

# Heathrow Airport – Bus and Coach Movement Charge

Provisional Decision Document

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## **Introduction**

Heathrow Airport Limited (HAL) issued a formal consultation document on 18 May 2011 which outlined in detail a proposal to change the bus and coach movement charge at Heathrow Airport. Changes to tariffs have been proposed to allow HAL to recover the costs associated with this activity and to ensure that we move towards a charging system more in accordance with the principle of cost recovery.

HAL developed a new methodology of charging based on infrastructure utilisation which it believes is an equitable and transparent way to allocate costs between activities within the Central Bus Station and Terminal 4 & Terminal 5 operations and facilities. The consultation document was developed and informed by engagement with the coach operators and the nominated trade body dating back to August 2010.

During the consultation period HAL received 4 formal responses to the consultation document. HAL has reviewed all of these responses in detail and those responses have been taken into account in the decision making process. The purpose of this document is to set out HAL's bus and coach movement charge provisional decision following formal consultation and to outline the next steps HAL will take in the implementation of its provisional decision.

## Chapter 1 - Legal Background

- 1.1 The Civil Aviation Authority (CAA) is responsible for the administration of the Airports Act 1986 and is required to set the maximum amount of airport charges that may be levied by HAL during five-year periods, known as quinquennia.
- 1.2 The current quinquennium (known as Q5) runs from 1st April 2008 to 31 March 2014, (including a one year extension).
- 1.3 Within the CAA's economic regulation of HAL and specifically Q5, a number of activities have been classified as Non-regulated aeronautical revenues or "Specified Activities". These include the provision of services for Bus and Coaches. Specified Activities are provided on a cost recovery basis only, no profit is included within the charges for these services.

## Chapter 2 - Review of Responses and Decision

- 2.1 HAL received 3 responses to the consultation document during the specified consultation period. 1 additional response was received soon after the end of the specified consultation period but has been included. All responses received were from coach operators and the nominated representative trade body currently operating at Heathrow, the Confederation of Passenger Transport (CPT). Each response consisted of a covering letter and a joint submission document from all 4 respondents.
- 2.2 Within the respondents' joint submission there are 3 core issues of principle against Heathrow's proposal.
- 2.2.1 "it contradicts the Civil Aviation Authority's (CAA) policy that it would not expect to see any material upward shift in these charges during Q5; "
- 2.2.2 "it does not follow the single till methodology that the CAA uses to set airport charges and thus unreasonably discriminates against users of coach services; and"
- 2.2.3 "It is not based on a fair and reasonable allocation of costs and contradicts HAL's own principle of cost allocation that costs should be charged *"on the basis of actual measured usage or by specific items of expenditure which can be charged to airport departments on a precise basis<sup>1</sup>"*.
- 2.3 In the following chapter we set out HAL's response to each of the "3 core issues of principle" identified by the CPT.

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<sup>1</sup> CPT Heathrow Airport Coach and Bus Movement Charge joint submission document 18 July 2011.

## Chapter 3 - “The 3 core issues of principle” raised within the joint submission formal responses

3.1 Within this chapter of the provisional decision document we deal with those “3 core issues of principle” raised within the formal responses as detailed below:

- 3.11 “it contradicts the Civil Aviation Authority’s (CAA) policy that it would not expect to see any material upward shift in these charges during Q5;
- 3.12 it does not follow the single till methodology that the CAA uses to set airport charges and thus unreasonably discriminates against users of coach services; and
- 3.13 it is not based on a fair and reasonable allocation of costs and contradicts HAL’s own principle of cost allocation that costs should be charged “*on the basis of actual measured usage or by specific items of expenditure which can be charged to airport departments on a precise basis*”<sup>2</sup>.

3.2 “No Material upward shift in charges”

3.21 CPT joint statement – issue 3

*“We consider that HAL’s proposed increase to the bus and coach movement charge is inconsistent with CAA policy. As you will be aware, the CAA’s approach to regulating Heathrow airport during the period April 2008 until March 2014 (known as Q5) is set out in the CAA’s Decision document dated 11 March 2008<sup>3</sup> (Q5 Decision). Under the single till approach that the CAA uses to set charges, HAL’s total projected costs for each control period are assumed to be paid for partly by regulated aeronautical charges and partly by non-aeronautical charges (for simplicity we refer to these in the remainder of this document as regulated and non-regulated charges respectively).”*

3.22 HAL’s Response

The CAA Q5 Decision, paragraph 6.23 states “given that cost recovery had been agreed as the basis of pricing the vast majority of non-regulated charges in Q5, the CAA would not expect to see any material upward shift in these charges during Q5, resulting from any change by BAA in accounting or cost recovery policy, beyond those already embedded in the revenue forecast for Q5.” As per previous discussions, HAL has sought to recover 100% of all direct costs associated with this activity, and the proportions used in creating Table 6.3 of annuity and allocated costs contribution. Evidence of the changes in levels of direct costs has been provided via the Trading Statements and a breakdown of costs for 2011/12. Thus there has not been a change in either accounting or cost recovery policies.

3.23 CPT Joint statement – issue 4

*“As the CAA is unable to impose caps on the level of non-regulated charges, such as the bus and coach movement charge, it uses conditions set out in a public interest finding and its regulatory policy statement to protect users from exploitative increases in the level of these charges.”*

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<sup>2</sup> Economic Regulation of Heathrow and Gatwick Airports 2008-2013 CAA decision 11 March 2008

<sup>3</sup> Economic Regulation of Heathrow and Gatwick Airports 2008-2013 CAA decision 11 March 2008

### 3.24 HAL's Response

HAL has fulfilled its obligations under Annex D of the Q5 Decision "CONDITIONS AS TO THE COST INFORMATION AVAILABLE TO USERS IN RESPECT OF HEATHROW AIRPORT LTD IN ACCORDANCE WITH SECTION 46(2) OF THE AIRPORTS ACT 1986 and the modified conditions imposed by the CAA thereunder."

- 1) HAL has notified the CAA of the system used to allocate costs to non-airport charges activities on an annual basis and any amendments thereto.
- 2) Annual trading statements demonstrate actual costs and revenues for each of the facilities specified in paragraph 7 of Annex D (including facilities for bus and coach operators).
- 3) Statements of the pricing principles for this activity have been provided to users and their representative organisations prior to implementing the proposed price change.
- 4) Data has been provided to detail the assumptions and relevant cost information to demonstrate that the charges derive from the application of the pricing principles.
- 5) The costs stated to be in connection with this activity are as per those provided in the Profit Centre Reports submitted to the CAA.
- 6) Charges for this activity are established in relation to cost as demonstrated via the consultation process to date.
- 7) HAL has provided reasons for the difference in revenue sought to be recovered under the new proposals versus the revenue forecast in the price control review for the Q5 period.

### 3.25 CPT Joint statement – Issue 5

*"In practice this means that when it set the level of the regulated charge for Q5, the CAA made an assumption about the income that would be generated from non-regulated charges in each relevant year. In estimating the level of this income, the CAA relied heavily on information provided by HAL and ultimately adopted HAL's own projections of £1.39m (07/08 prices) in each year of the control period."*

### 3.26 HAL's response

HAL's proposals are based on the assumptions used for the projections outlined in Table 6-3 of the Q5 Decision but as can be seen from historical trading statements, direct costs have substantially increased year on year. These increases were not forecast within the income projection made in 2007. The increases proposed have been made in order to fulfil the principle of cost recovery.

### 3.27 CPT Joint Statement – Issue 6

*"Our analysis indicates that there has been no under recovery against the price cap, in fact HAL has over recovered in the two years for which information is available as set out in the table below."*

<i>Outturn prices</i>	<i>2008/09</i>	<i>2009/10</i>
<i>Actual income</i>	<i>£1.46m</i>	<i>£1.56m</i>
<i>CAA assumption</i>	<i>£1.41m</i>	<i>£1.47m</i>
<i>Variance</i>	<i>£0.5m</i>	<i>£0.9m</i>

*Notes: 08/09 and 09/10 income has been extracted from the HAL specified activities trading statements for year ended 31 March 2010.*

*The CAA assumption has been extracted from table 6-3 of the CAA final decision document and uplifted for inflation to ensure like for like comparisons.”*

### 3.28 HAL’s response

The income projections in Table 6-3 of the Q5 decision are forecast of income, these do not represent a cap on pricing. Non-regulated charges are recovered on a cost only basis. HAL has demonstrated the under recovery between income and cost via the trading statements provided as per the Q5 decision.

### 3.29 CPT Joint Statement – Issue 7

*“The nub of our concern is that the level of the regulated charge set by the CAA assumed that HAL would generate revenues of £1.39m (07/08 prices) in each year of Q5. If the CAA had assumed that HAL would generate the revenues set out in HAL’s proposal then it follows that the charge for bus and coach services may have been higher and the regulated charge would have been lower by an exactly equivalent amount. In this scenario, HAL would be revenue neutral. However, as this proposal to significantly increase the bus and coach charge is coming mid-period, then HAL will benefit unfairly from a windfall gain until the CAA returns to reset charges in 2014. We consider that this contradicts the CAA’s stated policy in respect of the treatment of non-regulated charges.”*

### 3.30 HAL’s response

HAL’s proposal to increase the charges for Bus and Coach Services is to ensure revenues reflect cost recovery, and not to increase revenues above those in the regulatory settlement.

### 3.31 CPT Joint Statement – Issue 8

*“In order to prevent this kind of mid-period readjustment of non-regulated charges, paragraph 6.23 of the CAA’s March 2008 Decision describes the measures the CAA proposed to introduce to strengthen regulatory expectations in this area:*

- given that cost-recovery had been agreed as the basis for pricing the vast majority of non-regulated charges, the CAA would not expect to see any material upward shift in these charges during Q5 resulting from any change by BAA in accounting or cost-recovery policy, beyond those already embedded in the revenue forecasts for Q5. Any such charge increase would be carefully scrutinised by the CAA and could be considered by the CAA in setting price caps for the relevant airport for the next price control period; and*
- the CAA does not preclude any adjustments of airport charges in the next review for any increase in non-regulated charges in Q5 that has not been adequately justified with reference to stated principles of cost recovery and the published forecasts of charges over Q5. Any new charges, which had not been foreseen in the setting of Q5 forecasts, should be subject to consultation with*



*airline users in advance of their introduction, and should demonstrate compliance with the principle of cost recovery and a robust and consistent approach to cost allocation across services and facilities.”*

### 3.32 HAL’s Response

The Q5 Decision, paragraph 6.23 states “given that cost recovery had been agreed as the basis of pricing the vast majority of non-regulated charges in Q5, the CAA would not expect to see any material upward shift in these charges during Q5, resulting from any change by BAA in accounting or cost recovery policy, beyond those already embedded in the revenue forecast for Q5.” As per previous discussions, HAL has sought to recover 100% of all direct costs associated with this activity, and the proportions used in creating Table 6.3 of annuity and allocated costs contribution. Evidence of the changes in levels of direct costs has been provided via the Trading Statements and a breakdown of costs for 2011/12. Thus there has not been a change in either accounting or cost recovery policies.

### 3.33 CPT Joint Statement – Issue 9

*“The CAA went on to state that it would look to BAA to demonstrate that it had worked pro-actively towards securing the confidence of users that BAA’s projections are soundly based on reasonable cost estimates and reasonable cost allocation policies. We consider that the proposal represents a material upward shift in charges from a change in cost-recovery policy on precisely the terms that the CAA stated it would not expect to see during Q5.”*

### 3.34 HAL’s response

A number of engagements with users have been held to explain the costs forecast to be recovered under this proposal. Further, HAL has not made any changes in accounting or cost recovery policy. The price increases reflect changes in the levels of direct costs from those forecast when the Q5 Decision was issued and recovery of costs.

### 3.35 CPT Joint Statement – Issue 10

*“Furthermore, CPT and the operators consider that the information supplied by HAL to date has not been sufficient for us to be satisfied that the proposed charge is related to reasonable costs and is based on appropriate allocation methodologies. We consider that this situation must be resolved in order for HAL to adequately meet the requirements of the 1991 Public Interest finding on specified activities.”*

### 3.36 HAL’s response

HAL has provided evidence to all attendees on costs incurred. The issues to date have centred on allocated costs and the proportionality of these to this specified activity. The levying of allocated costs has been explained and demonstrated in accordance with HAL’s transparency statement. The allocated costs levied against this activity represent 0.41% of HAL’s allocated costs per annum. This has not changed during Q5.

## 3.4 “The Principle of the single till”

### 3.41 CPT Joint Statement – Issue 11

*“Our second issue of principle relates to the treatment of revenue streams associated with the bus and coach movement charge. Our understanding of HAL’s methodology for calculating the revised charge is that it does not take into account the retail and other income that passengers travelling by bus and coach bring in to the airport. A central tenet of the CAA’s approach to airport regulation is that charges should be set on a single till basis i.e. the commercial and other revenues that are generated as a direct consequence of airport activities should be used to offset the level of charges imposed by the airport operator.”*

#### 3.42 HAL’s response

“Economic Regulation of Heathrow Airport is based on a single till approach taking into account the regulatory building blocks which include commercial revenues. Commercial revenues will include a forecast for retail revenues generated at the central bus station. Under the single till approach, the projected revenues from commercial activities are deducted from the total revenue requirement. The remainder represents the revenue to be recovered through regulated aeronautical charges from the airlines. This approach is widely recognised and has been applied to the economic regulation of Heathrow for over two decades.

The regulatory settlement for Q5 contains a forecast for non regulated charges which includes bus and coach station facilities. This is based solely on cost related principles.

The single till approach and the forecast for bus and coach facilities was endorsed by the CAA and is included as part of the Q5 regulatory settlement.

#### 3.43 CPT Joint Statement – Issue 12

*“In this regard, we consider that bus and coach operators should enjoy equitable treatment with airlines insofar as the charges that they pay for using the airport should be offset by the relevant revenues. In practice this would mean that HAL would calculate charges based on a coach terminal single till which would take account of the ticketing commission income, Cafe Nero/WH Smith income, etc”*

#### 3.44 HAL’s response

Under the single till approach, the projected revenues from commercial activities are deducted from the total revenue requirement. The remainder represents the revenue to be recovered through regulated aeronautical charges from the airlines. Commercial activities cover both terminal and non terminal revenues i.e. this includes retail revenues generated in the bus station.

The regulatory settlement for Q5 includes a forecast for non regulated charges which includes bus and coach station facilities. This is based solely based on cost related principles.

The single till approach and the forecast for bus and coach facilities was endorsed by the CAA and is included as part of the Q5 regulatory settlement.

#### 3.45 CPT Joint Statement – Issue 13

*“As an extension of this principle we consider that the calculation of commercial revenues should also include a portion of the on-airport revenues that are generated by bus and coach users. We consider that a failure to base the bus and coach*

*charge on a single till approach is likely to constitute unreasonable discrimination against bus and coach users and the unfair exploitation of a bargaining position under Section 41 of the Airports Act 1986.”*

#### 3.46 HAL’s response

We do not accept these allegations. Non-regulated charges are calculated based on cost recovery only. The regulatory settlement for Q5 includes a forecast for non regulated charges which includes bus and coach station facilities and is solely based on cost related principles.

Under the single till approach, the projected revenues from commercial activities are deducted from the total revenue requirement. The remainder represents the revenue to be recovered through regulated aeronautical charges from the airlines. Commercial activities cover both terminal and non terminal revenues i.e. this includes retail revenues generated in the bus station.

The single till approach and the forecast for bus and coach facilities was endorsed by the CAA and is included as part of the Q5 regulatory settlement.

### 3.5 “The principle of cost allocation between coach and bus”

#### 3.51 CPT Joint Statement – Issue 14

*“Our third issue of principle relates to the allocation of costs to coach services. We do not support the methodology used to determine the split between coach and bus. HAL has used the number of bays utilised by coach and bus as the allocation metric which leads to 61% of costs being allocated to coach services. Our detailed review in this area indicates that a much more relevant driver of costs would be vehicle movements. For that reason, we consider that the ‘number of departures’ should be used as the allocation basis. This would result in a 33% allocation of cost to coach services.”*

#### 3.52 HAL’s response

HAL considers its cost allocation method proposal for direct costs to be fair and reasonable. CPT’s proposal of allocating the allocated costs by total movements overly simplifies this calculation and does not take into account usage of space or usage of facilities.

The theory of allocation of space and therefore cost is entirely consistent with the current charging practices within Heathrow today.

Use of the central bus station departure lounge by coach customers is significantly greater than by those of bus customers. The Airport’s QSM survey for 2008/09 showed that 94% of passengers surveyed within the waiting area facility were coach customers. The recovery mechanism proposed by HAL is based upon usage data for these facilities.

#### 3.53 CPT Joint Statement – Issue 15

*“The use of the ‘number of departures’ as the best proxy of usage can be illustrated by examining the indirect costs broken down in pages 39 and 40 of the March 2010 trading statements. The main component of the £1m annuity charge is the cost of road surfacing which represents around 67% of the total annuity cost. We consider that these costs should clearly be allocated by the number of coach movements*

*rather than the number of bays. Similarly, the other costs in the annuity are land, drainage, information systems, furniture and signs, electrical systems and lifts. These are not related to coach bays and provide further evidence that the number of departures provides a more appropriate proxy under the 'user pays' principle. "*

#### 3.54 HAL's response

As per the annual trading statements, the annuity for Buses and Coaches is calculated based upon the return on assets associated with the Central Bus Station, the Central Bus Station Waiting Lounge and T5. These assets have been categorised as Information Systems; Furniture, Signs etc.; Electrical Systems; Lifts; Surface Construction and Drainage. The return on land is also included within this annuity. The recharging of the annuity in accordance with the number of bays is consistent with the methodology described on the Trading Statements for the T3 Coach Park.

### 3.6 "The basis of "Allocated Costs" to Coach and Bus"

#### 3.61 CPT Joint Statement – Issue 16

*"In a similar vein, we consider that the £1.6m of allocated costs have not been allocated based on usage. These costs include airport wide engineering, ground operations, medical centre and HAL's admin and overhead costs. These should also be allocated on a 'user pays' principle."*

#### 3.62 HAL's response

Allocated costs are costs that are incurred by HAL which are not directly related to delivery of the service, but where a proportion is allocated by the methodology set out in HAL's Transparency Statement as provided during consultation. These costs are mainly administrative costs carried out on an airport wide basis.

#### 3.63 CPT Joint Statement – Issue 17

*"At the meeting on 31 May 2011, the minutes record HAL stating "With regards indirect costs, this is on the basis of usage." Furthermore, the Transparency Conditions that set out HAL's cost allocation methodology state that indirect costs should be allocated "on the basis of actual measured usage or by specific items of expenditure which can be charged to airport departments on a precise basis".*

#### 3.64 HAL's response

The extract above refers to the methodology used for cost allocations between buses and coaches not the calculation of Allocated Costs which have been the subject of much discussion.

The Transparency Statement describes Allocated Costs as, "Those cost centres which cannot be wholly identified with individual Profit centres are allocated. They cover mainly administration carried out on an airport wide basis".

The full minute states: "SB: Presented HAL's proposals regarding the proposed cost allocation methodology. For direct costs the proposal is in line with guidance from the CBS management contract (slide 4). With regards to indirect costs, this is on the basis of usage. It was noted that since its previous work, HAL has revisited the previously

proposed methodology and tried to come up with a reasonable way to allocate costs and implement charges”.

This refers to the methodology of cost allocation between bus and coach as opposed to the calculation of allocated costs.

### 3.65 CPT Joint Statement – Issue 18

*“Appendix A records against each indirect cost the allocation basis as per the Transparency Conditions. It is clear from this analysis that costs incurred in other parts of the airport that are wholly outside of the Central Bus Station (CBS) or not relating to CBS have been allocated to CBS. For instance, IT costs have been allocated to CBS despite the fact there are no computers or IT within CBS provided by HAL and the engineering costs are from other parts of the airport and do not relate to CBS. These two alone account for £1.0m of the £1.6m of allocated costs”*

### 3.66 HAL’s response

Allocated costs are costs that are incurred by HAL which are not directly related to delivery of the service, but where a proportion is allocated by the methodology set out in accordance with HAL’s Transparency Statement. In the interests of transparency HAL provides the full value of Allocated Costs per activity on the Trading Statements, this is then adjusted to the levels used when Table 6-3 of the Q5 Decision was created. Post Table 6-3 adjustment, Allocated Costs represent £665k. The recovery of Allocated Costs from this particular activity represents 0.41% of HAL’s total Allocated Costs.

### 3.67 CPT Joint Statement – Issue 19

*“We propose that in light of the difficulty in allocating costs as highlighted above, charges should be based on a simplified approach based on the ratio of direct to indirect costs. This is an accepted accounting treatment for allocating indirect costs and is the basis for many of the cost allocation principles within HAL’s Trading Statement.”*

### 3.68 HAL’s response –

Due to the nature of airport regulation HAL allocates a proportion of the central costs to individual activities. The allocation of these costs is as per the HAL Transparency Statement set out in Appendix. Allocated costs are central activities carried out on an airport wide basis as opposed to Indirect costs which are charged on the basis of actual measured usage or can be recharged on a specific basis.

### 3.69 CPT Joint Statement – Issue 20

*“Our analysis of the other specified activities reveals that the typical allocation of indirect costs is around 25% of the direct costs. Applying that metric to the Coach charge would result in a cost of £300k. We would welcome the opportunity to explore this further with HAL, in the meantime CPT and the operators reserve their position on the reasonableness of the cost allocation metrics and the calculation of the annuity.”*

### 3.7 HAL's response –

HAL has sought to recover Allocated Costs and Annuity in accordance with previously submitted assumptions. The ratio of Allocated Costs to Direct Costs varies substantially across all Specified Activities. HAL does not accept the statement made above that typical allocation of indirect costs (sic) Allocated costs is around 25% of direct costs. HAL does not believe that it would be appropriate to change the recovery of Allocated Costs mid Quinquennium as this would represent a change of cost recovery policy.

## Chapter 4 - Response to joint submission proposal

4.1 In this Chapter HAL responds to the counter proposal that is set out within the joint statement submission.

### 4.11 CPT Joint Statement – Issue 21 –

*“The table below sets out a preliminary comparison of the HAL approach to calculating the fee with the methodology proposed by CPT and the operators. The latter results in a proposed maximum fee of £3.68 which is an equivalent to an increase of 55%. This compares with HAL’s proposal of 707%.*

	<b>HAL</b>	<b>CPT</b>
<i>Ticketing and Operations Contracts</i>	980,000	<b>-20,000</b>
<i>Cleaning &amp; Utilities</i>	273,000	273,000
<i>Rent</i>	56,500	56,500
<i>Annuity</i>	966,818	966,818
<i>Allocated Costs</i>	1,673,728	300,000
<i>Coach station commercial revenues</i>	(tbc)	<b>-583,000</b>
<b>Total</b>	<b>3,950,046</b>	<b>993,318</b>
<i>Allocation to Coach</i>	61%	33%
<i>Coach Departures</i>	141223	141223
<b>Coach Departure Fee</b>	<b>16.99</b>	<b>2.34</b>

### 4.12 HAL’s response

HAL has populated the above table, according to the request of the Joint submission. HAL does not agree with nor accept the principles used within this table to produce the counter proposal submitted by the CPT.

### 4.13 CPT Joint Statement – Issue 22

*“We consider that this analysis is preliminary pending further discussion on the allocation metrics and the calculation of the annuity. In addition, we would welcome further information from HAL on the commercial revenues generated from bus and coach services which should be deducted from the costs in line with the single till principle. It would be helpful if HAL could populate the table above with details of the revenues generated from Café Nero/WH Smith etc. in 2010. This should also include an appropriate allocation of the on-airport commercial revenues that are generated by bus and coach users”*

#### 4.14 HAL's response

Economic Regulation of Heathrow Airport is based on a single till approach taking into account the regulatory building blocks which include commercial revenues. Commercial revenues will include a forecast for retail revenues generated at the central bus station and these are offset against airport charges. Therefore it is not appropriate to double count those commercial revenues into this activity. HAL has populated the table with the Cafe Nero/ WH Smith 2010 income number. The value attributed to the difference between the Ticketing and Operations' contracts is not as suggested by the CPT in the table above.

#### 4.15 CPT Joint Statement – Issue 23

*“In conclusion, the CPT and operators reject HAL's proposal on the basis that:*

- it is not consistent with the CAA's regulatory framework and will lead to an unreasonable windfall gain for the airport;*
- it does not include the revenues that are generated by users of bus and coach services and therefore unreasonably discriminates against these users; and*
- it is not based on a fair and reasonable allocation of costs.”*

#### 4.16 HAL's response

HAL does not accept the points provided by the CPT to reject HAL's proposal to date.

- The CAA document states “ the CAA would not expect to see any material upward shift in these charges during Q5, resulting from any change by BAA in accounting or cost recovery policy, beyond those already embedded in the revenue forecast for Q5”. HAL have not sought to change either their accounting or cost recovery policies. The changes proposed have been in line with this policy.
- Non-regulated charges are calculated based on cost recovery only. The regulatory settlement for Q5 includes a forecast for non-regulated charges which includes Bus and Coach services and is solely based on cost related principles.

Under the single till approach, the projected revenues from commercial activities are deducted from the total revenue requirement. The remainder represents the revenue to be recovered through regulated aeronautical charges from the airlines. Commercial activities cover both terminal and non terminal revenues i.e. this includes retail revenues generated in the bus station.

The single till approach and the forecast for Bus and Coach services was endorsed by the CAA and is included as part of the Q5 regulatory settlement.

- HAL firmly believes that the way we have proposed to allocate costs between Bus and Coach is equitable and transparent. The theory of allocation of space and therefore cost is entirely consistent with the current charging practices within Heathrow today. The tariffs set represent cost recovery and this is most clearly demonstrated when compared with tariffs for commercial facilities such as Victoria Coach Station.



#### 4.17 CPT Joint Statement – Issue 24

*“We recommend that HAL uses the counter proposal set out above as the basis for future consultation on the level of the charge. CPT and operators consider that if an agreement cannot be reached on this matter then the CAA's policy of no material change to this charge in Q5 should come in to effect and further discussion on the level of the charge should be postponed until the Q6 review of airport charges”.*

#### 4.18 HAL's response

HAL reject the counter proposal submitted by the CPT for the reasons outlined above. With regards to the request to defer any price change to Q6, HAL rejects this request as it would perpetuate the under recoveries currently being made for this service. Also it should be noted that that no increases in price for this service have been levied since 2008.

## Chapter 5 - Individual Responses

5.1 In this chapter HAL responds to issues raised by the operators that fall outside of the Joint submission document.

### 5.11 Individual operator response

*“Our principal public transport competitor (apart from rail via Paddington involving HAL's own rail connections to Heathrow) is private hire cars and people carriers which we understand are not subject to charges, and we believe that a significant increase in the charge for our RailAir service could be considered anti-competitive.”*

### 5.12 HAL's response

Private Hire cars and commercial coaches operate within different segments of the market and we refute the statement that the proposal is anti-competitive. All Private Hire and private passenger vehicles are required to operate “pick ups” from within car parks at Heathrow and therefore contribute a minimum of £2.70 per pick up to the Airport. Further, these revenues are recovered on a commercial basis, as opposed to cost recovery, and the impact of such revenues is included within the single till.

## Chapter 6 - Provisional Decision & Implementation timetable

- 6.11 HAL has considered the responses submitted jointly by the CPT and Coach Operators, outlined above and has responded accordingly within this Provisional Decision document.
- 6.12 Following due consideration of the submissions above, HAL hereby confirms its intention to recover costs in accordance with HAL's original proposal as restated within this Provisional Decision.
- 6.13 The tariff will be set to recover costs as detailed below –
- Direct costs – (CBS contract) 66% to coach and 34% to local bus;
  - Indirect costs – (Utilities, Facilities Management, and Rent) 59% to coach and 41% to local bus;
  - Annuity and Allocated costs – 59% to coach and 41% to local bus.
- 6.14 Cost recovery model:

<b>Central Bus Station Costs 2011/2012</b>					
Activity	Total cost	Coach attributed cost	Coach attributed cost %	Local Bus attributed cost	Local Bus attributed cost %
CBS Ops contract cost	£980,000	£646,800	66%	£333,200	34%
Utilities	£39,912	£23,548	59%	£16,364	41%
Facilities Mgmt (incl cleaning)	£233,240	£137,612	59%	£95,628	41%
Rent	£56,500	£33,335	59%	£23,165	41%
Annuity	£966,818	£570,423	59%	£396,395	41%
Allocated costs	£1,673,728	£987,500	59%	£686,228	41%
<b>Total costs</b>	<b>£3,950,198</b>	<b>£2,399,217</b>	<b>61%</b>	<b>£1,550,981</b>	<b>39%</b>

- 6.15 The movement charge for operators will be calculated by dividing the cost by the appropriate number of movements, in accordance of the cost recovery metrics as detailed in paragraph 6.13 above.
- 6.16 The price per movement has been calculated in accordance with the declared number of movements for 2010 received from the Coach Operators. The tariff is set to recover the costs outlined above. In the event that the number of movements varies from those in 2010, this could impact future tariff levels.

<b>Heathrow Bus and Coach Movement Charge 2011/2012</b>	
Activity	Coach
<b>Movements</b>	<b>141,223</b>
<b>Costs</b>	<b>£2,399,127</b>
<b>Movement Charge</b>	<b>£16.99</b>

## 6.2 Implementation of the Provisional Decision

6.2.1 The consultation document invited comments on the implementation of the proposed Heathrow Bus and Coach Movement Charge. There was no specific feedback detailed within the responses other than the objection to the scale of the increase.

The consultation document provided two different options for implementation of the proposed Heathrow Bus and Coach Movement Charge.

1. Price increase from 1<sup>st</sup> November 2011 to £16.99 ; or
2. A phased approach to the implementation of pricing changes.
  - i) 1<sup>st</sup> November 2011 to £10.00;
  - ii) 1st April 2012 to £16.99.

Subsequently HAL would expect to move to recover the full recoverable costs associated with the activity.

Note: The level of charge associated with the second phase increase will be calculated on the same basis of the 2011/12 charge of £16.99 but is subject to variables such as coach movement changes and RPI and cost fluctuations.

6.3 HAL has considered the responses of the CPT and coach operating companies in the context of the overall objectives of the proposed changes to the Heathrow Bus and Coach Movement Charge.

6.4 In response to the submissions received to date, HAL has decided to present 3 further options for consultation on the implementation of the proposed Heathrow Bus and Coach Movement Charge as outlined below.

3. A phased approach to pricing changes –
  - i) 1<sup>st</sup> November 2011 - £7.00 per movement;
  - ii) 1<sup>st</sup> April 2012 - £13.00 per movement;
  - iii) 1<sup>st</sup> April 2013 - £16.99 per movement.
4. Retail Price Index linked increases per annum for the remainder of Q5 effective 1<sup>st</sup> October 2011, and 1<sup>st</sup> April each year thereafter. Full cost recovery shall apply from the commencement of Q6.
5. Incremental application of the price increase for the remainder of Q5 and early part of Q6 in order to achieve cost recovery levels by 1<sup>st</sup> April 2016.
  - i) 1<sup>st</sup> April 2012 - £4.80
  - ii) 1<sup>st</sup> April 2013 – £7.40
  - iii) 1<sup>st</sup> April 2014 - £10.00
  - iv) 1<sup>st</sup> April 2015 - £13.00
  - v) 1<sup>st</sup> April 2016 – full cost recovery.

6.5 Following due consideration of all responses and the proposals above, HAL hereby announces that its provisional decision is as follows:

**The Bus and Coach Movement tariff shall be increased in accordance with Option 3 above.**

A phased approach to pricing changes –

- i) 1<sup>st</sup> November 2011 - £7.00 per movement;
- ii) 1<sup>st</sup> April 2012 - £13.00 per movement;
- iii) 1<sup>st</sup> April 2013 - £16.99 per movement.

6.6 As per the Heathrow Airport – Bus and Coach Movement Charge Consultation Document dated 19<sup>th</sup> May 2011, as amended by letter dated 3<sup>rd</sup> June 2011, please submit your responses to this Provisional Decision Document in writing to [steve\\_bogg@baa.com](mailto:steve_bogg@baa.com) by 12 September 2011, a Final Decision will be published on 3<sup>rd</sup> October 2011. This decision will be implemented 1<sup>st</sup> November 2011.

## **Chapter 7 - List of Respondents**

Confederation of Passenger Transport

Oxford Bus Company

National Express

First Group

## **Appendix A - HAL's Transparency Statement for 09/10**

**AIRPORTS ACT 1986**

**HEATHROW AIRPORT LIMITED**

**TRANSPARENCY CONDITIONS**

**YEAR END 31 MARCH 2010**

The following information is prepared in accordance with the conditions as to cost information available to users imposed under Section 46(2) of the Airports Act 1986.

Page 2: Profit centre report for the specified facilities.

Pages 3 to 7: Principles of cost allocation

Page 8 to 9: Independent auditors' report

The information pages 2 to 7 attached, was approved by the Board of Directors on 8th October 2010.

Director: .....

J Leo

HEATHROW AIRPORT LIMITED											
PCR/CAA SUBMISSION 2010											
PROFIT CENTRE : SPECIFIED ACTIVITIES											
FY March 2010											
	FIXED	AIRSIDE	STAFF	STAFF	BAGGAGE AND	OTHER DESK	BUS & COACH	HEATING	WATER	ELECTRICITY	
	GROUND POWER	LICENCES	I.D. CARDS	CAR PARKS	CHECK-IN FACILITIES	LICENCES	OPERATORS				
	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000
<b>TOTAL INCOME</b>	<b>7,517.9</b>	<b>1,436.2</b>	<b>2,699.0</b>	<b>22,424.1</b>	<b>109,929.1</b>	<b>307.3</b>	<b>1,382.0</b>	<b>447.9</b>	<b>1,033.7</b>	<b>25,608.7</b>	
<b>DIRECT EXPENDITURE</b>											
Staff Costs	0.0	0.0	624.6	0.0	7,439.3	0.0	0.0	659.3	1,109.5	0.0	
Property Related Costs	0.0	0.9	13.3	5,763.3	19,685.3	0.0	339.9	575.2	2,300.6	86,238.7	
Retail Expenditure	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Maintenance & Equipment	0.0	0.0	393.6	1,102.5	60,165.4	0.0	0.0	924.9	387.3	0.0	
General Expenses	0.0	0.0	557.9	137.8	12,624.3	0.0	0.0	25.2	119.1	3.0	
Capitalisation of Revenue	0.0	0.0	0.0	-822.4	2,849.0	0.0	0.0	0.0	-24.2	0.0	
Depreciation	388.4	1.3	13.6	66.1	35,595.2	0.0	3.7	15.3	258.2	59.1	
Indirect Charges	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
<b>TOTAL DIRECT</b>	<b>388.4</b>	<b>2.2</b>	<b>1,603.0</b>	<b>6,247.2</b>	<b>138,358.6</b>	<b>0.0</b>	<b>343.6</b>	<b>2,199.9</b>	<b>4,150.4</b>	<b>86,300.8</b>	
<b>ALLOCATED EXPENDITURE</b>											
Terminal Management	0.0	0.0	14.4	56.0	2,371.0	122.0	3.1	19.8	35.3	781.8	
Airside Safety and Security	87.6	772.5	172.8	5.1	75.4	0.0	3.0	6.5	5.1	8.5	
Ground Operations	0.0	0.0	0.1	315.2	2.6	0.0	1,307.8	0.1	31.5	5.6	
Engineering	1,274.8	6.7	60.5	1,321.6	13,843.1	0.0	1,721.7	772.0	3,362.6	228.7	
Rates	48.1	120.3	144.4	4,154.9	3,970.4	200.5	385.0	385.0	32.1	328.9	
Finance	0.0	0.0	63.4	246.7	1,594.8	0.0	13.6	87.2	155.4	3,442.2	
IT	545.5	230.6	635.5	787.4	5,095.3	101.2	511.8	826.7	359.9	511.8	
Group Supply	0.0	0.0	14.0	54.6	353.1	0.0	3.0	19.3	34.4	762.1	
Police	19.0	47.6	57.1	1,643.1	1,570.2	79.3	152.3	152.3	12.7	130.1	
Airport Management	30.8	32.0	135.7	471.5	3,154.8	0.0	36.3	184.5	310.9	6,350.0	
Medical Centre	9.9	10.3	6.1	5.7	71.5	0.0	3.6	7.7	8.1	6.7	
Human Resources	22.0	22.8	13.6	12.7	159.0	0.0	7.9	17.1	18.0	14.9	
Property Management	91.6	12.2	278.1	303.1	392.5	11.9	281.1	392.4	160.8	360.9	
Commercial	0.0	0.0	0.0	32.8	0.0	0.0	103.8	0.0	0.0	0.0	
Public Relations	-1.2	-0.2	-0.4	-3.7	-12.9	-0.1	-0.2	-0.1	-0.2	-4.2	
Depreciation	1,251.1	693.8	1,011.1	2,267.1	13,371.7	-1,848.0	1,945.0	983.7	1,259.5	20,017.3	
Sundry Income	-318.4	-223.0	-359.4	-497.8	-3,374.9	-76.0	-305.3	-532.0	-255.4	-1,003.9	
<b>TOTAL ALLOCATION</b>	<b>3,060.8</b>	<b>1,725.7</b>	<b>2,247.0</b>	<b>11,176.0</b>	<b>42,637.4</b>	<b>-1,409.0</b>	<b>6,173.2</b>	<b>3,322.1</b>	<b>5,530.8</b>	<b>31,941.2</b>	
<b>TOTAL EXPENDITURE</b>	<b>3,449.2</b>	<b>1,727.9</b>	<b>3,850.0</b>	<b>17,423.2</b>	<b>180,996.0</b>	<b>-1,409.0</b>	<b>6,516.8</b>	<b>5,522.0</b>	<b>9,681.2</b>	<b>118,242.0</b>	
<b>PROFIT/(LOSS)</b>	<b>4,068.7</b>	<b>-291.7</b>	<b>-1,151.0</b>	<b>5,000.9</b>	<b>-71,066.9</b>	<b>1,716.3</b>	<b>-5,134.8</b>	<b>-5,074.1</b>	<b>-8,647.5</b>	<b>-92,633.3</b>	



**HEATHROW AIRPORT LIMITED**  
**BROAD PRINCIPLES OF COST ALLOCATION**

1. Direct Expenditure

All transactions (income and expenditure) are posted to General Ledger Cost Codes which represent Cost Centres within the management accounting system. Transactions posted to the Cost Centres which can be wholly identified with a Profit Centre, form the income and direct expenditure allocated to a Profit Centre. Direct expenditure includes depreciation of fixed assets and indirect charges.

1.1 Depreciation

Depreciation is charged directly to Cost Codes in accordance with the appropriate fixed assets identified with individual Cost Codes within the fixed asset register. The depreciation posted to the Cost Centres which can be wholly identified with a Profit Centre therefore forms the direct depreciation allocated to a Profit Centre.

1.2 Indirect Charges

Indirect charges cover those Cost Centres, which are either activities in their own right and can be Profit Centres but which also provide services to other airport departments. These are charged on the basis of actual measured usage or by specific items of expenditure which can be charged to airport departments on a precise basis. The internal charges are not reflected in the PCRs due to the back out journal posted each month at a department level. These activities/items include:-

**Rent & Rates-**

Rates recharged to the Connections department are based on the Rates liability for which they are responsible as assessed by the District Valuations Officer. Rent & rates for the Heathrow Point Complex are recharged to occupying departments based on sq ft. All other Rates charged as direct expenditure.

**Electricity-**

the electricity units consumed are re-charged to tenants and indirectly charged to airport departments at the current resale price per unit. The units consumed by tenants and internal users are measured and monitored by the Property/Utilities Department.

- Water** - this is indirectly charged mostly on the basis of metered consumption with some areas estimated based on the number of employees and an historically established consumption per person.
- Heating & Ventilation** - This is indirectly charged to internal departments on the same basis as it is to tenants. That is the current resale price per square foot for the area occupied.
- Maintenance** - For the 2009/10 financial year, indirect charges for maintenance were made via the Maximo system. Work undertaken has a provider code and receiver code to identify the beneficiary of the work. Any residual balance not charged out due to an under/over absorption of cost was allocated on the basis of staff time spent on each activity. The data used for this was captured from the system itself.

## 2. Allocated Expenditure

Those Cost Centres which cannot be wholly identified with individual Profit Centres are allocated. They cover mainly administration carried out on an airport-wide basis. The activities included in allocated expenditure and the bases of allocation are:-

- Airside Safety and Security** - the Safety and Security Management is allocated generally on the basis of staff deployment as assessed by the Airside Safety and Security Business Services Manager.
- Engineering** - These will include general engineering management costs and other costs not included in the engineering charge out rate. These are allocated out to profit centres based on the staff time spent on each activity.

- Finance** - The Finance Department costs are allocated on the basis of direct expenditure before depreciation. This is calculated by the Finance Department and based on data at 31 March 2010.
- I.T.** - IT Department costs have been allocated based on the number of computer terminals in use by each Profit Centre.
- Group Supply** - costs allocated on the basis of direct expenditure before depreciation. This is calculated by the Finance Department and based on data at 31 March 2010.
- Airport Management** - the cost of Airport Management including Corporate Office charges (excluding Group IT & Group Supply) is allocated on the basis of direct expenditure before depreciation. The allocation is based on actuals to 31 March 2010.
- Human Resources** - the cost of Human Resource Management, Administration, Training, Welfare, Employee relations etc. is allocated on the basis of staff numbers in each department.
- Terminal Management** - allocated on the basis of estimated staff deployment by the Departmental Managers.
- Terminal accommodation and common areas are allocated on the basis of the proportion of areas in each Profit Centre.
- Ground Operations** - Ground Operations Management costs are allocated on the basis of staff time associated with Profit Centre activities. The Management of Terminal Forecourts is allocated on an assessment of the area dedicated to each operation. Passenger subways and roads are allocated on estimates of usage.
- Medical Centre** - this allocation is based on staff numbers in each department.

<b>Commercial</b>	-	this allocation is based on Retail Income in each department. The calculation is made by the Finance Department based on actuals to 31 March 2010.
<b>Public Relations</b>	-	allocated on the basis of direct income within each profit centre. The calculation is made by the Finance Department based on actuals to 31 March 2010.
<b>Property Management</b>	-	Support functions within the department have been allocated on the direct income of the activities which they support. The Property Management function has been allocated on staff time.
<b>Rates</b>	-	the rateable value breakdown by area provided by BAA Rating Department is analysed by Profit Centre and the rates charge is allocated in proportion to the rateable values identified within each Profit Centre by Finance. As noted above the rates charges for the Connections Department, which are re-charged directly to the users of the airport's baggage systems are charged as an indirect charge.
<b>Police</b>	-	police costs charged to the airport are allocated on the same basis as rates.
<b>Depreciation</b>	-	depreciation is allocated on the same basis as the other expenses of a Cost Centre.
<b>Sundry Income</b>	-	sundry income is allocated on the same basis as the other expenses of a Cost Centre.
<b>Heathrow Express</b>	-	does not receive allocated costs as it is a separate entity under a separate identifiable management structure the costs of which are pointed directly to the HEX profit centre.

3. The profit centre report for the specified facilities shown at page 2 does not include reports for the following facilities specified in the transparency conditions:-

- Hydrant Refuelling
- Airside Parking
- Cable Routing
- Maintenance Rentals

Profit centres have not been established in respect of these facilities.

The income from Hydrant Refuelling in 2009/10 was £6.3m and is included in the Profit Centre Perimeter Properties which is not a specified facility. The majority of income is attributable to a lease of the Heathrow fuel hydrant system granted to the Heathrow Fuel Consortium.

In the case of Airside Parking and Cable Routing the level of income is not sufficiently material to warrant separate identification. No income is derived specifically from the provision of cable routing through the airports infrastructure. However £21k is generated from Minor Facility Licences where cable routing may form part of the licence fee, but is not specifically identified.

The income from Maintenance Rentals (which excludes baggage system maintenance which is recovered separately) in 2009/10 amounted to £3.9m and is included in the various property related profit centres which are not specified facilities. The current rentals per square foot have evolved from an initial base uplifted each year in accordance with appropriate indices. Service Charges are also received whereby tenants receive a full breakdown of costs being recovered. Income from Service Charges in 2009/10 amounted to £1.7m.

## INDEPENDENT REPORT FROM PRICEWATERHOUSECOOPER LLP

### Report in respect of the Transparency Statements for Heathrow Airport Limited (“the Airport”)

We have reviewed the Transparency Statements for Heathrow Airport Limited for the year ended 31 March 2010 (“the Statements”) in accordance with our engagement letter between the Civil Aviation Authority (“the CAA”) and Heathrow Airport Limited (“the Airport”) of 10 August 2004 (“engagement letter”). A copy of the Statements, which is the responsibility of the directors, is attached to this report.

Our report is made solely to the Airport and the CAA in accordance with our engagement letter. Our work has been undertaken so that we might report to the Airport and the CAA those matters we are required to state to them in this report in accordance with the engagement letter and for no other purpose. To the fullest extent permitted by law we do not accept or assume responsibility to anyone other than the Airport and the CAA for our work, for this report or for the opinions we have formed.

We carried out the following procedures:

- Obtained a signed copy of the audited Financial Statements of the Airport for the year ended December 31, 2009, formally approved by the Directors;
- Obtained a copy of the unaudited management accounts of the Airport for the financial year and the three months period ended 31 March, 2010 and the three months ended 31 March, 2009;
- Obtained a copy of the statements as prepared by the Airports’ directors;
- Checked that the process described in the “Broad Principles of cost allocations” by which the Airports’ directors compile the Statement and for the preparation of the Profit Centre Reports have been followed;
- Checked that the financial information provided in the statements and Principles of Costs allocation has been accurately extracted from the Airport’s books and records;
- Agreed the information included in within the Statement for the Airport to the audited financial statements and unaudited management accounts, as applicable;
- Recalculated all calculations in the Statements;
- Checked that any necessary amendments to the Statements arising from the above work are correctly reflected in the final Statements approved by the Directors.

Based on the procedures carried out:

- the information presented in the Statements has been properly extracted from the books and records of the Airport, and is arithmetically accurate;
- the Statements have been compiled in accordance with the process established by the Airport’s directors for preparing the Statements.

We are the current auditors of the Airport. We do not accept, or assume responsibility to anyone other than the Airport and the Airport’s members as a body, for our audit work, for our audit report(s) or for the opinions we have formed. The statutory audit is undertaken in order that we might report to the Airport’s members, as a body, in accordance with Section 235 of the Companies Act 1985 on whether the financial statements of the Airport,

which are the sole responsibility of the Airport's directors, give a true and fair view of the state of affairs of the Airport as at the end of the relevant financial year and for no other purpose.

### **Third party**

Our report is addressed to you and is provided solely for your use and benefit and only in connection with the purpose set out in the engagement letter. Unless required by law, you shall not provide our report, or a copy thereof, in whole or in part, to any other person or party or refer to us or the Services without our prior written consent, which we may at our discretion grant, withhold or grant subject to conditions. In no event, regardless of whether consent has been provided, shall we assume any liability or responsibility to any third party to which any report or letter is disclosed or otherwise made available.

PricewaterhouseCoopers LLP

London

8th October 2010

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