To:
Louise Ellman
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House of Commons
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Date: 27 June 2014

Dear Ms Ellman

I am writing in reference to the letter Sir Howard Davies sent you on 21 March 2014 in your role as Chair of the Transport Select Committee. It has become apparent that a transcription error has been made in the letter.

In the table in paragraph 8 (please see attached original letter for reference) the cost figures for Heathrow NW and the Estuary options were correct, but the Gatwick and Heathrow Extended N runway options were transposed.

The table should read as below:

<table>
<thead>
<tr>
<th>Scheme</th>
<th>Cost to 2030</th>
<th>Cost to 2050</th>
</tr>
</thead>
<tbody>
<tr>
<td>Gatwick 2nd Runway</td>
<td>£10-13bn</td>
<td>£14-19bn</td>
</tr>
<tr>
<td>Heathrow NW Runway</td>
<td>£13-£18bn</td>
<td>£18-25bn</td>
</tr>
<tr>
<td>Heathrow Extended N Runway</td>
<td>£13-£18bn</td>
<td>£18-25bn</td>
</tr>
<tr>
<td>Inner Thames Estuary</td>
<td>£82-112bn</td>
<td>£93-125bn</td>
</tr>
</tbody>
</table>

I would like to apologise for this error and to confirm that our “Sift 3 Assessment Templates”, as referenced in our original letter and available on our website, were and are correct. I would be most grateful if you could share this correction with your members.

Yours Sincerely

Philip Graham
To:
Louise Ellman
Chair
Transport Select Committee
House of Commons
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SW1A 0AA

Sir Howard Davies
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Date: 21 March 2014

I am writing in response to your letter of 11th February following the Transport Select Committee session, which I attended on 20th January. Thank you for giving me the opportunity to explain our conclusions so far.

I respond to your points in turn below:

1. The Commission is carrying out additional feasibility and impacts analysis on the option of an inner Estuary airport over the coming months, the work for which we published draft Terms of Reference last month. On the basis of that additional work, the Commission will decide whether an inner Estuary option should be short-listed in September. If the Commission decides that it should, then it will be taken forward in the same way as the currently short-listed options at Heathrow and Gatwick. Since my appearance before your Committee, I have had one meeting with the Mayor on 4th March. We discussed work on the Estuary option and other aspects of our programme.

2. The Commission’s view is as set out in the interim report: that if a Thames Estuary airport were to proceed, the closure of Heathrow Airport would be likely to be required for commercial reasons, and the closures of Southend and London City for operational reasons. I believe my remarks to the Committee were consistent with that and they were certainly not intended to imply any alternative conclusion had been reached. I am sorry if I was unclear.

The airspace analysis informing the Commission’s view on Southend and London City is published in the document NATS Support to the Airports Commission (see in particular page 43). This can be found on the Commission’s website, by using the link ‘Long-Term Options: Consultancy Reports’ at the following webpage: https://www.gov.uk/government/
3. The advice which NATS provided in respect of air space for phase 1 is set out in its report, *NATS Support to the Airports Commission*, and summarised in the Interim Report. In particular, Box 6d on page 189 of the Interim Report gives a broad indication of the potential airspace impacts of some of the proposals for additional aviation capacity in London and the South East. ‘Appendix 2: Assessment of Long-Term Options’ sets out the Commission’s reasons for sifting out individual proposals.

4. The prime objective of the Commission’s demand forecasting in the first phase of its work has been to understand at national and regional level the potential for future growth in demand for aviation. We believe that the forecasting approach used, which was informed by responses to the Commission’s discussion paper on this issue, was entirely appropriate for this purpose.

There is significant uncertainty in any forecast, and this increases when forecasts are broken down to the individual airport level. Therefore it is important to look at the full range of potential outcomes, particularly where commercial factors may affect the level of demand at an individual airport. In the case of Stansted, this indicates the necessity of considering the Commission’s high demand scenario as well as its central forecasts. This scenario shows more rapid growth in demand, with the airport reaching capacity around 2030.

The Commission also recognises the need to understand better the drivers and effects of competition between airports and airlines. As part of the ongoing appraisal of potential schemes, the Commission will consider this issue and will use its analysis in conjunction with the existing demand forecasting methodology to inform the recommendations in its final report.

5. I attach separately a copy of the summary and conclusions of a round-table seminar that the International Transport Forum, which is part of the OECD, held on this subject, at which the Commission was represented. I attended part. The papers for this seminar are available online at [http://www.internationaltransportforum.org/trc/RoundTables/2013-Expanding-Airport-Capacity/index.html](http://www.internationaltransportforum.org/trc/RoundTables/2013-Expanding-Airport-Capacity/index.html)
6. The Commission’s legal advice on air service access at regional airports was provided in the form of comments on draft text and therefore cannot be directly shared with the Committee. I attach instead a paper describing the current policy and legal context and the Commission’s consideration of this issue. I trust this will provide the information you need.

7. In the second phase of its work, the Commission is continuing its dialogue with the airline sector. Members of both the Commission and its Secretariat have held meetings with both low-cost airlines and legacy carriers/airline alliances (including both SkyTeam and the Star Alliance). As for the former, we have met easyJet, Ryanair and Norwegian Air Shuttle. As part of the second phase of the Commission’s work, we will by carrying out additional analysis on the factors that might influence future choices made by airlines and alliances as to where to locate services.

8. The estimated infrastructure costs generated by the Commission in the first phase of its work for each of the proposals still under consideration are set out in the table below. These include surface access costs and allowances for risk and optimism bias.

<table>
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</table>

Additional information is provided in the ‘Sift 3 Assessment Templates’ published on our website.¹ The Commission will be preparing more detailed cost estimates for each of the short-listed options as part of the second phase of its work programme.

Please feel free to ask for any other details that you or your Committee need.

Yours Sincerely

Sir Howard Davies, Chair

Air Services Agreements at UK Airports

Introduction

The Committee raised the question of whether it would be possible and desirable for the UK to declare a unilateral “open skies” policy at regional airports, to facilitate their growth and enable them to open new routes.

The Commission received submissions suggesting this course of action in response to its call for evidence on the best means of making use of existing airport capacity, which it carried out during 2013. The Commission therefore examined this question as part of its work to prepare its Interim Report.

Background

For the most part, the air services market within the UK is already highly liberalised. The air services market within the European Union was liberalised over 20 years ago when the EU single aviation market was completed, and the market for services between the European Union and the United States was liberalised in 2007. The EU/US agreement means that EU and US carriers are free to operate between the US and any EU airport (including obviously any UK airport). Hence at present, a large number of routes operated from UK airports – and a significant majority of those operating at regional airports – are operated pursuant to either EU liberalisation or the EU/US agreement.

Under the EU single aviation market, UK carriers have the same rights within the rest of the EU as other EU carriers have within the UK. Conversely, the EU/US agreement does not place EU carriers on an equal footing with US carriers. So while US carriers may operate Intra-EU flights (flights between EU Member States), EU carriers may not operate intra-US flights (flights between points in the US). Although this imbalance clearly places EU carriers at some measure of disadvantage, the Commission has not encountered any evidence to suggest that it causes significant harm to the UK’s aviation connectivity at present.

Even outside these cases, where bilateral air service agreements are in place with states outside the EU single market, the UK’s policy is already highly liberal and rights to operate direct point-to-point services (“third and fourth freedom services”) between the UK and another state will usually be granted – without restriction on which airports in the UK may be served.. Such bilateral agreements are normally (though not exclusively) founded on the basis of reciprocal rights for UK airlines.
As in the case of third and fourth freedom air services, the UK Government’s position in respect of fifth freedom services (the right not only to operate into UK airports but also then to operate on to, and back from, a third country) is generally liberal, particularly in relation to regional airports. As recently as the 1990s policy was generally to refuse to grant fifth freedoms from UK airports, but since then policy has shifted towards liberalisation, beginning with a presumption in 2005 towards granting fifth freedoms from regional airports regardless of reciprocity. Regional airports, in this context, are those outside of the London & South East system (then defined as City, Gatwick, Heathrow, Luton and Stansted). However, one condition contained within this “general presumption” was that competition with UK airlines would not be distorted – for example, by an airline designated by another state to exercise the fifth freedom right being in receipt of state aid.

In 2011, the Government further extended its policy, so that the same presumption in favour of granting fifth freedoms that previously applied in respect of regional airports now applies in respect of Gatwick, Luton and Stansted. The general presumption, however, is still subject to certain caveats. These are articulated in the Government’s 2013 Aviation Policy Framework as follows:

“...the grant of such rights would be subject to a case-by-case consideration within the context of the current position in the UK’s bilateral aviation relationship with the country concerned (for example, we might not grant such rights if there were concerns that there was not a level competitive playing field in the market, such as if it were argued that the airline in question was in receipt of state aid that was distorting competition, or if the grant of such rights was felt likely to significantly diminish the possibility of securing a wider liberalisation that would deliver additional consumer benefits or if it was felt likely to result in significant and sustained disbenefits to consumers by restricting choice and value on a specific route).”

Commission’s consideration
Submissions on this issue to the Airports Commission recommended that the Government should abandon these caveats in relation to the granting of fifth freedoms. Despite the UK’s generally liberal policy, demand for fifth freedoms from less congested airports has remained extremely low. Some parties argued that this is because the UK’s caveats are a disincentive for airlines to apply to operate for fifth freedom services. The ability of UK airlines to raise objections to the granting of fifth freedoms out of UK airports is also cited as a disincentive. However, the Government is not bound to give effect to such objections. Other parties have presented evidence that the commercial case for many fifth freedoms (especially from regional airports) is often weak and that this presents the real disincentive for airlines to take them up. It is also the case that the third country concerned has to agree to the operation of such services by a non-UK carrier.
Recognising the potential benefits that fifth freedoms could bring to connectivity from less congested airports, the Commission examined whether it would be possible and desirable for the UK Government to further liberalise its policy and sought legal advice on this issue.

The Commission concluded that the UK's current caveats in relation to the granting of fifth freedom rights were consistent with general principles of competition law and modern practice in the negotiation of liberal air service agreements. Whilst there was no specific legal barrier to the Government further liberalising its policy towards fifth freedoms by abandoning the caveats, to do so could be contrary to the general principles of liberalisation and the protection of commercial entities from unfair competition, especially through state subsidy. In the light of those broader principles, the advice to the Commission suggested that a decision to allow an airline to exercise fifth freedom rights when in receipt of state aid (in the form, for example, of capital injections, cross-subsidisation, grants, guarantees, or tax relief or exemption) would be objectionable on competition policy grounds, even though not as a matter of law, in particular to UK airlines, which do not benefit from state aid.

The Commission therefore concluded that a unilateral and unconditional "open skies" policy, including fifth freedom rights at all or any of the UK airports would have the potential to harm the UK's aviation connectivity in the longer term. This was because it could undermine the competitive market in air services, particularly through causing harm to UK airlines and creating the potential for state aid assisted overseas carriers to eliminate competition on certain routes and then exploit this to the detriment of passengers.

Although the Commission could not, therefore, recommend a unilateral open skies policy for regional UK airports, this does not rule out the granting of fifth freedom rights at regional airports on a unilateral basis where such competition issues do not apply and services would be operated on a competitive commercial basis. The Commission strongly supports the highly liberalised position that the Government has already taken on this issue, and would encourage any application for such rights to be considered with an open mind.

In addition, the Commission intends to return to the issue of aviation connectivity for the UK's regions as part of its work ahead of the final report and the Commission's draft appraisal framework notes that proposals for adding new capacity will be assessed in terms of their implications for overall national connectivity.
Dear Sir Howard

Thank you for giving oral evidence to the Transport Select Committee on 20 January following the publication of the Airports Commission Interim Report. Committee Members and I found the session helpful in our ongoing scrutiny role. With that point in mind, I have several further questions of detail arising from the session which I hope you can clarify in writing for the benefit of the Committee:

1. Can you update the Committee on any follow-up meeting with the Mayor of London following our 20 January evidence session? Has any progress been made on agreeing how the Thames estuary option will be evaluated in the next stage of your work?

2. Can you clarify the position in relation to the closure of airports other than Heathrow—London City and Southend—if the development of a new airport in the Thames Estuary were to proceed? The Airports Commission Interim Report states that “it would be very challenging to manage the interactions between arrivals and departures at the new airport and those at London City, suggesting the latter would have to close” (para 6.38) and refers to “the likely closures of London City and Southend airports should an Estuary airport be taken forward” (para 6.40). At our evidence session, however, you indicated that such closures would not necessarily take place. Can you tell us what studies your team has undertaken to investigate the need for closure or otherwise?

3. Can you set out what work has been done to test the implications for air space of the various options, including those rejected at Stage 1?

4. We heard concerns about the robustness of your airport-specific demand projections in relation to Stansted. What steps are you taking to ensure that your Stage 2 modelling accurately reflects the commercial realities of airline decision making at specific airport locations?

5. You mentioned to the Committee that you had held a seminar with the OECD to discuss international airport issues. Are you in a position to forward us a copy of the proceedings?
6. You told the Committee that you had received legal advice on whether it is possible unilaterally to liberalise air service access to regional airports (para 5.93). Can you share that advice with the Committee?

7. Can you provide us with further details on your discussions with the airline alliances on relocating capacity to Gatwick? And have you discussed future capacity requirements with the low fares airlines?

8. Finally, you undertook to forward to the Committee details of the infrastructure costs of each of the proposals still under consideration, including the Isle of Grain option. Can we take up that offer?

I appreciate that those are detailed questions. Please take them as an indication of the weight that the Transport Committee and I attach to the work of your Commission.

Yours sincerely

Louise Ellman MP