

**Overall assessment: the public interest: summary of conclusions:  
the future**

**Overall assessment**

14.1. In the management of its affairs the British Airports Authority is continually faced with the need to decide between competing demands for limited facilities. All managers face such choices, but they are particularly frequent and difficult in the management of airports. The major airports inherited by the Authority are so sited that it is difficult to extend them (even if it were environmentally acceptable and economically sound so to do). All the Authority's airports were designed when air travel was the province of the few rather than the many, and the design and layout frequently inhibit development or expansion of the facilities (as in the Central Terminal Area at Heathrow). The growing demands on space in terminal buildings for operational use—for security, Customs and Immigration, the movement of passengers and their baggage—must be reconciled with each other and with the demands on space for commercial activities. The Chairman of the Authority told us

... the duty ... to provide proper facilities at the airports for passengers and cargo shippers must take precedence over commercial activities. Where considerations of space are concerned, commercial activities must take second place.

We believe that this attitude should be maintained in the future, particularly given the temptation which is likely to arise to put greater emphasis on commercial activities. However, the choice between operational and commercial needs is not black and white. Many commercial activities, although not strictly a pre-requisite for the safe and efficient movement of passengers, are seen by them as a basic necessity. It is commonplace that, as standards of living improve, yesterday's luxury becomes tomorrow's necessity. Air travellers in 1985 expect as a matter of course to find at an airport some catering and shopping facilities as well as adequate waiting areas and toilets. At the larger airports they will expect to find banking facilities, duty- and tax-free shops, and facilities for hiring a car and booking accommodation. The Chairman told us

It is very difficult to draw a line ... I cannot conceive that we could ever build an airport without certain commercial facilities which the average passenger today would demand ... So what are the basic requirements, and what are passengers' reasonable requirements, and what extra you provide is all very difficult to define, and it is changing all the time ... the nature of the traffic and ... the nature of the passengers and their requirements and their perception of what they ought to have, in five years in civil aviation changes dramatically.

14.2. It must also be borne in mind that those very circumstances which make it difficult to reconcile competing demands also provide an opportunity for exploitation. While in theory certain parts of an airport are open to all, it would

not be sensible to encourage people not involved in air travel to visit it in large numbers: to do so could seriously impede operations. The airside of an airport is accessible only to passengers and those who work there. Only passengers departing on international flights have access to airside duty- and tax-free shops. In practice an airport constitutes a closed market, in which monopolistic exploitation would be practicable.

14.3. These general considerations must be borne in mind in any attempt to assess how well—or badly—the Authority carries on its commercial activities. We have dealt in Chapter 4 with the difficulties of measuring performance by the available statistics, and we concluded there (paragraph 4.31) that the evidence is persuasive only in the case of rents. In this area, judged by comparisons made at Heathrow (which accounts for 72 per cent of the Authority's revenue from rents and services to tenants) the Authority can be seen to have done a little better than property owners generally, but not to such an extent as to justify any conclusion that it is abusing its monopoly position. For other sources of commercial revenue, movements in the figures over the past ten years can be largely if not wholly explained by extrinsic influences, and therefore provide no safe ground for assessing the Authority's performance. We must perforce make a more subjective judgment. This we base on all we have seen and heard during our inquiry: on our visits—and the visits of our staff—to the Authority's airports, and to a number of airports managed by local authorities: on our evaluation of the written and oral evidence given by the Authority and others and on our favourable assessment of the Authority's officers concerned with commercial affairs whom we met. We also bear in mind the limited range and extent of those matters about which, in the preceding chapters, we have been critical and have put forward suggestions for improvement. Taking all these together, it is our conclusion that the Authority has shown a generally satisfactory standard of performance of its commercial activities, although there is room for improvement.

### **The public interest**

14.4. Our terms of reference require us to consider whether, in relation to its commercial activities (excluding the application of the Authority's commercial revenues to finance non-commercial activities), the Authority is pursuing a course of conduct which operates against the public interest. The Act<sup>1</sup> specifies three heads under which such a course of conduct could arise:

- (a) Efficiency and costs. We have set out above our general conclusion that the Authority's standard of performance (ie efficiency) is satisfactory. We have not had any evidence to suggest that overall the Authority's costs could be materially reduced. We do not believe the Authority's attitude towards costs is such as to lead it into a course of conduct which operates against the public interest.
- (b) The service provided. We have pointed out several ways in which the service provided by the Authority in its commercial activities can be improved, particularly in relation to competition, but we received only a small number of complaints about it.
- (c) Possible abuse of a monopoly situation. The danger is real: and in a closed market such as is found at an airport there is always bound to be some

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<sup>1</sup>Section 11(1) Competition Act 1980.

suspicion of exploitation. However, while we have reservations about the Authority's attitude to competition, we do not think that so far it is acting in disregard of its duty as a public body.

We conclude that while there is scope for improvement in the service provided by the Authority in its commercial activities it is not, in relation to those activities, pursuing a course of conduct which operates against the public interest.

### Summary of conclusions

14.5. Our terms of reference require us to consider whether, in relation to its commercial activities, the Authority could improve its efficiency, or reduce its costs, or improve the service provided, with particular reference to:

- (a) the scope for increasing competition at the point of sale, having regard to security and safety requirements and the need to ensure the comfort and convenience of passengers and the efficient operation of the airport;
- (b) the methods and practices of the Authority in selecting the persons to whom concessions are to be granted including the Authority's procedures for inviting and accepting tenders, the imposition on concessionaires by the Authority of contractual terms relating to the price, nature, range and quality of the goods and services to be provided by concessionaires and the award and renewal by the Authority of contracts;
- (c) the monitoring and control by the Authority of the standard of services provided to passengers by concessionaires;
- (d) the administration and management by the Authority of leases of land where the Authority is the lessor.

The extent to which the Authority could in our judgment improve its efficiency, reduce its costs or improve the service it provides appears from our conclusions in Chapters 4 to 13, of which the following is a summary.

## Summary of Conclusions

*Recommendation  
Number*

*Paragraph  
Number*

### The role of the BAA Board

1. BAA encourages its part-time Board members to take an interest in specific activities according to their individual expertise and experience. There is at present no member with retailing experience, despite the scale of BAA's commercial activities. An increase in the size of the Board would give an opportunity to appoint such a member. We recommend such a change. 5.44
2. The Board should, in approaching a decision on the provision and allocation of space in new and redeveloped terminals, tell the Executive what range of options should be considered, and require the Executive to demonstrate that the full range of commercial possibilities, within the constraints imposed by physical conditions, has been explored. 5.45

### Planning Guidelines

3. **Planning Guidelines, which are currently being updated after seven years, should be updated more frequently. Care should be taken to ensure that they are appropriate to facilities on the scale likely to be planned.** 5.46

### Targets

4. **The Board will be able to set feasible but more challenging targets for commercial performance for the year ensuing if it can achieve greater understanding of the relative roles of, on the one hand, managerial effectiveness and other factors largely under BAA's control, and, on the other hand, those external factors which are largely outside its control.** 5.47

### Organisation

The organisational changes resulting from 'Chewton Glen' reinforced BAA's trend towards decentralisation, with the exception of the new arrangements for the organisation of commercial functions which went against this trend. On BAA's own admission, it is too early to be sure that the new commercial organisation fulfils Chewton Glen's hopes. Accepting that, the Chewton Glen decision on commercial matters seems to us to have been soundly based. 5.48

5. **In setting up the Trading Department, the Commercial Development Director has given priority to the retailing activities at terminals. In due course it will be necessary to ensure that the potential of other commercial activities including, for example, car parks, cargo and property receives the attention already given to retailing.** 5.49

6. **The division of responsibility for commercial performance between the Trading Department and the airport managements is currently being debated within BAA. We consider that the present arrangements are satisfactory. The Commercial Development Director should retain his responsibility for advising BAA on the exploitation of all commercial potential, and the Director or General Manager of an airport should have final responsibility for all activities at his airport.** 5.50

### Information and computing

BAA has in recent years noted deficiencies in the management information relevant to its commercial activities and has developed, or begun to develop, new systems to remedy these deficiencies. 6.30

Continuing difficulties with the property system suggest that not all the problems identified in the 1983 review of the whole of the Authority's information processing strategy have been solved. 6.31

At an early stage in our inquiry the Authority admitted to 'serious...concern' over its new computerised property management system. From BAA's own statement on the present position past mistakes are evident, and most important and urgent decisions, particularly concerning Heathrow, remain to be taken. BAA is now seeking information about computerised property management systems recently developed elsewhere. 6.32

7. **In view of our proposal that final responsibility for all activities at an airport, including Trading and other commercial activities, should remain with its Director or General Manager, it will be**

necessary to ensure that the new computerised Trading Information System meets the specific requirements of the airport management responsible for Trading performance.

6.33

**Finance**

BAA did not achieve the targets set for it by the Government for the period 1980-81 to 1982-83, when traffic growth was less than had been expected. It expects to achieve the targets set for the period 1983-84 to 1985-86.

7.52

**Budgets**

The fact that the Authority has exceeded its concession income budgets and kept within its expenditure budgets during recent years may suggest that its budgets should be made more rigorous and challenging. We recommend that it reviews its budget-setting procedures accordingly.

8.

7.53

**Presentation of results**

A substantial proportion of the Authority's expenditure is not directly attributable to particular activities and an element of judgment therefore enters into the allocation of that expenditure, which may affect the extent to which the reported results for each activity are meaningful. BAA told us that this would not affect its traffic charges but we nevertheless consider it important that the Authority's results from particular activities at different airports should be reported more accurately and as clearly as possible. The Authority is making changes to this end, particularly in the development of its new 'general ledger' management accounting and information system. We accept that the Authority is correct to treat expenditure on such items as terminal concourses, roads and airport administration as wholly attributable to traffic operations even though the first two are also used to give access to commercial facilities. To do otherwise would imply that commercial activities were of comparable significance to the Authority's primary objective to operate, plan and develop its airports so that air travellers and cargo may pass through safely, swiftly and as conveniently as possible.

7.54-7.59

9.

We consider that a distinction can and should continue to be drawn in the Authority's accounts between the results of its traffic operations and its commercial activities at each airport. This should continue to apply if privatisation takes place, so that the extent of subsidisation of traffic operations by commercial activities and of one airport by another is disclosed.

7.59, 7.60

10.

We recommend that the Authority should show separately in its published accounts for particular activities at airports the contribution made by each activity first to the Authority's non-specific expenditure and profits and overhead expenditure and secondly to the Authority's trading profits or losses after deducting from those contributions an allocation of its non-specific expenditure made on a 'best judgment' basis together with an explanation of the basis used.

7.61

**Internal audit**

11.

While we have no reason to believe that posts in the internal audit branch are not correctly graded, we hope that the Authority will keep

**under careful review the grading of internal audit staff, including the Chief Internal Auditor, so that the branch can operate effectively and carry appropriate weight in its dealings with operational management.**

7.62

12.

We found the general organisation and operation of the internal audit function to be satisfactory (although response times were tending to lengthen). But the efficiency of internal audit depends not only on a sound structure but on continued support being given by the Managing Director and senior management. **We therefore consider it desirable that the Chief Internal Auditor should report directly to a Board member. The Audit Committee should become more closely involved in overseeing the internal audit function.**

7.63

#### **Investment appraisal**

Our examination of the appraisal of a number of investment projects indicates that the majority of investments have been subject to formal investment appraisal. The recent adoption of revised guidelines for project assessment should, however, lead to some improvement in the techniques of investment appraisal, particularly as applied to smaller projects.

8.21

In particular, the standard of investment appraisal should benefit from a wider quantification of available options; from a greater use of sensitivity analysis; from a more systematic assessment of non-financial benefits; and from a regular programme of back-checks as proposed in the revised guidelines.

8.22

13.

No separate appraisal is carried out of the commercial content of the major 'combined' investments. BAA argued that options for provision of commercial facilities have been constrained by the nature of the sites available. We believe this argument can be overstated. **Where there are options for the provision of commercial facilities in these major developments, these options also should be subjected to a formal economic appraisal.**

8.23

#### **Concessions**

Five-year contracts may not be in the best interests of the concessionaires; nevertheless, given the nature of the monopoly rights granted by BAA, **we think that all contracts should remain subject to regular tendering.**

14.

9.24

15.

**We consider that the question of capital investment by catering concessionaires should be kept under review in the light of the outcome of BAA's recent proposals to provide them with a greater incentive.**

9.24

#### **Property management**

Examination of files and discussions with airport staff showed that the policies and procedures for leasing were being followed in detail.

10.29

Present vacant office accommodation at Heathrow and Gatwick represents a small proportion of total office accommodation at the two airports, and is projected by BAA to be fully absorbed within five years. The increase in rents at Heathrow has been greater than the national average and the level of rents at the airport is generally above that in surrounding areas. BAA policy for determining rental levels appears reasonable.

10.30, 10.31

**Aircraft fuel supply**

16. The new fuel agreement at Heathrow makes provision for the entry of new suppliers to the hydrant consortium. It will be easier to judge the effectiveness of this provision when the result of British Airways' application to join the consortium is known. **BAA should increase competition in the supply of fuel at Gatwick when the present fuel arrangements are re-negotiated.** 10.32

**Competition**

The extent of competition at point of sale is limited by the lack of space within the airport terminals.<sup>1</sup> Nevertheless even where competition would be possible, either directly or through promotional activities, BAA effectively restricts or prevents it. BAA believes that it has an obligation to offer a considerable degree of protection to concessionaires who, through competitive tendering, have won the right to trade. BAA also believes that consumer choice is better secured through a variety of products for sale than through duplication of suppliers and tries to ensure by price regulation and other controls over concessionaires that customers get value for money.

11.66, 11.67

We do not find these arrangements fully effective. In order to increase competition we recommend that the Authority:

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17. (a) continues to make every effort to attract a greater range of tenderers with a view to reducing the present concentration of concessions among a small number of firms, and thus providing a better spread of experience on which to judge concessionaires' performance; 11.68
18. (b) should seek to ensure that full information is provided at the outset, and that the time allowed for the preparation of the tenders is adequate for new tenderers; 11.69
19. (c) should allow Skyshop concessionaires to trade under their own names in the interests of staff motivation and customer service; 11.70
20. (d) should review the terms of its car hire concessions to ensure that customers are charged on a basis appropriate to the type of hire involved; 11.71
21. (e) should facilitate competition in car rentals, allow off-airport car hire operators to advertise without discrimination and provide adequate generic signposting and coach pick-up facilities; 11.71
22. (f) should cease its present practice of discriminating against advertisements at its airports for off-airport competitors to its concessionaires; 11.72
23. (g) should arrange matters so that in any Heathrow terminal an airline without rights to handle its own traffic has a choice of at least two handlers neither of which is an airline with which it is in direct competition; 11.75
24. (h) should, in determining the arrangements for ground handling at Heathrow, not limit its consideration to airlines with existing self-handling rights and should take account of the charges made to airlines and the cost savings achievable; 11.75

<sup>1</sup>The Chairman said, however, he hoped that in the development of Terminal 4 at Heathrow enough space would be available, for the first time, to introduce competition in catering. When our report was nearly complete BAA told us that all the catering outlets in Terminal 4 had nevertheless been let to a single concessionaire, who does not hold a catering concession at any other BAA airport.

<i>Recommendation Number</i>		<i>Paragraph Number</i>
25.	(i) should, on the expiry of the present Aer Lingus contract, open the opportunity to tender for the position of nominated handler to any airline using Heathrow (whether or not that airline currently has handling rights) and to any outside handling agency;	11.76
26.	(j) should allow airlines with handling rights at Heathrow to undertake business in any terminal, particularly where this would improve utilisation of equipment: to this end the Authority should survey with the Airline Operators Committee the utilisation of equipment and staff at Heathrow and the charges made; and	11.77
27.	(k) should take advantage of the opening of the North Terminal at Gatwick to invite tenders for additional handlers and should establish the degree of choice set out in (g) above.	11.78

#### **Basis of tendering**

The general form of a concession and the basis upon which tenders are judged benefits BAA rather than the consumer. This is consistent with the Authority's policy to maximise revenue but may not be consistent with its obligations as a public enterprise. An alternative approach might be to let concession contracts on a different basis, for example a fixed rental and prescribed standards of service, tenders being judged on the lowest prices proposed to be charged to customers.

11.79

#### **Air traffic services**

28. It might be difficult to introduce a contractor other than the CAA in the London area. We recommend, in view of the potential reduction in costs to airlines, that the Authority should consider employing another contractor at its smaller airports.

4.30

#### **Manpower efficiency**

It has not been possible to apportion accurately the man-hours spent on commercial activities but we have seen no evidence of over- or under-staffing. We are satisfied that the downward pressure on staffing stemming from performance targets has been effective. Our judgment is that there is a high level of expertise and effectiveness among BAA's staff responsible for its commercial activities.

12.21

#### **Staff training**

29. The Authority has devoted considerable resources to staff training during the past three years. We hope that it will be able to carry out an objective assessment of the effects of this training.

12.22

#### **Industrial relations**

BAA has a satisfactory industrial relations system and we have been aware of a feeling of common purpose among all staff engaged in commercial activities.

12.23

#### **Quality of service**

BAA considers that in the medium to long term the maintenance or increase of commercial revenue is an indication of satisfactory service. We accept that an increase in such revenue resulting from an increase in the goods and services bought per passenger is one indication that passengers find those goods and services attractive.

13.36

<i>Recommendation Number</i>		<i>Paragraph Number</i>
30.	The quality of service associated with specific commercial activities may differ significantly. <b>BAA must therefore continue to look separately at the individual performance of specific activities.</b>	13.37
	<b>Performance indicators</b>	
31.	Available statistics do not provide a satisfactory guide to BAA's performance of its commercial activities. <b>We recommend that further effort should be devoted to the establishment of meaningful performance indicators.</b>	4.31, 4.32 4.33
32.	BAA is placing increasing emphasis, in its monitoring of commercial services, on passenger opinion surveys. <b>The results of these should be made available, as a matter of routine, to the Passenger Services sub-Committee at each airport.</b>	13.38
33.	<b>Passenger Services sub-Committees should continue to represent passengers' interests.</b> Given the variety of roles which an airport Consultative Committee is required to play, <b>consideration should be given to increasing the independence of the Passenger Services sub-Committees by separating their funding and the appointment of members from those of the Consultative Committees.</b>	13.39

### **The future**

14.6. We have examined the Authority as it has been and as it is now, and our recommendations for change relate to the present organisation. We cannot, however, ignore the announced policy of the present Government to bring about a major change by the early privatisation of the Authority. Indeed, this policy was translated into a detailed programme of action in the White Paper 'Airports Policy'<sup>1</sup> published on 5 June 1985 during the course of our inquiry. We have therefore thought it right to examine our recommendations in the light of the White Paper. As a result, we have concluded that, although they are made in respect of the existing organisation, we have no reason to believe that the general sense of our recommendations will be found inapplicable to the new organisation envisaged.

14.7. The captive nature of the concessionaires' market, and the airlines' pressure to maintain the existing degree of cross-subsidy between commercial and non-commercial activities, already encourage the Authority to exploit its commercial opportunities. While it is not for us to comment on the new arrangements proposed in the White Paper, we think it right to draw attention to the additional pressures which might be generated by the search for a high rate of return to shareholders in the new enterprise: pressures which will make it even more difficult for the Authority's successor to hold a proper balance between an entrepreneurial approach to commercial activities and a possible abuse of a monopoly position.<sup>2</sup>

<sup>1</sup>Cmnd 9542.

<sup>2</sup>BAA told us that its commercial activities were not being affected by the prospect of privatisation. The Authority did express concern about the demands for operational space posed by the continuous and rapid growth of passenger numbers. The Managing Director told us he was '... very worried about the huge surge of passenger traffic which we are experiencing ... The balance ... is, if anything, stacked against the ability for commercial activities to get into new areas or new parts of the airport ... Given our prime responsibility is the processing of passengers and freight and airlines, if there is ... a conflict it may well be that we will have to cut back on some of the space allocated to commercial activities'. However, another strand of thought about the future appears in the Trading Department's Marketing Plan Summary 1985: 'it is a safe assumption that 'privatisation' will result in an increased prominence of the profit-earning commercial functions'.

J G LE QUESNE (*Chairman*)

PATRICIA MANN

B C OWENS

J S SADLER

D P THOMSON

Professor K D George, being a member of the Group, dissents from the conclusions for the reason set out in this report

N E D BURTON (*Secretary*)

*2 September 1985*

### **Note of Dissent**

**by Professor K D George**

I agree with the conclusions that have been arrived at by my colleagues except with respect to one matter, which is the public interest finding on the way in which BAA has effectively restricted or prevented competition to its concessionaires even where such competition would be possible. I conclude that in this respect the Authority has been pursuing a course of conduct that operates against the public interest. A partial remedy of the situation would be for BAA to be obliged to implement the relevant recommendations made in this report.

K D GEORGE

*2 September 1985*