



From the Parliamentary Under Secretary of State
for Corporate and Consumer Affairs

DEPARTMENT OF TRADE AND INDUSTRY

1-19 VICTORIA STREET

LONDON SW1H 0ET

Telephone (Direct dialling) 01-215 5662

GTN 215)

(Switchboard) 215 7877

Michael Howard QC MP

Mrs Lynda Chalker MP
Minister of State
Department of Transport
2 Marsham Street
LONDON
SW1

B/f S/11

30 October 1985

Dear Lynda

ECONOMIC REGULATION OF AIRPORTS

Our officials have discussed further the proposals outlined in your minute of 4 October to the Prime Minister. In the light of those discussions I can agree to your proposals, subject to the following points:

- File with on.*
- a) That the CAA's powers and duties should be extended to require transparency in the accounts of an airport undertaking, not simply as between different airports, but also as between the different activities of an airport. I understand that you have agreed to this.
 - b) That the CAA's general duty to further the reasonable interests of persons using airports for the purposes of air transport should be wide enough to cover those persons' interest in their capacity as users of all the services of an airport, and that it is to these criteria that the MMC will have regard in reporting on any matters referred to them by the CAA.
 - c) That the MMC should be able, in a report under a quinquennial review, to make a public interest judgement in respect of any aspect of an airport's activities, including aeronautical charges; and that the CAA's discretion to modify a recommendation by the MMC as to the level of such charges should be subject to:

CONFIDENTIAL

- 1 -



- i) its obligation to remedy or prevent any effects adverse to the public interest identified by the MMC;
- ii) tighter procedural disciplines, in the form of an obligation to give notice of the proposed modification, together with reasons for this, and to consider any representations or objections made within a designated timescale.

George Younger, in his letter of 21 October to Nicholas Ridley, queried the need for an overlap of responsibilities between the DGFT and the CAA. My view is that this is the most effective solution to the problem of regulating airports. Certainly, we should not impose additional regulation upon any industry if the normal competition legislation is adequate to deal with potential abuses of monopoly or anti-competitive practices. But the normal competition legislation was not designed to cope with "natural" monopolies in the private sector, and it is generally necessary to impose some more continuous and detailed regulatory mechanism. In the case of airports, the White Paper gave this role to the CAA. However, the dividing line between those activities which require special regulation and those which can be subject only to the normal competition legislation - never easy to draw - is even more difficult to set in the case of airports, because by international agreement the charges imposed for aeronautical services depend upon the level of profits made by the commercial services. It is necessary for the regulating authority to take a view on the appropriate balance between the contributions made to an airport undertaking's financing by the various activities.

It would be possible for the OFT and the MMC to look at these issues by means of a monopoly reference under the Fair Trading Act: but only if the reference covered the services of an airport as a whole. In the case of "designated" airports, that would involve an element of duplication with the quinquennial reviews which the MMC must in any case carry out on behalf of the CAA. It therefore seems most sensible to rely on the quinquennial review to look at the whole of these airports' activities. In these cases, the DGFT's powers under the Fair Trading Act and Competition Act remain as a "long stop" to deal with any problem which, in exceptional circumstances, the CAA might request the DGFT to look at (perhaps because the CAA considered that the complaint was more amenable to effective treatment under the competition legislation); or where a complainant is dissatisfied with action taken by the CAA. I regard some such "long-stop" as an important safeguard - though I hope it would not prove necessary to invoke it - against the possibility of "capture" of the CAA by the airports, especially in view of the CAA's commercial relationship with airports in the field of air navigation services.



In the case of non-designated airports within the regulatory framework, the CAA's powers will extend only to the core activities; and the competition legislation will be the only mechanism for examining an airport's activities as a whole. Some degree of overlap is therefore necessary in the case of the generality of regulated airports; and in the case of designated airports, whilst in practice it is not expected that the DGFT will wish to exercise his powers under normal cocompetition legislation, they remain as a backstop to deal with exceptional circumstances. On balance therefore, a degree of overlap seems inevitable.

I am copying this letter to the Prime Minister, to members of E(A) and to Sir Robert Armstrong.

*Yours ever
Michael*

MICHAEL HOWARD

Aerospace: Future of B.A. P.C. &

