposals.

‘The CAA recognises that the resulting increases in airport charges are significant. However, these higher airport charges are essentially paying for the modernisation of Heathrow and Gatwick, in terms of both facilities and service, for the direct benefit of the passenger. At Heathrow, this entails paying for the full capital and operating costs of Terminal 5 as it comes into service on 27 March 2008, the construction of the Heathrow East Terminal by 2013, and bringing the rest of the airport up to comparable modern standards.

‘At Gatwick, the next quinquennium will see the construction of a major new pier, the redevelopment of the South Terminal check-in area and forecourt access, and a new baggage system. In terms of service, the CAA’s decision provides for shorter security queuing times, enhanced levels of service across the airports (such as more reliable equipment and cleaner terminals), and greater and more immediate information to passengers from BAA (including displayed in the terminals themselves) of how it is performing against the standards it has been set.

‘It is important that airlines and passengers receive the services that they are paying for in airport charges. The CAA therefore confirms its earlier proposals for stronger incentives on each airport in the coming five-year period to deliver higher and consistent service quality and improved infrastructure.’

It says these stronger financial incentives mean that a greater proportion of the investment programme at each airport will be subject to ‘triggers’, under which penalty payments are incurred each month for late delivery of specified outputs from projects. The CAA has decided to set triggers covering over 60% of Heathrow’s and Gatwick’s respective capital programmes for Q5, under which around 5% and 4% respectively of airport charge revenue would be at risk during Q5 in the event that these projects were not delivered on time.
CAA issues London airports price controls

It adds that a broader range of services will be subject to financial incentives, with enhanced targets most notably for passenger security processing, which should deliver a quicker and more reliable experience for passengers – queues less than 5 minutes for 95% of the whole day. The CAA proposes to increase the maximum level of rebates for poor service performance from 3% to 7% of total airport charge revenue – up to around £63m ($126.8m) at Heathrow in 2008/09, and £17m ($34.2m) at Gatwick). The CAA has also introduced bonuses for performance above target, to promote continuous improvement in service beyond the enhanced minimum standards set by the CAA.

These bonuses can be up to two and a quarter per cent of airport charge revenue for passenger service performance above targets, delivered consistently across all terminals – up to around £20m ($40.2m) at Heathrow in 2008/09, and £5m ($10m) at Gatwick).

The CAA has maintained its earlier proposals for the price caps to be based on a pre-tax real weighted average cost of capital of 6.2% at Heathrow and 6.5% at Gatwick as recommended by the Competition Commission. Before doing so, the CAA has analysed recent turbulence in the financial markets, but found that while there had been movement in some individual components of the cost of capital, overall the Competition Commission’s recommendations remained valid.

Commenting on these decisions, which are informed by the recommendations of the Competition Commission and build on agreements reached between the airports and airlines, as well as over two and half years of consultation, Dr Harry Bush, CAA Group Director, Economic Regulation, said: “These decisions build on the enduring themes of the CAA’s previous regulatory proposals in this review. Passengers and airlines deserve better than they have been provided with at Heathrow and Gatwick in recent years. However, the resulting improvements in airport facilities and service standards – some £5bn ($10bn) of investment over the next five years and a halving of security queuing times – have to be paid for in increased charges.

“But airlines and passengers need to be sure that they are getting the enhanced facilities and services that they are paying for. Hence, the CAA’s emphasis on greater financial incentives – with BAA being penalised a lot more if it fails service standards and earning bonuses if it exceeds them – but only if passengers in every terminal benefit.

“The price caps have been carefully based on investment programmes emerging from airport-airline discussions and also on a shared airline-airport desire to improve quality of service, in particular for passengers at security. The CAA hopes that the constructive engagement between airports and airlines that underlies much of this pricing decision will continue in the future to the benefit of their shared customers.”

The CAA’s price control decision documents can be found at:
www.caa.co.uk/docs/5/ergdocs/heathrowgatwickdecision_mar08.pdf