Paul Smith
Consumers and Markets Group
Civil Aviation Authority

Submitted by email to: economicregulation@caa.co.uk

12th December 2022

Aer Lingus response to CAA CAP 2394 'Economic Regulation of NATS (En Route plc) – Initial Proposals for the next Price Control Review ("NR23")

Dear Mr. Smith

Aer Lingus is grateful for the opportunity to respond to this consultation and feed into the CAA's emerging thinking on this subject. We have restricted our response to some of the more important or interesting features that the CAA has requested feedback on. The lack of a response on any item should not be seen as our acceptance of the CAA's proposals.

For the avoidance of doubt Aer Lingus has seen and fully supports the submission of its sister airline, British Airways.

Traffic Forecasts
Using the most accurate and up to date traffic forecasts is an important element in ensuring that NATS is given a price control that is both fair and robust. We support the use of the STATFOR forecasts and appreciate that the CAA has used the latest available forecasts. However, the forecasts do not reflect our experience of passenger demand post-Covid, which has been for strong passenger growth. Consequently, we believe that using the current forecasts could underestimate passenger volumes and lead to an incorrect price. We would urge the CAA to use the latest schedules data from airlines where necessary. The CAA should consider the required calibrated adjustments across building blocks that would be appropriate as a result of adopting a revised traffic forecast.

Pensions
We agree with the CAA's experts (GAD and Steer) that NATS pension fund costs as proposed are not efficient and as a result we support the CAA's recommendations in its Initial Proposals. We support the suggestion that NERL consider introducing a new DC scheme in line with market norms, for new starters as a way of tackling the huge pension cost burden of the current schemes.

Capex
In general, we are broadly supportive of the CAA's proposals for Capex and believe the priority to be for NERL to deliver airspace modernisation and cost efficiently. We also

support the CAA's proposals to strengthen and clarify the Capex management incentive, especially regarding the quality of information supplied.

However, we have several observations on CAA's proposals for Capex in NR23, which revolve around the CAA's proposal to adopt NERL's '2+5' plan for Capex planning:

- We accept that planning a Capex budget 5-6 years out carries with it a risk that priorities and costs may change and consequently are sympathetic to proposals that give both flexibility and certainty (like the core-development process at Heathrow).
- There needs to be an opportunity for the airlines to further understand and develop the mechanisms that would support NERL's proposal to move to a 2+5.
- We believe that the CAA's proposal not to adjust prices to reflect capex profiling could lead to regulatory gaming. On this basis we expect that the CAA will set a price path based on a notional capex profile across the control period. If the actual profile differs and the CAA take no action, then NERL could for example take advantage of having been paid for capex they had not spent in control years 1 to 4 and spend it all in year 5. We would suggest a truing up process that matches prices to actual Capex profile.

It is clear that NERL's proposals for Capex are at a very early stage and will require proper review and scrutiny, so at this stage we cannot comment on whether the values are appropriate. However, it does seem to us that given the nascent stage of the costings that an additional allowance for risk and contingency is unwarranted as is a further £18m for 'emerging opportunities'.

Service Quality
We are broadly supportive of the CAA's proposals in this area, especially with respect to the environmental targets. We also believe that the SQ regime is a 'living' regime and that rather than standards remaining the same over time, like any commercial business, NERL should be required to improve its service offering where its customers, the airlines, require it.

In relation to the SQ regime, our request to CAA is to adopt an approach that has regulatory consistency at its core, both internally (how it treats NERL over time and across the control period) and externally (on common features its approach to HAL and NERL price controls should be the same). Consequently, we suggest that CAA treats the 2022 incentives as it did for 2021.

In terms of internal consistency, we recommend that the CAA revisits its proposals on the capacity targets to ensure that they are consistent with the CAA's decisions on Capex and Opex.

WACC
Aer Lingus has seen and fully supports the points raised by British Airways.

Oceanic
We do not see the need for a TRS mechanism for Oceanic traffic and remain supportive of the need for a cost/benefit review of the introduction of SB ADS-B data charges as well as the development of targets to ensure full value from the technology is permitted.

Other issues

In terms of the possible allowances for asymmetry we agree with the CAA. For NERL to claim that they are subject to asymmetric downside risk is not based on the evidence and there is no case for it to have an adverse shock factor included in the traffic forecasts and/or an asymmetry allowance.

On inflation, we agree with the CAA that these numbers are currently subject to change and that the CAA should use the latest available evidence from a robust reliable source. We are supportive of the CAA taking its CPI and RPI figures from the OBR.

We would welcome the opportunity to engage further with CAA on any of the issues above.

Yours sincerely,

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Marta Drozdz
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