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cc: B. Griffiths.

10 DOWNING STREET

6 December 1985

From the Private Secretary

Dear Richard,

ECONOMIC REGULATION OF AIRPORTS

The Prime Minister has seen your letter to me of 2 December. She is glad to know that the Department of Transport will be working to ensure that the British Airports Authority has every opportunity to become more efficient and profitable, within the constraints needed to prevent abuse of monopoly power.

I am copying this letter to the Private Secretaries to Members of E(A) and to Michael Stark.

Yours ever,
David.

DAVID NORGROVE

Richard Allan, Esq.,
Department of Transport

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ccBG



DEPARTMENT OF TRANSPORT
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David Norgrove Esq
Private Secretary
10 Downing Street
LONDON SW1

2 December 1985

Prime Minister 2
Evidence of your concern will
have done some good. Agree to
note now -

Dear David,

DLW 4/12

ECONOMIC REGULATION OF AIRPORTS

Your letter of 19 November recorded the Prime Minister's concern that the privatised British Airports Authority (BAA) should have the opportunity to become more enterprising and profitable than might be expected of a public utility. My Secretary of State shares this concern and is seeking to ensure that the arrangements for economic regulation encourage efficiency and profitability and are the minimum consistent with the need to prevent abuse of monopoly power.

The obligation on the regulator to secure "reasonable profits" was never meant to limit BAA's ability to make profits, rather to safeguard it: in order to make things totally clear, we now intend to avoid the term "reasonable".

However, there is a problem with our international obligations, principally the UK/US Air Services Agreement (Bermuda II) and the UK/US Memorandum of Understanding, signed in April 1983, which settled a legal action brought by US airlines against the BAA in respect of airport charges. These obligations appear to require a continuation of the BAA's present practice whereby, subject to achieving a reasonable rate of return on assets, they apply all of the profits of airport commercial activities (duty-free shops, restaurants, car parks etc) to reduce the traffic charges levied on airlines and their passengers.

We expect soon to consult the Law Officers on the extent to which our international obligations do in fact require this. My Secretary of State will keep the Prime Minister informed of developments. However, even if the "one till" doctrine (as it is called) has to be maintained, we still propose to give the BAA management incentives for efficiency through a price regulation formula; and their proven ability to earn good profits (even on the current cost accounting convention) should be enhanced

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by the opportunities they will have for developing commercial activities which are not primarily airport-related and which will be entirely excluded from regulation.

I am copying this to Private Secretaries to members of E(A) and to Michael Stark.

Yours,

Richard.

R A ALLAN
Private Secretary

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AEROSPACE

B.A. PTY

