

# **Report of the strategic review of the CAA**

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Department for Transport  
Great Minster House  
76 Marsham Street  
London SW1P 4DR  
Telephone 020 7944 8300  
Website [www.dft.gov.uk](http://www.dft.gov.uk)

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## FOREWORD

When I was asked to conduct this strategic review, I knew very little about aviation in the UK, save as an ordinary customer, and nothing at all about the Civil Aviation Authority.

I quickly realised that there had not been a comparable review in anyone's memory and that the Authority had been in existence for a very long time by the standards of the country's regulators. As indicated in Chapter 2 of my report on the CAA's general standing and performance, the evidence showed equally quickly that the CAA had been and continued to be a highly successful organisation. Our safety record in the UK, for example, is so good that for the superstitious it seems better not to mention it. As the report explains in more detail it is therefore concerned with suggestions to improve a high quality regulator. There was some scope to identify and propose modernised and improved arrangements simply because the review was not covering well-trodden ground.

The recommendations are mine and I accept complete responsibility for them but I have needed and received a great deal of help.

I am grateful to all the individuals and organisations listed in the report who have provided the evidence on which the thinking is founded. The list does not show, but it is natural because of their close interest, that far and away the most extensive and continuous help has come from the Department for Transport and the CAA itself. Many people from both organisations have written papers and talked to me. The Department and the Authority showed skill and determination in putting over their respective points of view matched by an understanding that in the end I had to make up my mind and take responsibility for what I said.

I am greatly in the debt of Lyn Bicker who helped us to design and then facilitated the four dialogues described in the report which were an indispensable part of the evidence-gathering.

My greatest debt is to the team of three people who have helped me throughout the work. Adrian Brett was seconded from the CAA. He provided a vital link to them and gathered much of the key evidence from the Authority. He documented and retained a systematic mastery of all the evidence from whatever source. He rose to the challenge of a potential conflict of interest. He supported the CAA and the review with obvious integrity. Hugh Westaway brought to our work the extensive experience of aviation that I conspicuously lacked. His insights helped me to evaluate what I heard and saved me from rushing into wrong conclusions on many occasions. Phil Killingley from the Department was the Secretary and has written the great majority of the report. He has given time and energy unstintingly to the review. I have relied on his efficiency; experience taught me to have high regard for his judgment. I could not have had better help than from this team.

Joe Pilling

26 June 2008

## THE CAA – THE UK’S INDEPENDENT AVIATION REGULATOR

### Main functions:

- safety regulation of civil aviation in the UK
- determining policy for the use of airspace
- economic regulation of designated airports and en route air traffic services
- licensing of airlines in relation to their finances
- licensing of air travel organisers
- provision of independent policy advice on aviation to Government

### The CAA regulates approximately:

50,000	Active professional and private pilots
12,400	Licensed engineers
2,350	Air traffic controllers
206	Air Operator Certificate holders
141	Licensed aerodromes
950	Organisations involved in design, production and maintenance of aircraft
2,400	ATOL holders
150	Operating licences (airlines)
19,000	Registered aircraft

### The CAA employs:

Over 900 (FTE) staff including about:

70	Professional pilots
3	Test pilots
31	Air traffic controllers
180	Qualified engineers
10	Doctors
5	Nurses
7	Economists
11	Qualified accountants
7	Lawyers
10	Technical researchers

The CAA was created in 1972. Since then, there have been many developments both within the organisation and in aviation more generally. These are set out in Annex A.

## 1 INTRODUCTION

1. The Civil Aviation Authority is the UK's aviation regulator. Its activities include economic regulation, setting airspace policy, safety regulation and consumer protection.
2. The House of Commons Transport Committee report – “The Work of the Civil Aviation Authority” – recommended that the Department for Transport should carry out a review of the Civil Aviation Authority.<sup>1</sup> The Secretary of State for Transport accepted the recommendation and commissioned me to conduct an independent strategic review of the organisation. Having received terms of reference in September 2007, the review began in October 2007, and I was asked to report back to the Secretary of State in the course of 2008.

### SCOPE AND CONTEXT

3. The review's terms of reference are set out below. Shortly after the review started, I was also asked to look at the role of the CAA in respect of passengers.

### Terms of reference – Strategic review of the CAA

Following a recommendation of the House of Commons Transport Committee, this review will consider the structure, scope and organisation of the Civil Aviation Authority (CAA) with a view to ensuring that the UK's arrangements for aviation regulation and policy making are fit for purpose and able to meet current and future challenges.

The Transport Committee said: "*While operating generally well against its remit, our inquiry identified a number of challenges for the CAA resulting from the ongoing development of the UK aviation sector.*"

The review will begin in October 2007 and conclude in 2008. Its report will be made available on the Department for Transport website. It is complementary to (but separate from) the Competition Commission enquiry into BAA, which may comment on CAA's specific powers for the economic regulation of airports.

(continued)

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<sup>1</sup> The Work of the Civil Aviation Authority – Transport Committee – November 2006

The review will be principally focused on

- the strategic and operating context for aviation regulation in the future, including
  - economic and environmental challenges as defined by the Eddington Transport Study and the Stern Review on the Economics of Climate Change
  - aviation industry developments and
  - evolution of the roles of ICAO and Europe in aviation regulation.
- what should be the functions and responsibilities of the CAA?
- the structure of the CAA including governance and statutory framework
- the CAA's relationship with Government and
- the CAA's relationships with those whom it regulates, including funding mechanisms, and more generally with aviation stakeholders.

In considering the above the review should consult stakeholders. It should make some comparisons with other regulators. The review will make recommendations to Ministers about the structure and functions of the CAA; and will also look for ideas as to how the way the CAA carries out its functions can be improved for the future.

4. Naturally the terms of reference have very much influenced the ground covered by the report but, when in doubt, we have also taken account of the volume and nature of the evidence we have received.

5. During the review all the interested parties have carried on their normal business. There have been a number of high-profile events. There has been the issue of the designation or de-designation of Stansted and Manchester airports, and the price cap review of Heathrow and Gatwick. The Department for Transport in October 2007 issued a paper on the end-to-end air passenger experience, concentrating on Heathrow, and consulted on the expansion of Heathrow. The Transport Committee held an inquiry into BAA and is now examining the problems encountered around the opening of Terminal 5. A British Airways Boeing 777 landed just short of the runway at Heathrow in January. NATS launched the largest ever consultation for airspace change in February. The Competition Commission's study of BAA continues and the Secretary of State has set up a review into the economic regulation of the UK airport system, with an advisory panel chaired by Professor Cave. The EU-US Open Skies agreement came into force and the ATOL scheme was reformed after 30 years.

6. This review has sought to avoid being drawn onto ground being covered by others. We have listened carefully to everything that has been said to us but we have kept our eye on what the terms of reference require us to consider and, in particular, we have tried to avoid being distracted from the strategic and long-term issues by all that has been said to us about current issues.

## EVIDENCE

7. A full list of those who contributed evidence to the review is at Annex B. The review began by asking for written evidence from the aviation community. A wide range of written material was provided from 60 organisations and individuals. The written evidence provided the initial base for the review to map out in some detail the ground that needed to be covered.
8. It was important that the review met stakeholders face-to-face to enable them to contribute their views in person. To this end, the review held 38 oral evidence hearings with the aviation community and other CAA stakeholders, and four dialogue events with about 15 people at each. These sessions enabled the review to clarify its thinking on existing lines of enquiry and add to these where new ideas emerged.
9. The oral hearings gave the review the chance to test ideas by posing questions to stakeholders, examining their views on the CAA and generally refining lines of enquiry.
10. The purpose of the dialogues was to hear from those who had not contributed written evidence to the review and from those who wanted to supplement their written evidence. The interaction of various stakeholders was designed to prompt thoughts that otherwise might not have emerged. They offered a chance for the aviation community to cross-examine the ideas of others and for the review to hear these challenges. A staff member of the CAA attended each dialogue. This was in order to respond to factual queries or correct factual inaccuracies about the organisation, rather than to contribute to the debate.
11. The first dialogue was on aviation in 2020 and its regulation by the CAA. Its aim was to consider the likely changes in regulation over the coming years, to work towards an ideal or a likely picture of how the CAA would operate in the future. The second dialogue focused on the sum of the CAA's roles and responsibilities, and on how people thought these should change. The third dialogue was also on the CAA's responsibilities, but specifically in respect of passengers. The fourth dialogue took a general overview of the way the CAA operated, including its costs, charges and financial arrangements, its interaction with stakeholders, and its effectiveness as a regulator.
12. In the initial stages of the review, while waiting for evidence to come in from stakeholders, we met each of the CAA's four regulatory groups and its corporate group in order to learn about their work. Towards the end of the review, when evidence had been collected and analysed closely, we returned to the CAA in order to give it the opportunity to respond to a wide range of points. We spoke to the Department for Transport, and a number of other Government Departments and European institutions. We also met several regulators in other sectors to understand their approaches to regulation. In total, 96 organisations and individuals gave evidence to the review.
13. Since the review was set up, we have carried out investigations on the main areas indicated in the terms of reference. These have focused on comparing the CAA with other regulators in a number of fields (for instance, corporate governance, appeals, statutory roles) and contrasting what happens in the CAA against other sectors and other countries. Along with the evidence from stakeholders and the comments from the CAA, these investigations have shaped the structure of the report and the review's recommendations.

14. The review received evidence on trends and specific developments in the aviation community and in regulation that might impact on the CAA's future work. These are set out in Annex C. We believe that three issues will become increasingly important for the CAA over the next five to ten years – the environment, the international dimension of aviation policy-making, and the interests of passengers/consumers.

15. As readers will see, evidence reported to us is reflected throughout the report. Despite this, some witnesses may be disappointed to see that points that they raised are not dealt with or are not dealt with in detail. In some cases we had to make a judgment that a point was not within our terms of reference or was not strategic.

## 2 GENERAL STANDING AND PERFORMANCE

### GENERAL STANDING

16. The review coincided with controversy about the CAA's economic regulation. We heard a large volume of strongly expressed criticism about that. The nature of the review meant that, prompted or unprompted by the questions, we also heard many other criticisms of different areas of the CAA's work. In the report we aim to deal with all the significant criticisms and suggestions for change that were within our terms of reference. We recognise that a proportion of the criticisms and suggestions we received came from organisations or individuals who were pursuing an agenda not directly connected to our review. Nevertheless, despite the controversy and the invitation to be critical, the strongest message we received from almost all our witnesses is that across its functions as a whole the CAA is a high quality organisation much respected for what it has done over the last 36 years and for its current capability.

17. Aviation is by definition an international business. It comes naturally to those who work in aviation to make international comparisons. No single witness suggested to us that the aviation regulator in any other country was better than the CAA. Few suggested that there was another regulator as good as the CAA. The preponderant view, which was significant even after aiming off a little for understandable national loyalty, was that the CAA is the best aviation regulator in the world.

18. The starting-point for my report is that the CAA is a world-class regulator. It follows that the recommendations are not concerned with rescuing a failing organisation. They are intended to help a good organisation to become even better.

19. In view of the positive accounts of the CAA that we heard, it is worth explaining that there are two main reasons why I have concluded that there is still scope for further improvements. First, the CAA is a longstanding regulator by any standards. This is the first strategic review of the CAA as a regulator since it began work in 1972. Of course, there have been many changes since 1972 but its framework and approach could arguably be modernised and improved, taking account of the lessons to be learned from relative newcomers in the regulatory field.

20. Second, a long record of success always brings dangers in its wake. Change comes more easily as a response to disaster and failure. It is hard to resist the temptation to stick to a formula which has been proved to be successful. But aviation is a fast-changing sector and, if anything, the pace of change is increasing rather than slackening. The pace of change in the wider context, including concern for the environment and the growing role of Europe both within and beyond the EU itself, is at least as fast. I intend that the changes I propose will not only help the CAA to make some changes in the short to medium term but also help it to respond to continuing change in its circumstances in the longer term.

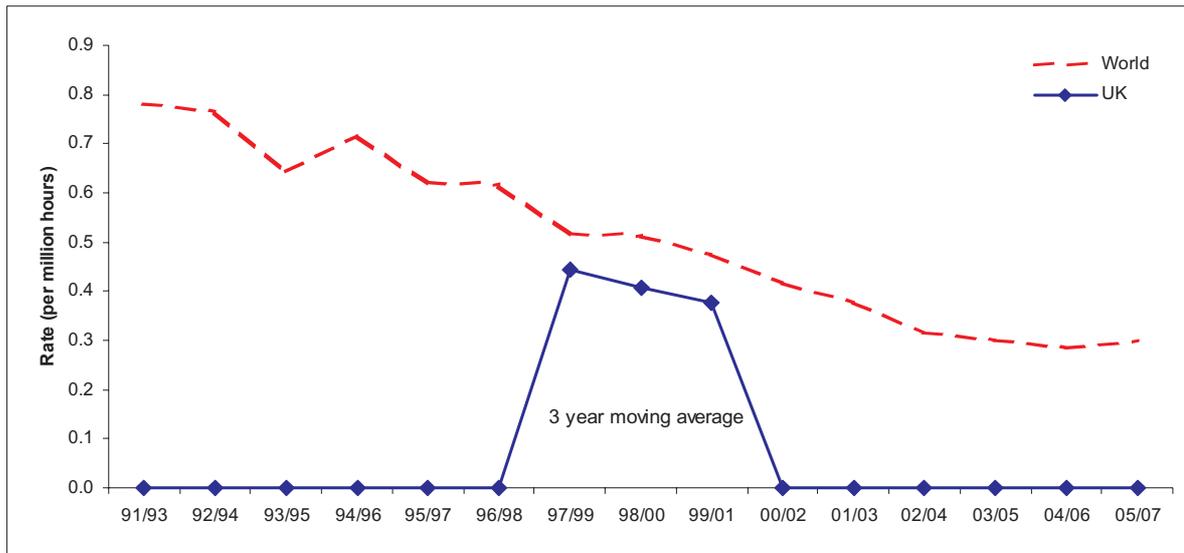
### PERFORMANCE

21. Many of the CAA's activities are not amenable to objective measures of performance, but there are some important areas in which useful performance

indicators can be drawn up. These are agreed by the CAA and DfT, and included in the annual report and accounts.

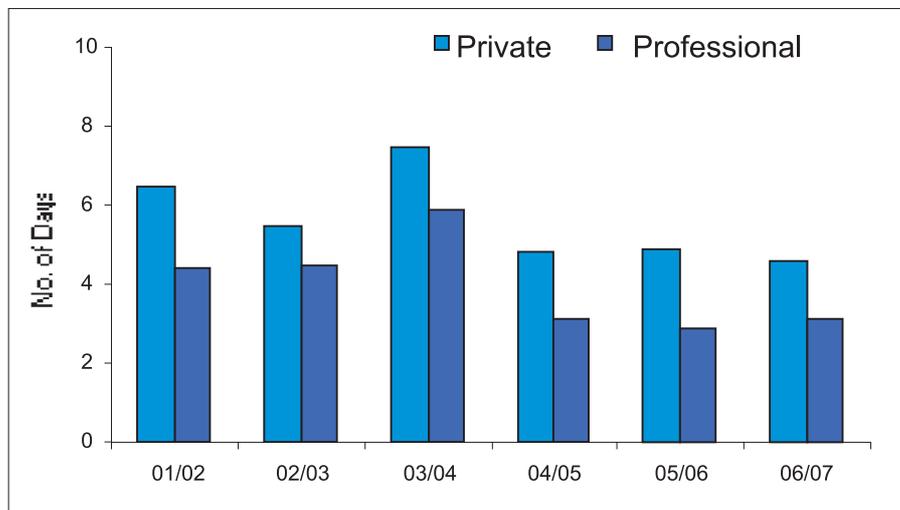
22. One of the most significant indicators is for safety. Although this is not a direct measure of the CAA's performance as a regulator, it is clear that under the CAA's regulation UK aviation has achieved one of the highest levels of aviation safety in Europe. For example, the CAA's statistics, as indicated in the graph below, show the UK and worldwide fatal accident rates for large transport jet aircraft in the last 15 years. The UK accident rate is about six times better than the world average.

**UK fatal accident rate for large transport jet aircraft**

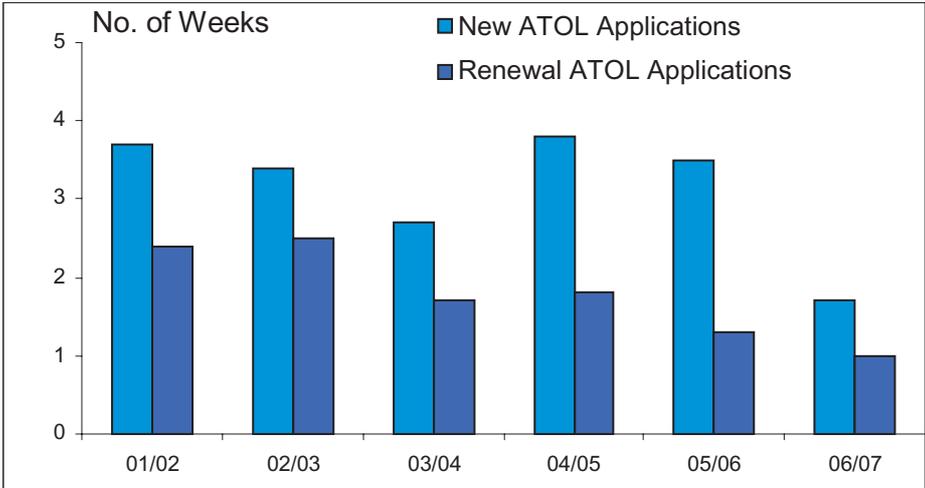


23. Where objective measures are available, it is also apparent that the CAA has improved its service delivery performance. For example, the time taken to issue pilot licences and approve ATOL applications has gone down significantly over the last five years, as shown in the two bar charts below.

**Number of days to issue pilot licences**

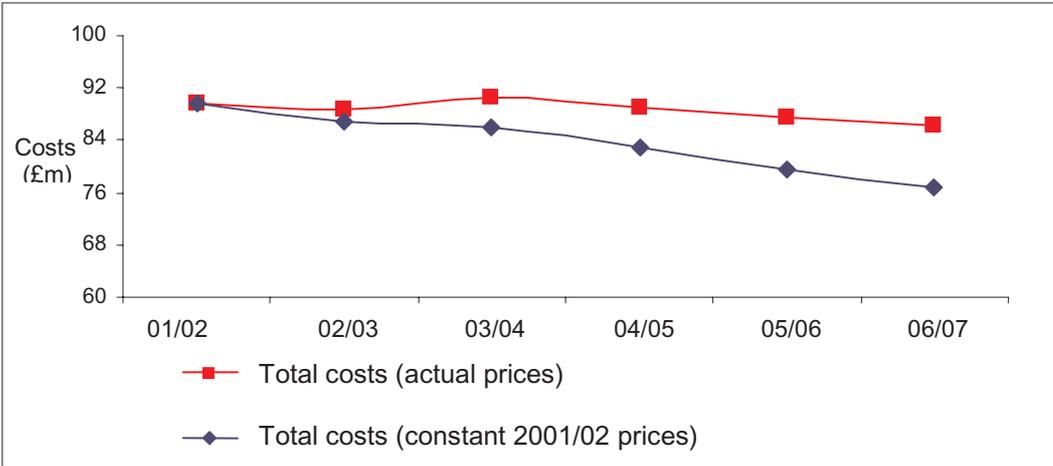


**Number of weeks to issue ATOL licences**



24. Another important indicator of the CAA’s performance is its total and unit costs over time. The CAA has significantly reduced its total operating costs in both actual and constant prices over the years 2001/2 to 2006/7. When combined with the continued growth in aviation activity, the CAA’s unit costs have fallen even more rapidly during this period. The result of this is that if passengers on commercial flights were paying the CAA’s full cost it would now be equivalent to about 30 pence per passenger journey.

**CAA’s total costs from 2001/2 to 2006/7**



### 3 ROLE AND STATUS

#### CAA ROLE

25. The CAA works within a regulatory framework which includes international standards set by the International Civil Aviation Organisation, European and UK legislation. The main legislation that defines the CAA's role is set out below.

#### Main UK primary legislation defining the CAA's role

**The Civil Aviation Act 1982** gives the CAA a role in

- licensing air transport
- licensing the provision of accommodation in aircraft (air travel organisers' licensing)
- licensing and operating aerodromes<sup>2</sup>
- providing air navigation services<sup>2</sup> and
- providing assistance and information to the Secretary of State.

Many of the CAA's functions and duties, especially for safety, are prescribed in secondary legislation made as Air Navigation Orders under section 60 of the Civil Aviation Act 1982

**The Airports Act 1986 Part IV** sets out the CAA's role for the economic regulation of airports

**The Transport Act 2000 Part 1** sets out the CAA's role in regulating air traffic services (other than safety) and the CAA's air navigation functions

**The Civil Aviation Act 2006** section 8 gives the CAA responsibility for the health of people on board aircraft.

<sup>2</sup> Whilst the Civil Aviation Act conferred service provision activities on the CAA, including aerodrome operation and air traffic management, all such activities have been disposed of.

### Main European Regulations with a bearing on the CAA's role

**EC Regulation 216/2008** sets common safety rules for civil aviation and establishes the European Aviation Safety Agency. UK legislation designates the CAA as the UK National Aviation Authority for the purposes of this regulation.

**Four EC Regulations** establish Single European Sky – the European Community's programme to increase airspace capacity and reduce delays. UK legislation designates the CAA as the UK National Supervisory Authority.

**EC Regulations 2407/92, 2408/92 and 2409/92** (soon to be consolidated and revised) created the single market in aviation in Europe, establishing common rules in the areas of airline licensing, market access and fares. The CAA was designated as the UK competent authority for implementing most of this legislation.

**EC Regulation 261/2004** provides for compensation and assistance in the event that air passengers are denied boarding, or have their flights cancelled or delayed. EC Regulation 1170/2006 establishes rights for disabled people and persons of reduced mobility when travelling by air. The CAA has enforcement powers for both regulations under UK legislation.

26. The main features of the CAA's role within this legislative framework are set out below.

#### SAFETY REGULATION

27. The safety regulation of aviation by the CAA is conducted within a global framework of standards and recommended practices set by the International Civil Aviation Organisation. The CAA also works within a European legislative framework in conjunction with the European Aviation Safety Agency. EASA develops rules, standardises the way that National Aviation Authorities ensure these rules are applied and certifies the designs for the majority of new aircraft.

28. The CAA's main functions in relation to safety are

- registering individual aircraft
- safety of air traffic management
- the continuing airworthiness of aircraft (except for design issues)
- certifying of aircraft operators
- licensing aircrews, aircraft engineers, air traffic controllers and
- regulating aerodromes.

The CAA grants licences, certificates, authorisations and approvals to applicants meeting specific criteria. The CAA carries out regulatory oversight of these approvals through inspection and audit. This work is undertaken within the context of wider information on aviation incidents and risks that the CAA collects and analyses.

The CAA has the power to vary, suspend or revoke these approvals if it cannot be satisfied of a holder's continued ability to achieve the required standards.

29. The CAA is also contracted to EASA to carry out tasks including type certification for newly designed products, continued airworthiness and design organisation approvals.

30. The CAA investigates and prosecutes, in appropriate cases, alleged breaches of UK and European safety legislation.

#### **AIRSPACE POLICY**

31. The CAA develops, promulgates, monitors and enforces a policy for the sustainable use of UK airspace and for the provision of necessary supporting infrastructure for air navigation (for example the provision of en route radar services). The primary objective is to ensure the most efficient use of airspace consistent with safety. In doing so the CAA aims to satisfy the requirements of users of all aircraft, taking account of wider airspace interests, environmental objectives, national security and international obligations. Other responsibilities include

- management of aeronautical radio spectrum
- environmental research and consultancy and
- production of maps and charts.

#### **ECONOMIC REGULATION**

32. Economic regulation of airports is focused on those airports that have been designated by the Secretary of State – currently Heathrow, Gatwick and Stansted – where the CAA set limits on the charges these airports may levy on air carriers. The limits are set every five years by the CAA following non-binding recommendations from the Competition Commission.

33. The provision of en route air traffic services by National Air Traffic Services (NATS) is regulated through a licence, issued by the Secretary of State, which is monitored and enforced by the CAA. NATS' charges to users for en route services are subject to five-year price caps. Service quality, which is measured by the length of delays experienced by aircraft and caused by NATS, is directly incorporated into the price control through a system of bonuses and penalties.

34. The CAA provides economic advice to the Government on a range of aviation policy issues. These include the liberalisation of airline markets and the promotion of effective economic structures for the supply of aviation services and infrastructure. Other responsibilities include

- the collection of statistics
- passenger surveys and
- research and policy assessments of the economics of the aviation industry.

## CONSUMER PROTECTION

35. The CAA is responsible for regulating air travel organisers. It provides consumer protection for holiday-makers through its Air Travel Organisers' Licensing (ATOL) scheme. Travel organisers (other than airlines or travel agents) need to hold an ATOL licence issued by the CAA. To obtain a licence, they must demonstrate their financial stability and their fitness to conduct business. An organisation's licence may be suspended or revoked if it ceases to meet standards in these areas. The CAA manages a system that provides refunds and repatriation for travellers covered by the ATOL scheme.

36. The CAA investigates and prosecutes, in appropriate cases, alleged breaches of some aviation-related consumer protection legislation. It also licenses UK airlines and enforces EU requirements in relation to their finances, nationality and insurance.

## CHANGES TO CAA'S ROLE

37. The review heard very little evidence arguing against having a specialist UK aviation regulator with the CAA's current range of responsibilities. We are not proposing any major changes. We go on to deal with whether economic and safety regulation should remain in the same organisation and the extent to which the CAA has a role to promote UK aviation. Changes to the CAA's role in respect of the environment and passengers are discussed in Chapters 6, 8 and 9.

38. The review received a number of comments on whether economic regulation and safety regulation should be in the same organisation. A few stakeholders believed that the CAA's span of responsibilities was too diverse and that the focus on safety might be lost because of distractions created by economic regulatory issues. There were also concerns raised over the possibility that the economic regulator might influence decisions related to safety.

39. A number of organisations were in favour of keeping the economic and safety regulators in the same organisation on the basis of the UK's good safety record. They had not detected any conflict between the two regulatory functions. There was also a view that the current structure allowed the sharing of information between the different regulatory functions and provided the relevant stakeholders with an interface to a single organisation.

40. The CAA is one of the few regulators to have both a safety and an economic remit. The only other regulator with a similar span of responsibilities is the Office of Rail Regulation (ORR). The ORR took over its safety role in 2006 from the Health and Safety Executive. It has a more limited role than the CAA, as it does not have responsibility for setting technical standards.

41. The CAA explained that its Economic Regulation Group seeks advice from the Safety Regulation Group (SRG) before taking decisions that could conceivably influence safety. SRG was content that there had been no conflict. It also said that safety considerations are treated as paramount by the CAA.

**42. It is clear to me that the CAA has to date managed safety and economic regulation without conflict. There are significant advantages to having both functions in the same organisation. I recommend that the two functions remain with the CAA.**

43. Some members of the aviation community believed that the CAA has a role to promote UK aviation and that it was not effective in discharging this responsibility. Others believed that its objectives should be modified to give it a clear role to promote UK aviation. In contrast, the CAA told the review that it saw its responsibilities as being to assist the aviation industry to meet the needs of the travelling public and society more widely.

44. The Civil Aviation Act 1982, section 4(1), requires the CAA to perform its functions "...in the manner which it considers is best calculated –

(a) to secure that British airlines provide air transport services which satisfy all substantial categories of public demand (so far as British airlines may reasonably be expected to provide such services) at the lowest charges consistent with a high standard of safety in operating the services and an economic return to efficient operators on the sums invested in providing the services and with securing the sound development of the civil air transport industry of the United Kingdom...."

45. This is a complicated statement designed to identify various components of the CAA's role and how they relate to each other. It does not include – nor is there anywhere else – a duty to promote UK aviation. The Act provides simply that the CAA should not encourage charges so low as to jeopardise the sound development of the industry.

**46. I believe that giving the CAA a general role to promote aviation would be incompatible with its duties as a regulator. The CAA is responsible for safeguarding the general public interest, which is broader than the aviation community. I recommend that the Department for Transport propose an amendment to the Civil Aviation Act 1982 to remove the current ambiguity.** The CAA needs to continue its efforts to engage with the aviation community to ensure that there is a shared understanding of its role.

#### **BRINGING THE LEGISLATIVE FRAMEWORK UP TO DATE**

47. The review has received evidence that the Airports Act 1986 is out of date and in need of radical reform. As outlined in Chapter 9 on economic regulation, this is mainly an issue for the DfT review of economic regulation and which the Competition Commission may also address.

48. There was little evidence received from the aviation community on the other parts of the CAA's legislative framework, but the CAA has identified several areas of the Civil Aviation Act 1982 that need to be updated. These areas are covered by a single recommendation at the end of this section, except where we have cross-referred to other parts of the report.

49. Section 4 of the 1982 Act gives the CAA a duty to "secure that British airlines provide air transport services which satisfy all substantial categories of public demand ...". This duty is not aligned with European legislation and has on a number of occasions had to be disapplied in UK legislation. The section has also been the subject of a recommendation by the CAA's Strategic Review of General Aviation to remove any suggestion of bias toward commercial air transport over General Aviation. Further, the section makes no reference to the environment or the consumer/passenger.

50. Section 5 requires the CAA to consider environmental factors when licensing an aerodrome that the Secretary of State has specified in an order. Chapter 6 on the environment makes a recommendation on this section.

51. Under section 11, the CAA sets a scheme of charges defining the amount that the CAA will charge the aviation community for each of its regulatory activities. It is reviewed and amended on an annual basis. Section 11 requires a sixty-day delay between the publication of the CAA's charging schemes and the charges coming into force. The sixty-day delay was initially intended to allow time for any final representations to the Secretary of State.

52. Since this legislation was enacted the CAA has established a more comprehensive and effective approach to consulting the aviation community. In particular, the Safety Regulation Finance Advisory Committee (SRFAC) was created to review the CAA's annual proposals to amend its safety regulation charges. This consultative body is chaired by a representative from the aviation community. Its members include a broad range of organisations regulated by the CAA. The CAA also undertakes a 12-week consultation exercise during which any interested parties may comment on the proposals.

53. The sixty-day delay makes it difficult for the CAA to align the development of its charges schemes with its financial planning cycles. The need for the delay was considered during a joint review of safety regulation charges by the CAA and the aviation community in 2004/05. The consensus was that the period should be reduced. This position is supported by the current SRFAC.

54. Part 2 of the Act makes provisions to allow the CAA to manage aerodromes. It has not managed an airport since Highlands & Islands Airports Ltd was transferred to the Secretary of State for Scotland in 1995. It is difficult to envisage a situation where the CAA will be given responsibility in the future to manage an airport.

55. Schedule 1 paragraph 6 of the Act requires that the Treasury consent to members' remuneration and pensions arrangements. This is discussed in Chapter 4 on corporate governance.

**56. I recommend that the Department for Transport work with the CAA to develop and propose amendments to address the specific issues identified in the report to bring the legislative framework up to date.**

## THE CAA'S STATUS

57. The CAA was established under statute and its statutory functions have been described earlier in this chapter. But the statute does not set out what type of public body it is for administrative purposes. Until the privatisation of National Air Traffic Services in 2001, the CAA was defined by Government as a nationalised industry. With the loss of air navigation service provision, the CAA's remit became much more focused on regulation. In recognition that it was no longer a nationalised industry and because of its need as a regulator to be, and be seen to be, independent of Government, the CAA was redefined by Government as a public corporation. The CAA remains a public corporation today, the most independent form of public body. The status of most similar regulators is defined as either non-Ministerial departments or non-departmental public bodies. These regulators receive substantial public funding and with it greater Parliamentary scrutiny.

58. This section considers whether the CAA's formal status as a public corporation is appropriate, or whether it should be closer to or further away from Government. It also looks at whether it is right that the aviation community is the main source of funding for the CAA.

59. A radical alternative to its public status would be to make the CAA a private sector regulator. No evidence was presented in favour of this option. The review saw no advantage in pursuing this option.

60. The opposite extreme to a private sector aviation regulator would be to bring it closer to Government, reducing its independence. This would entail making the CAA an agency or part of a Ministerial department (such as the Department for Transport), where it would have no voice of its own.

61. Closer proximity to Whitehall would bring advantages. There would be a more obvious line of accountability to Ministers, and thus to Parliament, for all of the CAA's regulatory decisions. Further, Government policy and regulation would be located in one body, reducing the risk of disconnects. Ministers would be able to take greater responsibility for striking the democratic balance between competing interests on aviation issues that may have wider environmental, social or economic impacts. But Ministers currently possess a number of levers that enable them to retain accountability and determine the strategic direction of regulation, if not the individual decisions. For example, the Secretary of State

- may issue directions in a national emergency and in other specific areas (air navigation, accounts)
- appoints the Chairman and Board members and determines their pay and strategic objectives
- may establish a formal sponsorship statement setting out the relationship between the CAA and DfT
- appoints the CAA's external auditors, presents the CAA's accounts to Parliament and is involved in the development of the corporate plan and
- with the Treasury's consent approves the CAA's national loans and overdraft each year; sets its required rate of return on capital; approves its Board members' pay and the accounts direction.

62. The key reason for the CAA to retain its independence is so that it can continue to make individual, high-profile regulatory decisions which the public can be

reassured are made free from short-term political considerations, bringing objectivity and consistency to the outcomes.

63. The CAA's independence from Government also enables it to retain a specific focus on aviation matters. It can give Government objective, specialist advice and, where appropriate, challenge Government positions. Its status gives it greater flexibility over salaries than is possible within Government. This flexibility, together with its pension scheme, allows it to recruit and retain the specialist professionals that are required to discharge its functions effectively.

64. It is not appropriate for the CAA to move into the private sector, or closer to Government. **I recommend that the CAA's current status as a public corporation be retained.**

#### **BOUNDARY BETWEEN DFT AND THE CAA**

65. The terms of reference asked us to consider the formal relationship between the CAA and Government. The natural starting point is to look at the respective roles of the CAA and the Department for Transport. In particular, the Department has briefed us on various activities that could feasibly sit in either body. The review has developed principles to guide decisions on where these might most appropriately be located.

66. We have heard extensively from both the CAA and the DfT on these issues. Others have tended not to cover this ground. But a significant number of organisations commented on the financial relationship between DfT and the CAA. Stakeholders said that work carried out and advice given by the CAA at the request of the Secretary of State should be paid for by DfT. Many organisations wanted more transparency in this financial relationship. These issues are considered in Chapter 11 on the CAA's financing and cost-effectiveness.

#### **THE ROLE OF DFT**

67. The Secretary of State for Transport is directly accountable to Parliament. Generally speaking, the role of officials in respect of aviation is to work with and advise the Secretary of State in formulating a strategic policy framework for the air transport sector in the context of the Government's overall transport objectives and in representing the Government's aviation policy to its stakeholders, including Parliament, the media, the wider public and internationally. This role is primarily conducted by Aviation Directorate, although DfT also contains an Air Accident Investigation Branch reporting direct to the Secretary of State, and Transec – the transport industry security regulator with responsibility for setting, monitoring and enforcing security standards.

68. It is the Department's role to lead on primary and secondary UK legislation, formulating policy in consultation with stakeholders, drafting most legislation and supporting the passage of this legislation through Parliament. (For some pieces of secondary legislation, particularly on safety, it is the CAA that does much of the preparatory work, including drafting). The Department also leads UK negotiations on air transport in the EU and in other international forums.

69. The Department develops the CAA's statutory framework (subject to Parliamentary approval), which outlines the Authority's roles and responsibilities. As the CAA's sponsor, DfT monitors how it fulfils its responsibilities set out under the framework.

70. The Secretary of State can initiate changes to the statutory framework and appoints members to the Board. The Secretary of State may also supplement the CAA's statutory framework by issuing directions (in particular instances) or guidance.

71. In areas where the CAA's statutory duties lead it to become involved with other Government Departments or other areas of transport policy, DfT needs to have the capacity to deal with any issues as they arise. This might be the case, for instance, with radio spectrum or defence. The CAA keeps DfT in touch with major developments in these areas.

### **THE ROLE OF THE CAA**

72. The CAA's main work is to discharge its statutory duties as described earlier in this chapter. This can include the provision of advice to Ministers under section 16 of the 1982 Act, such as the work the Secretary of State has recently asked the CAA to carry out on the passenger experience.

73. The CAA can also undertake other activities that it deems necessary to further its statutory duties.

74. Although it must produce an annual report for the Secretary of State, which is laid before Parliament, and the Transport Committee may call on the CAA to give oral and written evidence, its own accountability to Parliament is much less immediate and direct than DfT's.

### **DFT SPONSORSHIP OF THE CAA**

75. As the sponsoring Department of the CAA, DfT has an important role to play in establishing the CAA's remit, legal framework and strategic objectives. The Department and the CAA should discuss these issues systematically at least once a year and perhaps more frequently.

76. There must also be good and early communication between the organisations about potential changes in policy, as these will naturally have an impact on the work of the CAA. The timeframes in these instances are likely to be more critical. Leading up to a crucial decision or announcement, it may be necessary for both bodies to reflect weekly or even daily on what new developments need to be communicated to the other.

77. Finally, the legal framework within which the CAA operates should be reviewed from time to time to ensure that it continues to be fit for purpose.

**78. I recommend that the CAA's sponsorship statement should reflect the need for systematic discussion between the CAA and DfT on strategic objectives, policy changes and the legal framework.**

## ALLOCATION OF WORK BETWEEN DFT AND THE CAA

79. DfT commissioned a short study recently to identify areas of work that might more effectively be conducted by the CAA. The results of the study are still under discussion between the Department and the CAA. Some of the areas under consideration are relatively minor and non-controversial and I have seen little benefit in addressing each area and making specific recommendations. Instead I have sought to identify high-level principles which should help in the task of allocating work that could feasibly go to either the Department or the CAA.

80. There cannot be watertight boundaries between the two organisations. In many areas, although a preponderance of work will be done in one of the organisations, the other would still be engaged to some extent. This underlines the importance of the quality of the relationship between the CAA and the Department.

81. Any of the first three principles, if met convincingly, could represent a conclusive argument for the allocation of work. If they do not apply or are not decisive, the case must be judged through an assessment against all six principles. Individual decisions may need to be considered on a case-by-case basis by both organisations to make this process work effectively.

- i Statutory Framework – if an activity is covered by the CAA’s statutory framework, it should carry it out. This principle should trump those that follow, although if there were a strong case in terms of the other principles for the activity being located in DfT, this might justify amending the framework
- ii Democratic Accountability – there are some activities that should be undertaken by DfT, as an organisation with Ministers that the electorate can hold directly to account. This principle is particularly likely to hold where policy decisions are required involving a trade-off between aviation and other policy areas, including areas which are the responsibility of other Government Ministers. It is also important that DfT should take the overall lead in representing the UK where high-level international and EU negotiations are being conducted – this principle is expanded upon later in Chapter 7 on the CAA’s international work and
- iii Independence - the reverse of the ‘democratic accountability’ principle is that some essential and generally technical activities (e.g. safety regulatory decisions) may best be placed in CAA, precisely because of its independence from Government. As in many other cases across public life, this would reassure interested parties that decisions had not been affected by irrelevant considerations or lobbying.

The remaining principles are summarised below:

- iv Capability – an organisation will be better placed to carry out an activity if the skills required fit well with the normal range of skills found in the organisation. For instance, conducting European negotiations is often better suited to the skills and experience one might find in a Government Department – technical experts may not always be so well placed to take account of all the considerations relevant to shaping the line that best reflects the national interest. Nonetheless, some European negotiations are likely to be better suited to the skills and experience of technical experts. To use another example, one organisation may be better placed than the other to deal with particular stakeholders

- v Connectivity with other functions/activities – certain activities may sit well within an organisation because they are closely linked to core activities and
- vi Transition costs and other disruption – where the argument for the location of an activity is finely balanced, it may be preferable to leave it where it is, if significant costs or disruption will arise from any change. It will be important to assess the impacts and any possible mitigation, before deciding if an activity should be moved.

#### **APPLYING THE PRINCIPLES – AN EXAMPLE**

82. It may be helpful to consider how these principles might be applied to an example of work under consideration for transfer from DfT to the CAA. The example is illustrative – the review does not aim to come to a conclusion on where this activity should be placed.

83. The CAA currently conducts safety checks of non-EU aircraft. If it discovers a problem, the question arises as to what sanction should be imposed, an issue currently considered by DfT officials before referral to the Secretary of State for a decision. The options for sanction range from a warning to the removal of the airline's permit to fly. Sanctions may have international implications, such as prejudicing other negotiations or causing retaliatory measures against UK aircraft.

84. Deciding on sanctions is not a CAA statutory duty (principle (i)). But principle (ii) on democratic accountability comes into play, as foreign and diplomatic issues could arise from the imposition of a sanction – DfT being part of Government makes it better placed to weigh up these non-aviation factors, alongside, for example, safety considerations. On the other hand, there could be an argument for principle (iii) on independence to apply – a decision could appear fairer to external parties if it were made by the CAA, because it would be based on the technical, non-political opinion of safety experts.

85. In terms of capability (principle (iv)), there is no reason that the decision could not be made in either DfT or CAA once the safety advice had been given. For principle (v) – connectivity of functions – it could be argued that the work should take place in CAA, to allow connectivity with the safety experts who undertook the safety check. Alternatively, keeping the work in DfT would allow it to remain alongside international aviation negotiations staff, enabling sensitivities here to be taken into account. There are unlikely to be major transition costs (principle (vi)) involved.

**86. I recommend that the principles the review has developed governing the boundary between DfT and the CAA be incorporated into the CAA Sponsorship Statement.**

#### **THE RELATIONSHIP BETWEEN CAA AND DFT**

87. The terms of reference asked the review to look at the CAA's relationship with Government. The Department for Transport and the CAA have an agreed sponsorship statement,<sup>3</sup> last updated in May 2006. This document sets out the relationship between the Secretary of State and the CAA; the framework within which the CAA operates; any financial conditions and other guidance relevant to the

<sup>3</sup> Sponsorship Statement for the Civil Aviation Authority – May 2006

exercise of its functions; and how the CAA is held to account for these. It is drawn up by DfT in consultation with the CAA. One of the key features of the statement that has a major impact on the informal relationship between the two organisations is the section on communications setting out the principle of 'no surprises', shown in the box below. This is an important area for the review.

The Department and the CAA recognise that working together successfully requires effective two-way communication at many levels. In practical terms this means that both the Department and the CAA agree to operate a policy of 'no surprises' in relation to particular issues and cases likely to generate media, business or public interest or lead to significant announcements. To achieve this, the Department and the CAA will in particular

- keep each other informed in general terms about live issues, the timing and progress of significant issues, well ahead of announcements but without jeopardising effective enforcement or revealing the substance of individual investigations and
- give short-notice advance warning of any significant or sensitive announcements in relation to matters affecting each other.

The Department and the CAA will respect the requirements of confidentiality of any information which they share.

88. During the course of the review, the opportunity has arisen to talk to current and former senior members of the CAA and the Department about the links between the two organisations. The section of the sponsorship statement relating to communications was an important area of discussion.

89. The relationship between the Department and the CAA is a classic example of an interface that occurs in many other places in the public sector between Government Departments and independent 'arms-length' bodies. Regardless of the sector concerned, the mutual interest of two such bodies in working together constructively at a number of different levels is obvious. Nonetheless, there can be cases where the Department's desire for the independent body to follow a particular course, and the independent body's desire to preserve both its independence and the perception of its independence, can, particularly if exacerbated by tensions between individuals or by external circumstances, lead to a deterioration in trust between the organisations. But although trust and relationships are difficult to measure and it is not possible to get them right permanently, no dimension is as important as this to getting work done effectively.

90. On several occasions, evidence has been given to us about instances when the Sponsorship Statement's commitment to 'no surprises' has been broken. The review believes that it is not always possible for either organisation to keep the other organisation as up-to-date as it would like. At times, DfT will be required to study policy options that may never become reality, and which it would be unhelpful to divulge while they are in development. This, and the interplay between civil servants and Ministers, reduces the Department's ability always to be fully open with the CAA. Alternatively, the CAA might have work in progress with major public consequences and would want to protect the Department and itself by not showing the work to the

Department in advance, in order to avoid the appearance that the Department might impair the CAA's independence.

91. The commitment to 'no surprises' in the existing Sponsorship Statement is qualified. It talks about the desirability of keeping the other party informed ahead of significant announcements or in cases likely to generate media, public or business interest, but "without jeopardising enforcement or revealing the substance of individual investigations."

92. The review notes that these words give two examples of when the CAA might surprise the Department, but there is nothing about the reverse situation happening, which in practice may be more likely. The sponsorship statement has not been enough to prevent the relationship between the two organisations deteriorating when a surprise is sprung on one by the other. The 'no surprises' principle has been described to us by some as an unqualified commitment to keeping each other in the picture, which it manifestly is not. It is important that 'surprise' does not become the norm. But there will be occasions when 'no surprises' is not possible and the expectation of openness will exacerbate tensions that might occur anyway as a result of the decision not to consult the other.

93. **I recommend that the CAA sponsorship statement be revised at the earliest opportunity to reflect current requirements, to emphasise the need for constructive relationships and to explain that there will be instances where complete openness is simply not possible.** The text as it stands is capable of misinterpretation and creates high expectations of mutual consultation that cannot always be achieved. This can have a negative effect on relations between the organisations.

94. It is important that a reworded Statement is not used as an excuse to 'surprise' the other organisation when that can be avoided. Indeed the sponsorship statement itself can only ever be a small part of what it takes to achieve and maintain an excellent relationship. In the memory of those currently involved, the relationship has generally been as good as anyone could hope. In the last few months, there have been problems in some areas, but recently the relationship has again begun to go better. It would be wrong to exaggerate the difficulties, as constructive work has continued between teams in most areas, but both organisations would accept that their relationship now requires a fresh impetus.

## 4 CORPORATE GOVERNANCE

95. The Civil Aviation Act 1982 sets out the framework for the CAA's corporate governance. The organisation is defined as a body corporate, with between six and 16 members, including one Chairman and up to two Deputy Chairmen, appointed by the Secretary of State.<sup>4</sup> Appointments are subject to the Commissioner for Public Appointments Code of Practice for Ministerial Appointments to Public Bodies.<sup>5</sup> The Act makes no distinction between executive and non-executive members, although in practice when making appointments the Secretary of State differentiates between the two. Executive directors are appointed to specific roles (e.g. Group Director of Safety Regulation).

96. The CAA body corporate is led by a non-executive Chairman working three and a half days a week. There are five executive directors – the four regulatory group directors covering safety regulation, airspace policy, consumer protection and economic regulation, and the Chief Operating Officer (who is also the Finance Director). Under the Transport Act 2000, the Director of Airspace Policy is nominated by the Secretary of State to perform the CAA's air navigation functions on the CAA's behalf – decisions in this field are not taken by members collectively.

97. The Secretary of State has appointed five non-executive directors. One of these was subsequently appointed as Deputy Chairman in 2007. Four of the non-executive directors are appointed on a part-time basis with a commitment to work two to three days a week. The fifth, whose position is discussed later in this chapter, is nominated under the Transport Act 2000 for national security purposes.

98. The members of the CAA sit as a Board, generally on a monthly basis. The Board is fully accountable for all activities undertaken by the CAA. Many of the CAA's functions may be delegated to its staff. But section 7 of the 1982 Act specifies that certain decisions, such as on appeals and price reviews, can only be taken by members. For convenience, the Board forms panels of one or more members to take these decisions, although issues of importance are referred to the Board for discussion. The Board exercises oversight of the panels.

99. The Board has a number of formal committees working to it. There are policy committees for each of its four regulatory areas and an environmental policy committee. Broadly, these are responsible for giving direction to regulatory policy, approving business plans, monitoring performance, making decisions about service levels, charges, legislative changes and key appointments, and overseeing risk management. Policy committees are chaired by the Chairman or Deputy Chairman and include two non-executive directors, one or more executive directors and senior executive staff. The membership of the audit and remuneration committees is non-executive. Some executives attend for certain issues. The Chairman and the Chief Operating Officer attend the audit committee. The Chairman also attends the remuneration committee.

100. There is also a CAA management committee that deals with business management. The committee consists of the four group directors and the Chief Operating Officer, who is the chair. Senior executive staff attend as required.

<sup>4</sup> The Civil Aviation Act 1982 allowed for 12 members. This was later amended to 16 by section 72 of the Airports Act 1986.

<sup>5</sup> The Commissioner for Public Appointments Code of Practice for Ministerial Appointments to Public Bodies – August 2005.

101. In this chapter I make a number of high-level recommendations about the corporate governance of the CAA. As I indicated in the chapter on the CAA's general standing and performance, my recommendations are not made on the basis that the CAA is broken. The CAA's existing governance arrangements have been a part of the organisation's success. Nevertheless, I believe that modernisation and improvement of the governance structure will help the CAA to meet the significant challenges that lie ahead and to continue that record of success.

#### **CHAIRMAN AND CHIEF EXECUTIVE**

102. The CAA's Chairman Sir Roy McNulty is described as non-executive, but in practice works for the CAA three and a half days a week. He has significant involvement in the organisation, to the extent that many stakeholders think that he is an executive Chairman. He has held the position since 2001, and is due to complete his second and final term in August 2009.

103. The majority of other UK regulatory bodies were initially established with power focused in a single individual at the top of the organisation, a Director General. Following concerns about this concentration of responsibility in a single figure, the Government developed a new preferred model in the early 2000s, in which a Chairman shared decision-making responsibility with a board of executive and independent non-executive members. In most regulatory bodies, this model includes a Chief Executive as well as a Chairman. Since its inception, the CAA has been run by its Board, which is led by the Chairman. But it is unusual amongst regulators in that currently it has no Chief Executive.<sup>6</sup>

104. Various witnesses gave evidence on this issue, mainly from within the Department for Transport and the CAA. Neither the Department nor the CAA presented a uniform view on the subject. Of the private sector stakeholders, all of those mentioning the issue were in favour of a Chief Executive. They argued that a Chief Executive would provide additional leadership capacity and decision-making authority, and would help to share best practice across the organisation. A Chief Executive would also provide additional resource and a broader range of skills for high-level influencing and communications in Europe and within the UK.

105. Appointing a Chief Executive would bring possible disadvantages. In any organisation, introducing an extra layer of management can lead to an overlap in roles and possible relationship difficulties, at least initially, and has the potential to slow the decision-making process. It also creates the risk that accountability at the top of the organisation is blurred. In the CAA, these risks may be particularly relevant to the Chief Executive's interface with the group directors and Chairman. For instance, appointing a Chief Executive could reduce the scope of the group directors' responsibilities. This could have implications for the CAA's ability to recruit and retain high-quality individuals.

106. I believe that these disadvantages can be mitigated so long as the transition phase is well managed. The boundary between the role of the Chief Executive and those of the Chairman and executive directors would need to be set out carefully. My expectation is that the Chief Executive would work full-time, with a primary responsibility for the management of the work of the Authority as a whole. To

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<sup>6</sup> From 1986 to 1995 the CAA had a Managing Director and a Chairman. But this was when NATS, with approximately 6000 staff and operational responsibilities, was part of the CAA. With under 1000 staff and no NATS, the current CAA is different.

minimise the risk of overlap with the executive directors, I hope that it will be clear that they are expected to continue in the lead in their own areas. The Chief Executive would need to know what is going on in some detail in order to be an effective leader of the whole organisation and from time to time to represent the CAA publicly.

107. The Chairman and Chief Executive would need to have complementary skills, each adding something different to the organisation. To facilitate the likelihood of a good relationship between the two, the Chairman should have a role in appointing the Chief Executive. The Chairman would eventually work about two days a week, although this could be determined by DfT in consultation with the CAA after a period of working under the new structure. This would limit the extent to which the Chairman could be involved in policy committee and panel work.

108. It has been suggested that a drawback to a Chief Executive is the additional cost it would impose on the CAA's charge-payers. We take cost seriously and certainly the charge-payers do. But everyone has a keen interest in the CAA's ongoing effectiveness. If, as I believe, a Chief Executive would make a significant contribution to that, the costs would be fully justified.

109. Appointing a Chief Executive to the CAA would have three significant advantages. First, the review has heard many examples illustrating the considerable pace of change in aviation. These have been set out in Annex C on trends. The CAA's continued success as a regulator is dependent on it staying abreast of major developments, and having the capability to adapt swiftly. A Chief Executive, by virtue of his or her position in the organisation and also the additional resource, would strengthen the CAA's ability to innovate and adapt flexibly to challenges on the horizon, helping it to remain open both to new ideas from stakeholders and to best regulatory practice.

110. Looking to the future, a second key benefit of the Chief Executive would be to strengthen the CAA's ability to work across the whole organisation. The review has heard about three main areas of work that are rising in prominence and that affect the CAA as a whole. These are the environment, international developments, and passengers, covered in Chapters 6, 7 and 8 respectively. The review believes that a Chief Executive would be able to focus with DfT on developing the CAA's strategic approach to these areas, and increasing awareness of them across the organisation.

111. Finally, appointing a Chief Executive with contacts and experience in areas that complement those of the Chairman would improve the CAA's influencing capacity. This is particularly important in Europe, as highlighted in Chapter 7 on the CAA's international work, given the increasing tendency for regulation to be made there rather than nationally. Added influence would also be valuable when dealing with Parliament, Government and other UK stakeholders.

**112. Having considered the advantages and disadvantages, I recommend that the Secretary of State appoints a full-time Chief Executive to the CAA. I recommend that, once a Chief Executive is in place, the responsibilities and time commitment of the Chairman should be reduced.**

113. Under a Chief Executive, I believe that there would still be a need for the work done by the Finance Director, as Chief Operating Officer. That said, the detailed split of responsibilities, as with all executive directors, would need to be resolved in discussion with the Chairman and Chief Executive when the latter was appointed and when the role is being defined.

## THE ROLE OF THE BOARD

114. The Board has sight of a wide range of issues relevant to the CAA's work. It agrees the direction for the organisation, monitors performance, takes most major decisions and provides input on others. Despite this, some decisions are taken not by the Board as a whole but by individual group directors, policy committees, or by the panels set up by the Board to consider price reviews and appeals, amongst other issues. In these cases and where an issue is important enough, position papers are presented at the Board at appropriate stages in the process so that it can challenge and feed in ideas.

115. The review has received very little evidence on this subject. Nonetheless, there was a perception from some stakeholders that the way the CAA makes certain decisions is not fully transparent and could be improved by publicly exposing the rationale and process behind them. Others thought that the CAA relied too much on individuals to make key decisions. The CAA explained that it took this issue seriously and makes available information about its decision-making processes on its website and in consultation documents.

116. Looking across other UK regulatory bodies, it is more usual for key decisions to be made by the Board as a whole and not through the process of panels and policy committees used by the CAA. Adopting this more usual practice in the CAA could bring several advantages over the current arrangements. The Civil Aviation Act already makes the CAA Board accountable for decisions that the organisation makes. By having the Board make the final decision, its accountability would be enhanced and it would be easier to ensure that decisions incorporate all relevant considerations. Further, bringing the Board as a whole into decision-making may at times improve quality by drawing on a wider range of experience and opinion.

117. It has been suggested that while the Board is capable of making certain key decisions, some issues are too complex or technical to be condensed into a Board paper and these are best left to the relevant executive director or policy committee, perhaps after discussion at Board level. Further, it is said that the legal obligation for decision-makers to consider written and oral evidence on airport price review decisions means that it is unrealistic for these decisions to be made by the Board as a whole, rather than by a panel consisting of a few Board members. I believe that, regardless of the level of complexity involved, it is possible for issues to be crystallised into high-quality, readable papers for the Board. These would set out the important issues and arguments, enabling an informed and balanced decision to be made. It is true that these changes would create an additional briefing burden on the organisation. But the following advantages would arise

- increased accountability of Board for major decisions
- greater Board effectiveness and
- significant regulatory or high risk decisions subject to greater scrutiny and challenge, particularly by non-executive directors.

**118. I recommend that key decisions should be made by the Board as a whole. This is not to say that important preparatory work, for example on airport price review decisions, should not be undertaken by a smaller group consisting of or including members of the Board.**

119. As mentioned, the CAA's Director of Airspace Policy is appointed by the Secretary of State under the Transport Act 2000 to perform the CAA's air navigation functions. In making the appointment, the Secretary of State for Transport consults the Ministry of Defence (MOD). Regulatory decisions in this area are a matter for the

group director alone, rather than the whole CAA Board. This arrangement was not the subject of comment in any of our evidence.

120. We are not aware of any problems that have occurred as a result of these arrangements since they were put in place. Nonetheless, it is not easy to see why, uniquely, the power to make these decisions should be vested in an individual, rather than in the CAA Board. The Department for Transport and the CAA, in consultation with the Ministry of Defence, might reflect on whether the time has come to put these arrangements on a similar footing to the work of the CAA's other groups.

### **NON-EXECUTIVE DIRECTORS**

121. The CAA's non-executive directors have a significant time commitment to the organisation – four out of five non-executives work for the CAA either two or three days a week (the fifth is the national security nominee). Each of the five policy committees counts two non-executive directors amongst their membership. In addition to their role on the CAA Board, non-executives may be members of various regulatory policy and appeals panels, the remuneration and audit committees, and other bodies such as the Air Travel Trust, the pensions committee and subsidiary companies.

122. The review has been struck by the extent to which some of the non-executive directors' are closely involved in the decision-making processes of the organisation. Although the remuneration and audit committees and the appeals panels are typical non-executive roles, members are involved in a substantial amount of regulatory policy work beneath Board level. Their role on policy committees is the best example of this.

123. There are arguments for the non-executives to continue to be part of these committees. The CAA is a technical organisation and involvement in day-to-day activities helps the non-executives to understand it, which is clearly essential if they are to play a role in high-level decision-making. To this end, non-executives are placed on policy committees and encouraged to move around them. Their involvement brings challenge and an outside perspective below the Board, where a greater number of issues affecting the CAA are discussed.

124. Nonetheless, the main purpose of non-executives is to challenge at the Board where the issues that most matter to the organisation should be discussed. There is a clear risk that involving non-executives at the working level could bring them too close to the organisation, although I have identified no evidence to this effect. Much of their value as non-executives lies precisely in their distance from the detail of the organisation's work and in their ability to bring a fresh perspective and challenge to proposals presented by the executive. The existence of this challenge is what produces a well-rounded organisation capable of making decisions that take account of the interests of a wide range of stakeholders.

**125. I recommend that the CAA work in a way that ensures that, whilst the non-executives are adequately briefed, they are not overly involved in working level formulation of policies and decisions in regulatory panels and policy committees.**

126. DfT might in future consider the optimum ratio of non-executive to executive members on the CAA Board. This is a difficult issue and the right answer for the CAA is likely to depend on the timing and the individuals. For reasons of good

governance, it might be desirable for non-executives to outnumber the executives. But if any executive directors were not on the Board, this would diminish their personal standing. On the other hand, a Board with too many members might be unwieldy.

127. During the course of the review, several of the CAA's stakeholders suggested that the CAA Board should have a non-executive director to champion their area. Suggestions included a specific non-executive director for general aviation, for the aviation industry and for consumers. I do not believe that independent non-executive directors would continue to be independent if they had a specific duty to promote a particular sector of society, rather than the CAA's stakeholders in the round. Nonetheless, it may be helpful for the CAA to have a checklist of areas that the Board and other decision-making bodies or individuals in the CAA should take into account when making decisions.

#### NATIONAL SECURITY NOMINEE

128. Four out of five of the CAA's non-executive directors are appointed with a view to their carrying out the normal functions of such directors. The exception is a specific nomination that the Secretary of State makes under section 67 of the Transport Act 2000. This non-executive director has a statutory brief to safeguard national security in respect of the CAA's air navigation functions, but also has a wider role, to connect civil and military aviation at a senior level. The post has been filled since 2000 by a series of serving Air Vice-Marshal who move on after two years, sometimes more quickly. While at the CAA, officers also occupy a full-time post as Assistant Chief of the Air Staff in the Ministry of Defence.

129. There is a case for changing these arrangements. In particular, a member with more time to spare might contribute more fully to the CAA Board as a whole, on issues other than airspace, as the other non-executives currently do. Further, the fact that holders of the post tend to move on after less than two years means that they do not build up as much experience of the CAA as the other non-executives.

130. I believe that the benefit to the CAA in having a statutory national security nominee on the Board to provide security briefings is more theoretical than real. To the extent that it is required, briefing can be provided by the Ministry of Defence and others with relevant insights. But the current arrangements ensure that the Ministry of Defence and the CAA continue to be joined up in relation to airspace and safety issues, and that MOD resources are available to assist with CAA safety initiatives. The importance of this point outweighs the arguments for change. **I recommend that the Secretary of State keep the current arrangements whereby the Assistant Chief of the Air Staff from the Ministry of Defence is appointed as a non-executive director of the CAA.**

#### MINISTERIAL APPOINTMENT OF EXECUTIVE DIRECTORS

131. As mentioned, all members of the CAA Board are appointed by the Secretary of State, subject to the Code of Practice for Ministerial Appointments to Public Bodies. As a result appointees may be in position for a maximum of two terms, each one consisting of up to five years.

132. When they become vacant, some of the CAA executive director posts may be filled by staff already working for the CAA if they are successful in open competition, rather than by external applicants. To be promoted to executive director on the Board, the individual concerned resigns from the staff and is appointed as a member of the CAA by the Secretary of State. The effect of this for younger staff being promoted to the Board is that after two terms (i.e. up to ten years) of working as an executive director they would have to leave the CAA. The alternative of returning to the staff will naturally be unattractive and potentially disruptive for the organisation. This could cause the CAA to lose talented individuals with a wealth of experience while they are still performing at their peak. The trend towards later retirement adds to the sense that this constraint may be wasteful.

133. In some other UK regulatory bodies, the Board appoints executive directors (apart from the Chief Executive) without Ministerial involvement. There would seem to be a case for the CAA to have similar flexibility. The Department for Transport and the CAA might give this issue consideration.

#### **THE TREASURY'S APPROVAL OF CAA MEMBERS' REMUNERATION**

134. Schedule 1, Clause 6, of the Civil Aviation Act 1982 states that "the CAA shall pay each member such remuneration as the Secretary of State may determine with the consent of the Treasury." The Treasury takes seriously its power of approval, as it is bound to do, so long as it remains a statutory requirement.

135. The provision is a legacy from many years ago. In evidence to the review, the Treasury explained that the CAA was the only regulator it looked at in this way. It represented a drain on staff time to exercise the duty diligently.

**136. The statutory requirement for the Treasury to approve the CAA members' remuneration and pensions is an anomaly. I recommend that the Department for Transport seek to amend the legislation so that the responsibility lies solely with the Secretary of State.**

#### **POLICY COMMITTEES**

137. The current role and membership of policy committees is set out earlier in this chapter. It is beyond the review's strategic scope to make recommendations on these committees. But it is appropriate to observe that the appointment of a Chief Executive, and a change in the role of the Chairman and in the way that the Board made decisions would have an impact on the policy committees. The CAA may want in the future to review the number of policy committees, their role, who chairs them and their membership.

138. One witness suggested that the CAA might consider asking specialists who were not members of the CAA to feed into policy committees. For example, an expert on nuclear power safety regulation could sit on the safety policy committee. The review notes this issue for possible consideration by the CAA.

## THE CAA'S AUDIT ARRANGEMENTS

139. The Transport Committee report on the work of the CAA recommended that the National Audit Office be granted access to the organisation so that it could conduct value for money and efficiency studies. It acknowledged that the CAA had independent external audit (provided by PricewaterhouseCoopers, who are appointed by the Department for Transport) and that the CAA's costs were scrutinised by the aviation community. The Committee did not accept that the latter's scrutiny was sufficiently independent to safeguard the public interest.

140. The CAA has explained to the review that it already has a comprehensive internal audit programme, which includes an element of value for money audit. This service is currently provided by Deloitte. All areas within the CAA are subject to internal audit. These range from regulatory oversight activities to project delivery. They encourage the CAA to identify and implement efficiencies. The Deloitte senior management engage with the CAA's Board about this work from time to time. There would be benefit in the CAA Board placing a more specific duty on Deloitte to devise and carry out annually, in agreement with the Board, a specific programme of value for money audits. Deloitte have relevant experience which would enable them to make this a challenging and useful process for the CAA. It might also be fruitful for the CAA to consider asking Deloitte, when setting up this programme, to talk to the National Audit Office to draw on its experience of the issues that arise in relation to other regulators.

**141. In light of the CAA's existing audit arrangements and the opportunity to build on them in the way I have described, I see no need for the National Audit Office to be involved directly with the CAA. I recommend that the current arrangements be retained.**

## THE CAA'S PLANS

142. As part of its corporate governance, the CAA has in place a set of planning and reporting arrangements. The review received very few comments on this topic.

143. The CAA produces a corporate plan and business plans for each of the groups on an annual basis. These are five-year rolling plans. They are reviewed and endorsed by the CAA Board.

144. The corporate plan sets out

- the significant changes and challenges in the aviation and regulatory environment in which the CAA will operate
- the CAA's role, its objectives, and the strategies and key actions required to achieve them
- a summary of the CAA's activities across the four main regulatory functions and the work it expects to do in advising Government
- financial projections and forecasts of staff numbers and
- major risks and associated mitigating actions.

Before it is published on the website, the corporate plan is shared with DfT.

145. The four regulatory functions and the corporate centre produce more detailed business plans supporting the corporate plan. Performance against the key business plan deliverables is reported to the Board on quarterly basis.

146. The corporate and business plans form the basis for the annual budget. The budget is approved by the CAA's Board and monthly reports on performance are provided.

147. The CAA also produces and publishes a five-year safety plan which identifies by aviation sector the safety improvements upon which the CAA intends to focus over the period of the plan. An update on progress against the plan is produced on an annual basis.

148. The CAA produces an annual report and accounts that include a financial and regulatory review, statements on the CAA's corporate governance arrangements, the CAA's financial statements and the key performance indicators agreed with DfT. This report is reviewed by the CAA's Audit Committee and approved by the Board. It is provided to the Secretary of State to lay before Parliament and is made available on the CAA's website. The CAA also publishes and regularly updates key performance indicators on its website.

149. The review believes that the CAA's arrangements for planning and reporting are appropriate and effective. The plans address the major challenges facing the CAA and are reasonably transparent to stakeholders. To improve on these arrangements, in Chapter 10 on the CAA's stakeholder engagement, I recommend that the CAA consult its stakeholders on its priorities and plans.

## 5 APPEALS

150. Under the Civil Aviation Act 1982 and other UK and EU legislation, the CAA is responsible for issuing a variety of approvals (licences, certificates, etc.) in relation to a wide range of aviation activities. Most approvals are made by CAA staff, under authorisation from the Board. Certain decisions can only be made by members of the Board.

151. If an organisation or individual is not content with a decision made by the CAA, some form of appeal will normally be available to them. This will depend on the area in which the decision was made.

152. Some of the CAA's decisions, including many safety decisions, can be appealed to the CAA's non-executive directors, who are not involved in the original decision. The appeal is either to one non-executive director, or to a panel of several, acting as a tribunal as specified in the Tribunals and Inquiries Act 1992. For many of these decisions, there is a further recourse to appeal to external bodies after the non-executives' decision. There are other decisions that are not subject to appeal to the non-executives, but which can be appealed to an external body. External appeal bodies include the County Court, the Competition Commission, the Secretary of State and the European Commission. For a few types of CAA decisions there is no appeal available on the substance of the decision, notably airport price reviews and airspace changes.

153. For any CAA decision, there is recourse to Judicial Review, but, as with this remedy generally, this does not address the substantive merits of the original decision. Complainants can also go to the Parliamentary Ombudsman, but only on the basis that the CAA has not acted properly or fairly, or has provided a poor service.

154. The review notes that the CAA has introduced an appeals portal on its website to give better access to appeals and to give appellants guidance on how to use the procedures.

155. The general trend in society is towards increasing levels of litigation. There is no evidence of a similar trend for the CAA, where the number of appeals continues to be low. Over the last five years, 11 safety decisions went to appeal.<sup>7</sup> The CAA's decision was upheld in seven and overruled in three; one decision is outstanding. The CAA has been taken to Judicial Review four times. The Parliamentary Ombudsman considered five complaints about the CAA – none were upheld.

156. Other regulators have a mixture of different remedies, including recourse to the courts, the Secretary of State and to tribunals. For decisions concerning economic regulation or competition issues, the Competition Commission and the Competition Appeal Tribunal respectively are the reviewing or appeals bodies. In this respect, the CAA's setting of price caps at designated airports is an exception, as there is no appeal to the Competition Commission - this is discussed further in Chapter 9 on economic regulation.

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<sup>7</sup> 30 appeals were lodged; 19 of these were withdrawn.

### APPEALS HEARD BY CAA NON-EXECUTIVE DIRECTORS

157. The review heard limited evidence on the CAA's appeals. A number of organisations from the general aviation community wanted a more independent and a less onerous appeals procedure for safety appeals. Some thought that the appeals procedure was too legalistic and formal.

158. In cases where the non-executives make appeal decisions, the process is much more informal than in a Court. Appellants have the opportunity to present their position in writing or by appearing at a hearing and do not need to be represented by a lawyer. By comparison with other approaches, making an appeal does not seem to be overly onerous.

159. The review considered whether the non-executive directors could be considered sufficiently independent to be the final appeals body (Judicial Review aside), or whether an independent external route of appeal might be preferable.

160. It is possible to establish a tribunal, under the Tribunals Courts and Enforcement Act 2007, to hear appeals on regulatory decisions. There was concern that such tribunals might have difficulty dealing with some of the complex issues that arise from the CAA's work. The review received advice that this could be overcome by retaining specialists to attend or sit on the tribunal. But a tribunal would take time and money to set up for what would be a small number of cases. In its last review of the CAA's activities as a tribunal in 2006, the Administrative Justice and Tribunals Council declared itself content with both the CAA's appeals procedures and the way it conducts its hearings. **I recommend that the current appeals procedures involving the non-executives are left in place. The CAA should review other regulatory tribunals to incorporate any relevant best practice into its own procedures.** It may also wish to ensure that its appeal route to non-executive members is fully compliant with Article 6 of the Human Rights Act, which establishes the right to a fair and public hearing.

### APPEALS ON FITNESS OF CHARACTER

161. Where an approval has been rejected because the CAA does not believe an individual's character to be fit, the appeal is heard by the County Court. The review was advised that there is an existing tribunal - the general regulatory tribunal – that could hear these appeals. This would have the advantage of being more accessible and user-friendly than the County Court. **I recommend that the CAA and the Government consider changing the route of appeal for fitness of character decisions so that they are made by the general regulatory tribunal instead of the County Court.** The CAA and the Government will want to ensure that arrangements are put in place for the separate jurisdictions in Scotland and Northern Ireland that take account of the points I have made.

162. In the case of appeals to the external bodies listed in paragraph 152, no evidence was received to indicate that the appeals route was unsatisfactory. The review makes no recommendations in respect of these.

## 6 ENVIRONMENT

163. The review's terms of reference mention the Stern report on the economics of climate change and its impact on the future strategic and operating context for aviation regulation. We have looked at the CAA's general responsibilities and activities concerning the environment, including noise and air quality, as well as climate change.

164. The CAA has manifold responsibilities in relation to the environment. These are derived from international standards, European legislation, and domestic legislation, directions and guidance. The responsibilities apply to a wide range of functions carried out by the CAA. The CAA's corporate plan includes an objective to encourage civil aviation to reduce, control and mitigate the impact of the aviation community on the environment. The CAA supports the principle that aviation should meet its full environmental costs, ensuring that growth in aviation only occurs where these costs are outweighed by the economic and social benefits.

165. There are two main pieces of primary legislation that refer to the CAA's environmental duties. Under the Transport Act 2000, when exercising its air navigation functions, the CAA must balance the environment against a range of other factors determined in the Act. In doing so, it must take account of any guidance on environmental objectives given by the Secretary of State.

166. The second reference is in the Civil Aviation Act 1982. Section 5 requires the CAA to consider environmental factors when licensing an aerodrome that the Secretary of State has specified in an order. In such circumstances, the CAA would be required to minimise so far as reasonably practicable any adverse effects on the environment and any disturbance to the public. The Secretary of State has not used these powers.

167. The CAA also undertakes other environmental activities. Its Environmental Research and Consultancy Department gives authoritative scientific advice to the Government on noise and represents the UK in technical forums nationally and internationally. In safety regulation, there are aircraft engine experts who advise Government on emissions performance for the purpose of international negotiations (paid for by Government). Environmental design issues in respect of aviation have now transferred to the European Aviation Safety Agency. In economic regulation, the CAA can take into account environmental expenditure as part of the airports price control process. It also provides advice on economic instruments related to climate change.

168. The European Union Emissions Trading Scheme (EUETS) is expected to include aviation emissions from flights to, from and within the European Union from 2012. Introducing market mechanisms in this way is a key aspect of European and UK Government policy on transport and the environment. The CAA has been closely involved in the development of this policy and Government is currently considering the extent of the role (if any) that the CAA should play in the regulation of aircraft operators within the scheme.

169. The review has received a wealth of evidence on the environment. Generally, stakeholders thought that the environment was a growing issue and it was important that aviation should develop in a sustainable way. The evidence was clear that Government had a strong role to play in setting a framework for the CAA's environmental activities, rather than leaving the CAA to make trade-offs between

environmental and other issues itself. Many thought that this should be done not only by giving the CAA a statutory duty or responsibility, but also through setting a policy framework or guidance. It was suggested, for instance, that current guidance could be more helpful on deciding whether to reduce flights over tranquil or populated areas.

170. One organisation thought that the CAA should not be given new responsibilities, but rather should factor the environment into its existing activities. Two wanted the Secretary of State to use powers under section 5 of the 1982 Act to require the CAA to assume an environmental role when making decisions on licences for aerodromes.

171. Various organisations thought that the CAA could be a source of independent information and expertise on air quality and climate change, informing the wider public or advising the Department for Transport in a similar fashion as on noise. For the EU Emissions Trading Scheme, the CAA could either take the lead in regulating the UK aspects of the scheme, or play an advisory role, with the Environment Agency in charge. Some organisations did not want the CAA to be involved at all, although a recent Government consultation indicated that a majority of respondents were in favour of the CAA having some part in the scheme.

172. In terms of airspace, some organisations considered that the CAA's Directorate of Airspace Policy (DAP) should be clearer about how it took account of the environment in its decisions. Others thought that the DAP should do more to help reduce emissions through efficient use of airspace.

173. One organisation considered that the CAA's Safety Regulation Group could play a role in helping the aviation community with the certification of environmentally friendly aircraft engines.

174. It is clear to all that the environment is an area of increasing importance in today's society and in the aviation world. It is only likely to grow in stature over the coming years as air traffic movements increase, airspace capacity comes under greater pressure, and public awareness of climate change and health-related environmental issues sharpens. The issues have been highlighted by the public debate over a third runway at Heathrow.

175. The environment cuts across the CAA's four groups – it needs to be taken account of in relation to a range of the CAA's activities even where it is not the foremost consideration. For example, while safety is the priority in considering airspace change proposals, the environment is a key consideration.

176. There is a broad range of views on how to respond to the challenge of aviation and the environment, including strong opinions at either end of the spectrum. As a result, there is a risk that pressure is placed on the CAA to go beyond its role of independent regulator and become a campaign body on the environment. The CAA should continue to maintain its impartial status, as it has successfully done in the past.

177. It would be wrong to give the CAA an environmental responsibility merely because of the growing prominence of the area. But the CAA already takes the environment into account in various areas, as indicated in the introduction to this chapter. There would be a broad welcome for this to be reflected in legislation. **I recommend that the CAA should have a general statutory duty in relation to the environment.** This would fill what is currently a notable gap. It would allow the CAA actively to seek out improvements in existing areas of work and to justify its

intentions to do so. A statutory duty could be expressed so that it did not detract from the pre-eminence that Parliament and the public expect the CAA to give to safety considerations.

**178. The CAA should not be given a general duty in statute without a clear policy framework from Government. The Secretary of State should be responsible for providing a framework which offers guidance to the CAA on how to strike the balance on the inevitably difficult issues where there is a trade off to be made between the environment and other considerations. The framework should make clear the boundary between the roles of the CAA, the Government and other stakeholders. It must give enough of a steer to allow the CAA to make a decision that is aligned with Government policy. But at the same time the framework must not be overly prescriptive.**

179. The review recognises the difficulty of producing an environmental policy framework in the context of aviation. Various factors must be taken into account, such as: the needs of users; the economy as a whole and the aviation sector in particular; safety; and, of course, the environment itself. There may be circumstances where it is difficult to achieve one desirable environmental goal without failing to achieve another. The framework would not be able to envisage every case that might arise, but might state principles which would help the best balance to be struck. To enable changes to be made in what is a fast moving field, the framework should be administrative though, of course, made under a power conferred by statute.

180. Environmental factors are so important to the population at large that, when it is far from clear how best to reconcile conflicting issues, more time needs to be built into the decision-making process. This will help all issues to be fully explained and ensure that stakeholders know what the environmental impacts of a decision will be. Whatever decision is taken, it needs to be fully clear what factors were taken into account, what weighting was given to each of them and how the final decision was arrived at.

181. There are several areas where the CAA could potentially take on a greater role in the future. The review has not considered these areas in detail and is not advocating that they be incorporated into the CAA's remit. But the Department, when pursuing this subject, could consider the CAA's potential role in

- collating and publishing authoritative information on air quality and carbon relating to aviation, so as to help promote a shared understanding among stakeholders in these areas. The review understands that there is an information gap in this area and
- spreading best practice (for example, innovative airport operations to cut taxiing emissions).

182. Evidence received by the review made reference to the Secretary of State's powers under section 5 of the 1982 Act. The review believes that this is a blunt instrument, as the only means the CAA would have of incentivising environmental performance at airports would be to threaten the removal of their licence. **I recommend that the Department for Transport propose the repeal of section 5 of the 1982 Act.**

183. Paragraph 165 of this chapter mentions existing environmental guidance. **The Secretary of State's guidance on environmental objectives in relation to the CAA's air navigation functions is now nearly six years old. I recommend that it be reviewed to ensure that it continues to be up to date.**

## 7 INTERNATIONAL

184. The terms of reference asked the review to look at the CAA in relation to the evolving roles of the International Civil Aviation Organisation (ICAO) and Europe in aviation regulation.

### INTERNATIONAL CIVIL AVIATION ORGANISATION

185. The International Civil Aviation Organisation (ICAO) is an agency of the United Nations - the global forum for civil aviation – and was set up in 1947 within the framework of the Chicago Convention. Its 190 member states work together to achieve the safe, secure and sustainable development of civil aviation through the adoption of standards and recommended practices regulating international air transport.

186. The UK is an active member of ICAO and has always held a seat on the 36-strong elected Council that manages business between the three-yearly General Assemblies. This business represents a significant area of work for DfT and the CAA. The CAA seconds a member of staff to DfT to sit on ICAO's senior technical body – the Air Navigation Commission.

187. In contrast to the European Union, where the supra-national European Commission and European Parliament are key players in decision-making, in ICAO, member states alone are responsible for making decisions. The European Commission participates as an observer.

188. The review has not received evidence arguing for DfT and the CAA to change the way they work in ICAO and, unless there is any move to member states being represented by supra-national bodies, the review would not recommend any changes to current practice.

### THE EUROPEAN UNION

189. In all four of the CAA's regulatory areas and in the fields of environmental protection, security and external relations, it is apparent that the influence of Europe is rising, to the extent that airport construction and planning is the only major policy area remaining entirely the responsibility of member states. Until 1990, aviation safety was regulated by individual nations, within the framework provided by ICAO. In that year, a number of European member states created the Joint Aviation Authorities (JAA) – a non-statutory assembly of the European Civil Aviation Conference - with the aim of achieving a high, consistent level of aviation safety, harmonising standards with the USA. Although the JAA is still in operation, much of its work has been taken over by the European Aviation Safety Agency (EASA), created under European law in 2002 as an agency of the European Community. EASA's rules differ from those adopted by the JAA and ICAO in that they are legally binding – member states cannot opt out.

190. EASA is responsible for preparation of rules in the fields of design, production and maintenance, and standardises the way that National Aviation Authorities ensure these rules are applied. It also covers continuing airworthiness (design) and the issue of type certificates for aircraft. In future, its role will be extended to include the

preparation and standardisation of rules for flight operations, flying training organisations, air traffic service providers, aerodromes and flight crew licensing. The CAA is designated as the UK's NAA for the purposes of implementing the European safety framework. It assists in the development of safety rules by participating in the rule-making process and provides the UK member of the EASA Management Board. The advent of EASA means that many tasks once carried out by the CAA have now transferred to Europe, although the CAA retains responsibility in a number of areas (the split of responsibilities between EASA and the CAA is set out in Annex D). The way that the CAA has adapted to these changes is an important area for this review and is covered in the EASA section below.

191. The European Union, on the initiative of the European Commission, is taking a greater role in respect of air traffic management (ATM) in order to tackle the current and predicted air traffic congestion generated by an increasing number of air traffic movements. It is taking forward the Single European Sky (SES) programme, which aims to increase capacity, eradicate delays and reduce costs by restructuring European ATM arrangements. DfT and the CAA are represented on the Single Sky Committee, the main forum for engaging member states. SES has four main strands

- introducing performance regulation to ATM, facilitating integration of service provision and improving environmental performance
- extending EASA's safety remit to cover ATM and aerodrome operations
- research to exploit new ATM technology, introduce innovative procedures and enhance the synchronisation of airborne and ground systems, looking to the next 30 years and
- taking forward a European action plan for airport capacity, efficiency and safety, recognising that airport infrastructure is critical to European aviation.

192. Eurocontrol was founded in 1963 as the European Organisation for the Safety of Air Navigation. It is made up of 38 member states (and the European Commission, which joined in 2002) and has technical expertise in air traffic management issues. Eurocontrol has been formally contracted by the European Commission to assist with the implementation of the Single European Sky by developing Single European Sky implementing rules. These rules cover diverse areas including the flexible use of airspace between civil and military use, airspace classification and design, functional airspace blocks, common charging schemes, interoperable systems and air traffic flow management. Eurocontrol consults on the rules it develops and the CAA contributes to the process.

193. The European Union has been increasingly active in the field of economic regulation, with a near finalised Directive on airport charges. It has also created an economic framework for the regulation of air traffic management, mandating the separation of regulation and service provision. In consumer protection, the EU has adopted legislation to enforce passenger rights on denied boarding, cancellation and delays, on passengers of reduced mobility and on minimum levels of insurance for air carriers and aircraft operators.

194. As a result of European initiatives in all these areas, there is now less scope for national Governments and regulators to create and implement their own policies. This makes it important for them to influence policy development and regulation in Europe. As part of evidence-gathering, the review met the European Commission, EASA and Eurocontrol. These organisations set out their role in developing European aviation and emphasised the high value they attached to the CAA's input. These latter comments were echoed by DfT's representative in ICAO.

195. Several organisations were complimentary about the CAA's expertise at the European level, particularly with regard to their input on economic regulation issues. But others thought that the CAA should do more to help shape the development of aviation regulation in Europe in line with UK objectives and the needs of UK aviation. Either way, there was general agreement about the importance of furthering the CAA's influencing power and networks in Europe to help achieve common goals, build constructive relationships and learn from best practice in other Member States. For instance, it could help promote the consolidation of air navigation service providers across Europe. It was said that the CAA needed greater representation on safety rule-making groups. The CAA's influence could be improved through placing or seconding staff into organisations like EASA.

196. There was some sense that the CAA had taken over too much of DfT's remit in Europe. On the other hand, it was clear there was pressure on DfT to transfer more functions to the CAA, based on the CAA's technical expertise and DfT's limited resources. Others thought, and it was expressed clearly at the dialogue events held by the review, that if the CAA was involved in such work, it should be funded by the taxpayer, not the aviation community.

#### **CAA AND DFT'S ROLES IN EUROPE**

197. Influence at the early stages of European regulatory policy development is essential and this will involve DfT and the CAA participating in ad-hoc discussions with the European Commission and other participants to try to shape issues in a way that is beneficial for the UK and for Europe. Often discussions will be about potential proposals from the Commission for European legislation.

198. It is also important for the UK to be present at EASA and Eurocontrol working groups, where implementing rules for safety and airspace are developed. The CAA usually participates in the development of these rules, with DfT getting involved when the rules are finalised.

199. Following proposals for new legislation, negotiations take place between Member States and the European Commission, where the UK is represented at the highest level by Ministers or by UKREP (the UK Permanent Representation to the European Union, part of the Foreign Office). This report is concerned with what goes on beneath these levels to brief Ministers and UKREP, and where DfT and the CAA become involved. UKREP speaks in European Council working groups chaired by the Presidency. DfT leads in providing advice and the CAA gives technical support as appropriate. In other groups chaired by the Commission, DfT normally leads, with the CAA in support, although the CAA sometimes leads on issues requiring significant technical expertise.

200. There are also other types of European meeting outside the legislative and rule-making process, attended variously by DfT or the CAA, including the Council of Eurocontrol, the EASA Management Board and the Single Sky Committee.

201. It is clear from our evidence that the CAA has a strong role to play in influencing European affairs and that the expertise they bring to the table is welcomed in Government, the UK aviation community and across Europe. This must be balanced against the need for DfT to continue to lead in certain areas of European engagement, particularly where there are issues of national interest at stake, and where issues cutting across different policy areas must be considered. This accords with the principles the review has developed in Chapter 3 on the CAA's role and

status for defining the boundary between the CAA and DfT. The national interest will best be served if both organisations approach the responsibilities that each must undertake in relation to Europe in a spirit of partnership.

202. The review considers that the broad approach of keeping the CAA in charge on technical groups across the range of its functions, with DfT in the lead on the rest, is roughly correct at the moment. But with DfT coming under increasing pressure to reduce headcount and given its occasional tendency to underestimate the importance of its own non-technical role in negotiations, there is a risk that the CAA could be left to work too much on its own in Europe. Mainly because of the argument about DfT's and the CAA's appropriate roles and also because of DfT's negotiating skills and knowledge of the European process, **I recommend that DfT should stay in the overall lead on European engagement, in particular liaising with the European Commission over emerging policy and on high-level negotiations. DfT should be resourced to fulfil this, with CAA support as necessary. But there will be a range of activities in the middle ground where either DfT or the CAA could take the lead. In areas that are technical and without wider policy implications, DfT may see fit to cede full responsibility to the CAA. Whichever of them is in the lead, it is imperative that the CAA and DfT continue to work in partnership, using the rules of engagement that I go on to propose.**

203. Where an aspect of European work has policy implications, in particular where the boundary between Europe and national Governments could shift, and where there are trade-offs with other (non-aviation) issues, DfT should lead. It should also take the lead in most cases when lobbying the European Commission and Parliament, particularly for aspects of European work that touch on the work of other Government Departments.

204. In technical discussions and negotiations, it is likely to be appropriate for the CAA to take the lead. The line taken at these meetings should be on the basis of an agreed position, as set out below.

205. The Department and the CAA should continue to observe the following rules of engagement when working together in Europe

- both organisations should recognise that their effectiveness in representing the UK's position in Europe depends on genuine partnership
- where the Department is involved in European work in which the CAA has an interest, based on its statutory functions, DfT should consult the CAA in formulating the negotiating line and fall-back positions before the European meeting
- if the two organisations will be engaging together in Europe, they should work together beforehand to arrive at a shared view of the UK line and the fall-back positions
- where the CAA is working alone in Europe, it should agree the line and fall-back positions beforehand with the Department, and in all international contexts it should support known Government positions.

## **SKILLS AND TECHNIQUES FOR SUCCESS IN EUROPE**

206. The volume of work to be done in Europe is growing, along with the level of technicality, particularly in safety and airspace. This means that, notwithstanding the recommendation I have made, the Department's presence will not always be

required or justified and the CAA will need to be effective negotiators and influencers in Europe.

207. In order to excel in this environment, it will be helpful for CAA to reinforce its current practices, including work it is undertaking to improve in a number of fields. Both organisations should continue efforts to join up on European issues. The Department currently has an industry liaison group that the CAA attends, which helps communicate UK policy and European developments. Further briefing on European developments from DfT to the CAA will help improve the CAA's effectiveness. The CAA should also maintain current efforts to join up internally. As mentioned in Chapter 4 on corporate governance, Europe is an issue that cuts across the CAA's four groups, and a Chief Executive would help to coordinate the organisation's approach to these issues and increase its ability to engage effectively in Europe. The CAA already has internal steering groups on EASA, Single European Sky and other European issues. It has conducted European workshops at Board level and below.

208. The review is encouraged by the training arrangements in the CAA directed at improving representatives' negotiating skills and knowledge of European institutions and processes. It is not possible successfully to conduct much of the European work without the help of experts. Consequently, increasing the effectiveness of experts through training is important. It will increase their awareness of when DfT need to be involved and when they do not.

**209. There is a useful contribution already made by two or three members of staff whose expertise is in the fields of policy and international negotiation. I recommend that the CAA consider increasing this number to about half a dozen and maintaining it at around that level.** These non-specialists would be able to move between CAA groups and undertake secondments in European institutions or other UK regulators, helping to bring a new perspective and fresh ideas to the organisation.

210. To this end, it will be helpful to encourage the transfer of employees between the CAA and European institutions and vice versa, either on a secondment or on a more permanent basis. The review understands that the CAA has already seconded staff to the Commission and EASA and is developing its secondments policy with DfT involvement. The review believes that, given the increasing interaction with Europe, experience working for a European institution will become a significant advantage for those applying to senior positions in the CAA. The current split of nationalities amongst EASA staff is set out in the table below. This shows that the UK has about half as many staff in EASA as France or Germany.

Nationality of EASA Staff	%
France	24
Germany	23
UK	12.5
Italy	8
Belgium	6
Netherlands	6
Spain	4
Greece	4
Others	12.5

**THE INTERFACE BETWEEN THE CAA AND EASA**

211. The transfer of work from the CAA to the European Aviation Safety Agency (EASA) was studied by the Transport Committee's report on the work of the CAA in 2006. This report expressed strong concerns about the harmonisation of safety regulation through the creation of EASA and the possible impact on safety. A year and a half on, the review has found stakeholders to be more moderate in their views of the Agency.

212. I have not made any specific recommendations in this section, as the review is not concerned with the detail of safety matters, particularly when these relate to EASA, not the CAA. I record the evidence we have received and the CAA's responses. Nonetheless, this report proposes new governance arrangements for the CAA and a new way of dealing with Europe that together will increase the ability of the organisation flexibly to adapt to changes from outside. Whether the CAA has the power to act itself, or whether it must influence in Europe to secure change, these measures should help to improve the safety regulatory regime for all concerned.

213. Several organisations mentioned the benefits of having harmonised safety regulation across Europe. Many thought that the CAA's Safety Regulation Group should become an agency of EASA, rather than part of the national regulator. To some extent, this view was driven by the hope that it would lead to reduced charges overall. EASA itself said that it had no plans to eliminate the role of national regulators. This was unsurprising because the present arrangements for safety reflect a division of responsibilities between Member States and the central European institutions which is common across other areas of EU business. The review also received comments about EASA's performance, including its style of regulation, its ability to recruit and retain staff, its role in safety research and its charges schemes, amongst other issues. These issues are outside our terms of reference.

214. There was concern that important safety tasks might fall between the CAA and EASA during the transfer of functions – the examples of safety research and airworthiness directives were given in evidence. The CAA said that it had addressed this concern with EASA. The organisations had also considered the challenge of retaining sufficient skilled certification expertise in the system and how far EASA's work should be centralised in Cologne (where EASA is based) rather than carried out locally. These issues led to the establishment of the EASA National Aviation Authorities Certification Transition Working Group (or ENACT), a sub-group of the EASA Management Board that identifies and seeks to resolve potential gaps. ENACT is co-chaired by the Executive Director of EASA and the UK member of the EASA Management Board.

215. Many thought that the CAA had not reduced staff sufficiently in response to the transfer of some functions to EASA. The CAA informed us that its aircraft certification function, which had had a particularly strong involvement in the approval of product design and of design organisations before EASA was created, had reduced its staff from 120 people in 2003 to 40 today. It did not expect further reductions as a result of the extension of EASA's scope into operations and licensing as the CAA would still be required to implement these requirements. On the contrary there would be new tasks from increased regulation of non-commercial operators (e.g. glider pilots) and from EASA standardisation audits.

216. A number of organisations said that a certain amount of duplication of costs remained between the CAA and EASA. One organisation clarified this further with an example. It explained that although design had been transferred to EASA, and

design experts were in EASA, the maintenance and manufacturing regulation teams in the CAA would need to retain design experience in-house because of the synergies between the fields. In addition to this, organisations had on occasion needed to brief both the CAA and EASA on certain issues. The duplication of costs could be seen in part as an inescapable consequence of dividing regulatory responsibilities between two organisations when originally they were carried out by one. The CAA said that it had a number of standing committees and focused working groups that met regularly and which afforded the aviation community the opportunity to raise concerns about overlaps.

217. Some witnesses considered that the CAA had a tendency to implement EASA rules more strictly or earlier than other European countries, leading to higher costs for UK operators compared with their European competitors. This concern was also reflected in comments that the safety record was worse in other parts of Europe. The EASA standardisation regulation aims to address these concerns by requiring that EASA oversee the application of its rules across Europe in a uniform way. It is clear that the CAA has the difficult task of appropriately balancing the need to maintain the UK's high safety standards with minimising the regulatory burden on the aviation community.

218. The Transport Committee's report stated that there was significant confusion among the CAA's stakeholders over the transfer of functions between the CAA and EASA. The review notes that this confusion still exists and refers to this issue in Chapter 10 on the CAA's stakeholders. The evolving split of responsibilities between EASA and the CAA is set out at Annex D. The CAA itself is well aware of the need to communicate actively on the scope and timing of the transfer of work and maintains a section of its website which provides information about EASA.

#### **CAA INTERNATIONAL**

219. Since its inception, the CAA has provided consultancy and training services in the UK and overseas on a commercial basis, as permitted under section 16(5) of the 1982 Act. CAA International Ltd was formed in April 2007 as a wholly owned subsidiary to put these activities on a better business footing and to ensure proper separation between the CAA's regulatory and commercial work. CAA International has a Board of six directors, all of whom are members or employees of the CAA.

220. The review has heard little evidence from the CAA's stakeholders about CAA International. Nonetheless, it is clear that CAI's work helps to raise safety standards internationally, to the benefit of UK and other air passengers. The existence of this work generates an opportunity for CAA staff to gain wider experience, which is beneficial for their UK work. It also allows the CAA to retain skills where its UK-based work alone would not sustain a full-time member of staff. The profit generated by the company reduces the charges paid by the UK aviation community.

221. I believe that there are advantages for the UK aviation community, passengers globally and the CAA in the work carried out by CAA International, subject to the CAA continuing to manage the risks involved.

## 8 PASSENGERS

222. Since increased security requirements were introduced at UK airports in the summer of 2006, aviation has seen an increased focus on the quality of the experience for air passengers. As part of this, in November 2007 the Department for Transport published “Improving the air passenger experience – an analysis of end-to-end journeys with a focus on Heathrow”<sup>8</sup>. The Department is currently looking at the air passenger experience at other major UK airports.

223. This chapter pulls together several passenger-related strands of work that are relevant to the CAA. First, the review considers whether the CAA’s Economic Regulation Group and Consumer Protection Group should be merged. It goes on to look at the Consumer Protection Group’s responsibilities for the ATOL scheme and for regulating the financial fitness of air operators, both of which the CAA performs in order to meet requirements in European legislation. The chapter also covers the Air Transport Users’ Council and its formal relationship with the CAA.

224. The way that the CAA’s Economic Regulation Group regulates airports plays a significant part in the passenger experience. The review covers this issue in Chapter 9 on economic regulation.

225. We note that the CAA and the Office of Fair Trading are working together with a view to the CAA becoming more involved in enforcement of consumer issues, such as airline terms and conditions. The two organisations are developing a Memorandum of Understanding to this effect. The CAA also has a role in enforcing EU passenger regulations.

226. The review received evidence suggesting that the CAA should have a general responsibility towards consumers across all its functions, as distinct from a specific consumer responsibility for economic regulation. In Chapter 3 on the CAA’s role and status, the review recommends that DfT and the CAA work together to tidy up the legislation relating to the performance of the CAA’s functions. In doing so, they might take account of the potential for a general duty related to passengers or consumers.

### CONSUMER PROTECTION GROUP AND ECONOMIC REGULATION GROUP

227. A number of stakeholders have suggested the possibility of changing the structure of the regulatory groups in various ways, including a merger of SRG and DAP and, separately, of CPG and ERG. None have addressed the point in depth.

228. The roles of the CAA’s Consumer Protection Group and Economic Regulation Group are set out in Chapter 3 on the CAA’s role and status. Until 1998 consumer protection and economic regulation were the responsibilities of a single group. According to the CAA, they were separated because the consumer function had become largely autonomous and the director found it hard to give the growing number of ATOL licensees the attention they deserved while at the same time focusing effectively on the demanding price review processes.

229. The review notes that there is an increased focus on passenger issues and this is likely to be here to stay. Bringing consumer issues into ERG might enhance the

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<sup>8</sup> “Improving the Air Passenger Experience – an analysis of end-to-end journeys with a focus on Heathrow” – November 2007

passenger focus in the price reviews. There may be some efficiencies to be gained by joining the groups together. CPG might share with ERG their skills in corporate finance and credit analysis for use in price reviews and commercial knowledge of the aviation industry could pass both ways. The merger might provide stakeholders, particularly airlines, with a single point of contact for economic and consumer issues, although we recognise that different individuals are likely to be involved in each case.

230. Both groups are currently in or about to enter into transition phases. CPG is taking the lead on significant changes to the way the ATOL scheme is funded, introduced in April this year. ERG is possibly to adopt a new economic regulation framework in the next few years depending on the outcome of the Competition Commission and Department for Transport reviews. Any organisational change on top of these challenges would be unwise. The position is quite likely to be different in, say, five years' time. By then any new regime for economic regulation should have been introduced and bedded in. It could well have been possible to capitalise on the remaining opportunities to outsource some of the ATOL work provided the April 2008 initiative is working effectively. **I recommend that the CAA examine the case for a merger of its Economic Regulation and Consumer Protection Groups in 2013 and bring it about if the savings are no longer outweighed by the risks.**

#### **AIR TRAVEL OPERATOR LICENSING (ATOL)**

231. The ATOL scheme was created by the Civil Aviation (Air Travel Organisers' Licensing) Regulations 1972 to protect holidaymakers against the risk of their tour operator or travel agent going bankrupt. Having paid upfront for their holidays, consumers would be repatriated if they were abroad at the time and refunded if they had not yet travelled. The UK regulations were subsequently reinforced at the European level by the 1990 Package Travel Directive, regulating package travel across all transport modes. The ATOL scheme is the UK's way of complying with this Directive in respect of aviation. In the year to March 2008, the scheme repatriated or refunded around 21,000 holiday-makers and paid out approximately £5 million to consumers. The CAA works closely with Trading Standards to enforce ATOL and, specifically on this issue, reports jointly to the Department for Transport, and the Department for Business, Enterprise and Regulatory Reform.

232. Tour operators selling air package holidays are required to hold an ATOL licence. Until April 2008, ATOL holders were obliged to lodge a bond with the CAA as insurance against their potential bankruptcy. In cases where the bond was insufficient to meet repatriation and refund costs, the remainder would be made up from the Air Travel Trust Fund. In April, bonds were primarily replaced by a per-passenger contribution, called the ATOL Protection Contribution, which is generally considered to be less onerous on the travel industry. The CAA aims to build up a stable fund in the Air Travel Trust from these contributions.

233. ATOL involves two main activities: issuing tour operators with ATOL licences, following a check on their financial fitness and crisis management, which handles claims for refunds and repatriation of stranded holidaymakers. Licensing of about 200 smaller tour operators is outsourced to four external organisations, who take on the administration and most of the financial risk. The remaining operators are licensed in-house. The call centre for customer queries, which deals with the aftermath of ATOL holder failures and other information about ATOL, is outsourced to a commercial organisation. Management of repatriation and complicated refund cases are conducted in-house.

234. Several organisations thought that the law requiring protection of air package holidays through ATOL was old-fashioned in a society where many are protected through their credit cards. But they acknowledged that it would be difficult to revoke the scheme for political and legal reasons. One airline thought that there was scope to outsource ATOL. This could lead to efficiency savings and could also free up the CAA's Consumer Protection Group to focus on wider consumer issues. Another stakeholder was concerned that outsourcing could lead to less effective enforcement.

235. Approximately two-thirds of Consumer Protection Group's 71 staff currently work on the ATOL scheme. Much of the work on the scheme could be described as operational. The review considered whether more aspects of it could be outsourced, thereby achieving cost savings for the CAA and those that pay its charges.

236. Over the past few years, the CAA has already outsourced a number of activities. Three main areas remain in-house. Of these, the CAA has argued convincingly that repatriation should remain with them, on the basis that the CAA's staff are able to use contacts in the aviation business to secure charter planes at short notice. Outsourcing could significantly increase costs here.

237. The second area is making refunds to passengers affected by tour operator failure. Here, until recently, bonding arrangements could require complicated decisions on refund policy and this limited the outsourcing of claims payments to around three-quarters of all refunds. Once the new arrangements have bedded in, and provided a stable financial position has been achieved, this function will probably be suitable for outsourcing in its entirety.

238. The third and by far the largest area in terms of staff numbers is ATOL licensing. Until recently, financial institutions have been reluctant to take on all the financial risk associated with licensing ATOL holders. Nonetheless, as the Air Travel Trust Fund builds a substantial surplus, which it is hoped will be in the next three to five years, the CAA is committed to consulting on the restructuring of the fund. At this stage, the case for outsourcing the management of the Fund and realising efficiency savings will be stronger. **I recommend that the CAA keep Consumer Protection Group's ATOL work under consideration to identify potential efficiency savings from further outsourcing within the next three to five years and that the Department ask the CAA for progress reports in September 2011 and September 2013.**

239. Some evidence proposed that the CAA should, in addition to its role in regulating aviation package holidays, take over non-aviation holidays. This would enable organisations with both types of business to be regulated by a single authority. I understand that this proposal has been under consideration by the Better Regulation Executive and the Department for Transport and is on hold while the new ATOL Protection Contribution has had time to settle in. I make no recommendations in this area.

## FINANCIAL FITNESS

240. In order to carry passengers, cargo or mail for payment, air operators based in the European Economic Area must hold an operating licence granted by the Member State in which they have their principal place of business. The CAA grants such licences for UK airlines. To obtain a licence, or to maintain it in force, operators of aircraft with 20 seats or more must meet certain financial as well as safety criteria.

241. Article 5 of European Regulation 2407/92 sets out the specific financial requirements. These are more onerous in the first two years of an air operator's existence. Thereafter, monitoring is less intense and the CAA only looks at the business plan and management accounts, although it has the power to revert to more intense scrutiny if it has any concerns.

242. We heard argument that the requirements for monitoring of financial fitness – particularly for established airlines – were onerous and expensive and could be dispensed with. When airlines were listed on the stock exchange, scrutiny of their financial position was likely to be just as intense, if not more so, than what was done by the CAA. This view was not shared by all airlines.

243. The requirement for monitoring of financial fitness is at a European level and the UK cannot choose unilaterally to discard it. Nor does it seem sensible to challenge the requirements for start-up operators, which have a higher likelihood of failing to meet their obligations to financiers and customers than more established operators.

244. The CAA considers their scrutiny of established airlines, as described, to be relatively light touch. Some airlines find their dialogue with the CAA productive, and say so. The CAA did not feel that resources could be squeezed further in this area – there were only two staff working on financial fitness – and a reduction might bring about infraction proceedings from the European Commission or, of course, failure to spot an airline in financial difficulty.

245. The requirements for scrutiny of established operators do not seem to be overly onerous and there is little scope for efficiency savings within the CAA from halting this activity. **I recommend that the CAA should continue to carry out its oversight of the financial fitness of air carriers along current lines.**

#### **CONSUMER PROTECTION AND AIR PASSENGER RIGHTS**

246. Air passenger rights have increased over recent years with the coming into force of EC regulations on denied boarding and cancellation, and on persons of reduced mobility. The CAA is the enforcement body for these regulations and works closely with industry to ensure that core passenger rights are upheld.

247. The CAA is also empowered to take action under general UK consumer protection legislation. Under Part 8 of the Enterprise Act 2002, the CAA can take action against the aviation industry for breaches of UK consumer law. This includes enforcing provisions relating to unfair contract terms and the information that air travellers must be provided with at the time of booking. In May, consumer protection was strengthened with the Consumer Protection from Unfair Trading Regulations 2008. In consideration of the increasing importance of consumer rights, the CAA is reviewing its approach to consumer policy and developing its consumer protection policies and procedures. Included within the scope of the consumer review is the work commissioned by the Secretary of State on improving the air passenger experience. **I recommend that the CAA should continue its work on developing consumer policy.**

## AIR TRANSPORT USERS COUNCIL

248. The AUC was founded in 1973 and is a non-statutory body working from the CAA's London offices. It has a budget of twelve staff and a Council of fourteen members (not including its Chairman). Its remit is in areas of work relating to the direct interface between airlines/airports and the air passenger. This falls outside the CAA's regulatory responsibilities. Its three main functions are to provide information to passengers, to mediate between airlines/airports and passengers where passengers have not been able to resolve an issue directly and to act as a consumer advocate by formulating policies, issuing reports and responding to consultations to further the reasonable interests of passengers. It is free to express its own opinions in matters relating to consumers. The AUC may also commission research in support of these functions.

249. The AUC is funded by a specific charge that the CAA makes on airlines, although it has freedom to seek funding from other sources. Its budget is £0.8 million per year. The CAA agrees the AUC's business plan, operational and financial objectives, and performance indicators. The AUC is subject to the CAA's internal audit. Its Chairman, Council Members and Chief Executive are appointed by the CAA, in conjunction with the AUC where appropriate.

250. The recent House of Lords report on Economic Regulators,<sup>9</sup> pointed to two types of consumer body – those that were closely linked to the regulator like the AUC and those that stood apart and reported direct to the Secretary of State. Stand-alone consumer bodies can take a more challenging stance towards the regulator and are more transparently independent. But they can lead the regulator to eschew softer aspects of consumer policy to concentrate solely on competition. If a consumer body is closer to the regulator it can influence all aspects of regulatory policy from inside the tent, but possibly at the cost of transparency.

251. Many consumer bodies operate in sectors where market forces hold less sway than aviation and which also deal with essentials for life, such as water, gas and electricity. The presence of competition on most airline routes led some witnesses to question the need for the AUC's existence.

252. I believe that the AUC carries out a useful function in relation to helping passengers and that it should continue to do so. The current informal structure whereby the AUC sits alongside the regulator allows it the opportunity to have an impact on the CAA's policies and regulatory decisions, but its lack of formal separation does not meet the regulatory best practice embodied by the consumer bodies set up in the past decade. For example, its lack of a statutory basis means that in theory the CAA could abolish the AUC, although in practice this is of course very unlikely to occur. **I recommend that the Department for Transport propose legislation to put the status and functions of the AUC as a specific aviation consumer body on a firm statutory basis.** This was originally suggested as an option in the Government's 2000 consultation document "The Future of Aviation", but was not adopted.

253. **I recommend that in developing legislation for the AUC, more weight should be given to its existing role as consumer advocate. It would make sense for the AUC to retain its present responsibility for handling complaints. The Secretary of State should be responsible for approving the CAA's appointment of the AUC's Chairman and Council members. The Chief**

<sup>9</sup> UK Economic Regulators – House of Lords Committee on Regulators – November 2007

**Executive would be nominated by the Council and approved by the CAA. To avoid any perception that the organisations are too close, the AUC should work from its own premises.**

254. These recommendations are prompted not by any evidence of past problems, but, in line with accepted good practice, to clarify the respective roles of regulator and consumer body.

**255. I recommend that the AUC's funding arrangements remain the same and that the CAA should continue to set the level of funding in response to business plans from the AUC. The new legislation should give the AUC the right to appeal to the Secretary of State if it wishes to challenge the CAA's view of the proper level of funds. The AUC should produce accounts.**

## 9 ECONOMIC REGULATION

256. The CAA's Economic Regulation Group regulates airports and air traffic services and provides advice on aviation policy from an economic standpoint. It acts as expert adviser to the Government and collects, analyses and publishes statistical information on air carriers and airports.

257. Under the Airports Act 1986, the CAA regulates the charges paid by air carriers at airports designated by the Secretary of State (currently Heathrow, Gatwick and Stansted) and deals with complaints about the conduct of airports. The Act requires that, before determining the charges, the CAA must make a reference to the Competition Commission. The Competition Commission then makes a non-binding recommendation to the CAA on what the price caps on airport charges for the following period of five years should be. The Competition Commission also decides whether the airport has pursued a course of conduct against the public interest. In addition the CAA has functions under the European directive on ground handling at airports.

258. Under the Transport Act 2000 the CAA is the economic regulator of NATS (En Route) plc (NERL), the provider of en route air traffic services in the UK. The CAA exercises this role mainly through monitoring, modifying and enforcing the conditions of NERL's licence, including setting five yearly price caps. In this case, there is no automatic referral to the Competition Commission. But the CAA may refer matters to the Competition Commission, in which case the Competition Commission's findings are conclusive.

259. In giving evidence to the review, one organisation observed that the process whereby the CAA set price caps for NERL was overly protracted. They also observed that the extensive requirements for NERL to publish commercial information set them at a disadvantage to many of their European competitors who were not subject to such requirements.

260. The terms of reference explain that this review is "complementary to (but separate from) the Competition Commission inquiry into BAA, which may comment on the CAA's specific powers for the economic regulation of airports." Following the Competition Commission's emerging findings in April 2008, the Secretary of State for Transport announced a further review of the economic regulation of the UK airports system, with an advisory panel chaired by Professor Cave. With two specialist reviews looking into the UK airports market, there is little scope for me to make detailed comments.

261. Much evidence has been given on the economic regulation of airports and it is right that it should be recorded. The subject matter is contentious and has a significant impact on the aviation industry at the designated airports. It is also a live issue - during the course of the review, the CAA set price caps at Heathrow and Gatwick airports and made its automatic reference to the Competition Commission for the review of prices at Stansted. In January 2008, the Secretary of State for Transport de-designated Manchester airport for the purposes of price review. The inquiries mentioned in the previous paragraph are in progress.

262. Neither the airlines nor BAA thought they had obtained a good deal from past price settlements. For example, airlines were extremely disappointed about both recent and potential price rises at the designated airports, together with what they described as a poor level of service. On the other hand, BAA felt that the rate of

return on capital imposed on them for the Heathrow and Gatwick price review significantly reduced their incentives to invest.

263. A number of the CAA's stakeholders thought that the statutory framework in the 1986 Airports Act was a major contributor to this state of affairs. Whilst there was general agreement that investment in airport infrastructure was necessary, particularly at Heathrow and Gatwick, many believed that the current framework placed inappropriate incentives on BAA to maximise capital expenditure and not necessarily in the right areas. One stakeholder expressed the view that BAA should be licensed like NATS, with a statutory obligation to provide new infrastructure. It thought that the current absence of such an obligation meant that BAA was afforded an overly strong position in negotiations. Another proposal was to give the CAA a duty to promote competition.

264. Some stakeholders, almost exclusively airlines, extended their criticism to the CAA's performance. A number of airlines declared a total loss of confidence in the economic regulator's ability or willingness to regulate BAA, leading them to propose the appointment of an alternative regulator. They variously cited a number of failures including the lack of early 'thought leadership' to push for regulatory change, an overly lengthy, complicated and resource-intensive consultation process, an unwillingness to enforce information disclosure and prevent 'gaming' from the airport during the constructive engagement process, an excessive focus on regulatory theory when setting price caps, a lack of understanding of the realities of the aviation business, an impression that the CAA was not listening during consultation, and lastly a tendency for CAA decisions to emerge in favour of the airport.

265. Various organisations said that there was a lack of clarity about who in the CAA made the final decision on airport price reviews. Others thought that decisions appeared to have been made by an individual – the Group Director of Economic Regulation - and that the Board was not accountable. In practice, price review decisions are made by a panel consisting of two non-executive directors and the Group Director of Economic Regulation. I have addressed the way that the CAA Board makes this and other decisions in Chapter 4 on the CAA's corporate governance.

266. The CAA has responded to all these criticisms, both in evidence to the review and in documents provided to the Competition Commission's market inquiry into BAA airports. It said that many of its critics have their own vested interests and thought that many of the comments made against it related to the regulatory framework rather than how the CAA implemented it. For instance, price reviews were lengthened by the mandatory reference to the Competition Commission. The CAA believed that it had sought to promote better consultation through Constructive Engagement. Whatever the imperfections of this process, it had led to an improved consultation framework. Further, the CAA said that the outcome of the review could not be said to favour the airports, given the marked reduction in cost of capital for BAA. The review does not attempt to make a judgment about the fairness or unfairness of the criticisms made of the CAA. But it is clear that the economic statutory framework is in need of revision: an issue for the DfT Review and which the Competition Commission may also address.

267. The criticism of the CAA was by no means universal. One organisation believed that the CAA's understanding of the economics of the airports market constituted an exceptional repository of expertise: probably the leading source in the EU. Another commented favourably on the expert studies on current aviation issues that it produced. Several more praised the advice that the CAA, acting as expert

adviser to the Government, had brought to the table in bilateral and multilateral negotiations on air service agreements. There was also acknowledgement of the CAA's role in liberalising the airline market.

268. A few organisations, including the CAA, thought that the power to choose which airports should be designated for economic regulation should be transferred from the Secretary of State to the CAA. Another said that DfT should retain the power. The House of Lords Committee report on Economic Regulators, published in November 2007, favoured the former option, saying that this would help the CAA to stimulate competition.<sup>10</sup> It is noteworthy that the Secretary of State earlier this year used her statutory powers, rejecting advice from the CAA about the de-designation of Stansted. If the issue continues to be debated, it is best approached when the Competition Commission has completed its work, and therefore I have not addressed it in this report.

269. The Airports Act 1986 contains a duty for the CAA “to further the reasonable interests of users of airports within the United Kingdom.” The definition of a user in the Act is broad. Amongst others, it includes passengers and air carriers. In this respect the CAA's airport regulation duties differ from those of many other UK regulators who have a principal duty to promote consumer interests.

270. A number of organisations thought that the needs of consumers should be given greater prominence when regulating airports. It was pointed out by one organisation in particular that different consumers had different service level expectations, but that this was not taken into account in the price cap settlements. Others thought that consumer needs should be taken care of by the market. In particular, airlines have said that they are proxies for the passenger and the passenger will be helped if airlines' interests are served.

271. In evidence to the Competition Commission's market investigation of BAA in February 2008, the CAA pointed out that “although airlines' interests will often align with consumer interests, there may be divergences.” It suggested that there needed to be clarity about the CAA's precise responsibilities towards the consumer in relation to airport regulation.

**272. I recommend that the DfT review of the economic regulation of airports should consider whether the CAA's current duty towards users should be amended to give greater weight to passengers or consumers.** Chapter 8 on passengers deals with some broader consumer-related issues.

273. Finally, a few organisations commented on the CAA's obligation to make a referral to the Competition Commission in airport price review decisions. This was generally thought to be an outdated mechanism. Airlines and BAA thought that it added length and complexity to the process, and significantly increased the cost to industry.

274. The Transport Committee's inquiry into the Future of BAA, published in March 2008, suggested that I might consider this issue.<sup>11</sup> I believe that it is an appropriate exception to my decision to keep off the territory of the other reviews because it concerns the position of one of the bodies conducting one of the reviews. The procedure in other regulated industries does not involve an automatic referral to the

<sup>10</sup> UK Economic Regulators – House of Lords Committee on Regulators, 1<sup>st</sup> report of Session 06-07 – November 2007

<sup>11</sup> The Future of BAA – Transport Committee – March 2008

Competition Commission. It is common for the Competition Commission to have a formal appellate role when the original decision has been made. The only option for aggrieved parties in the case of aviation is Judicial Review, which is inadequate as a sole remedy not least because it may not address the substantive merits of the original decision. There is a strong case for a proper appellate stage in this process. The Competition Commission is far and away the best placed body to provide that. To do so it must no longer have a role in the process leading to the original determination. This should have the incidental benefit of shortening the process, which will be welcomed by everyone. **I recommend that the Department propose amending the existing legislation to remove the automatic statutory reference to the Competition Commission in the setting of airport price caps and establish this organisation as the appellate body.**

## 10 STAKEHOLDER ENGAGEMENT

275. The CAA has a wide range of stakeholders. This includes the UK aviation industry, general aviation, consumers (especially air passengers), the general public and representative bodies, such as environmental organisations.

276. Stakeholder engagement is a key part of the CAA's work. A regulator cannot set policy, rules and standards for the people it regulates in a vacuum and the CAA spends a good deal of time and resource interacting with its stakeholders. Engagement would seem to fall into three main categories: engaging stakeholders to understand their needs and the environment in which they operate; consulting stakeholders for their views on regulatory proposals; and building relationships and influencing, particularly in Europe. Of course, it is entirely possible that a particular form of engagement may cover two or three of these categories. The review has already covered the CAA's influence in Europe in Chapter 7 on the CAA's international work. This chapter reports on the way that the CAA consults and on its wider engagement to understand and be understood by its stakeholders.

277. The CAA's groups consult on their annual business plans and their costs and charges to different degrees and using different mechanisms. Some witnesses said that they would like to hear more from the CAA about the general direction of travel and the upcoming big issues, in addition to the CAA's plans for new initiatives and resources. **I recommend that the CAA should consult its stakeholders periodically on its overall objectives and plans.**

278. Concerning consultation on costs, the review received evidence which commended the process put in place by the CAA's Safety Regulation Group (SRG). SRG has an industry-led Finance Advisory Committee that challenges SRG's financial arrangements. Witnesses spoke of the high degree of transparency over the nature of the costs and how they were apportioned. Some stakeholders thought that the CAA's Economic Regulation Group (ERG) could do more to emulate SRG, although it was acknowledged that ERG's costs were significantly lower than those of SRG. **I recommend that the CAA should review its various costs and charges consultation processes to identify best practice across the organisation and to implement it in a way that is consistent with the size and complexity of the charges involved.**

279. The review notes that the CAA spends considerable time on consultation, in order to discharge its statutory functions and in recognition of the principles of better regulation. As with any public body, the pressure to consult, and to do so early, is increasing. In Chapter 6 on the environment, the review observes that in future more time may need to be built in to consultation processes on environmental issues, to ensure that stakeholders have a full opportunity to understand the impacts of what is at stake and the chance to respond meaningfully.

280. As mentioned in the introduction, over the last six months the review has held a number of one-to-one oral evidence sessions and a series of group dialogues involving the CAA's stakeholders. It was clear at times that not all stakeholders were well informed about the role of the CAA. This tended to have a bearing on their opinions of the CAA's effectiveness. To choose three examples that we have attempted to elucidate in this report: there appeared to be confusion in some quarters over the CAA's role in respect of promoting UK aviation;<sup>12</sup> over the CAA's handover

<sup>12</sup> see Chapter 3 – Role and Status

of functions to the European Aviation Safety Agency;<sup>13</sup> and over how decisions on airport price reviews are taken.<sup>14</sup> The review recognises that some stakeholders may have appeared to know less than they did as part of an agenda not directly related to this review, but this was certainly not true of everyone. **I recommend that the CAA seek to identify where there are gaps in stakeholders' knowledge about the CAA's role and activities. It should focus its communications resources to address these.** But the process is clearly not one-way. There may be scope, for instance, for trade bodies to ensure that their members are well informed about the CAA's work.

281. The review also received a small amount of evidence about the CAA's knowledge of the aviation community. In Chapter 9 on economic regulation, the report refers to some criticisms of ERG on this front. Generally speaking, it was clear that the majority of stakeholders had a great deal of respect for the CAA's expertise in the aviation field and, where appropriate, on wider issues. For instance, several stakeholders praised the CAA's Consumer Protection Group for its financial awareness. The limited amount of evidence on this subject would seem to indicate that there were no significant gaps and that the CAA's staff were well equipped to carry out its functions. This matches the review's general impressions from having met a range of senior and junior CAA staff.

282. Some evidence presented to the review said that the CAA was at times reluctant to enforce breaches of safety legislation. It is not our place to go into the examples in depth and without doing so it is not easy to be sure whether the CAA has got this right. We note that in the four years to March 2008, the CAA prosecuted 119 cases of breaches against aviation legislation. It said that it was willing to prosecute where it had evidence to support its case. The CAA's policy on prosecuting rightly takes account of the fact that a collaborative approach, where individuals or organisations are free to share information and concerns with the regulator, is more beneficial to safety for the vast majority of people who want to comply with the law.

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<sup>13</sup> see Chapter 7 – International

<sup>14</sup> see Chapter 9 - Economic Regulation

## 11 FINANCING AND COST-EFFECTIVENESS

283. Sections 8 to 15 of the 1982 Act set out the CAA's financial provisions. Section 8 imposes a general duty on the CAA to secure enough revenue to meet its costs, taking one year with another. Section 15 requires that the CAA's accounts be audited annually and that a copy be laid in each House of Parliament. External auditors are appointed by the Secretary of State after a public competition. Under section 10, the Secretary of State also approves the CAA's borrowing, its overdraft limit and sets its required rate of return on capital. Section 10 provisions are approved by the Secretary of State for Transport in consultation with the Treasury.

284. Of particular importance to this chapter is section 11, which sets out the CAA's principal charging mechanisms. Section 11 allows the CAA, having consulted the Secretary of State, to create charging schemes to recover the cost of performing most of its statutory functions. It does not permit the CAA to create charging schemes in respect of its air navigation function. The CAA instead recovers the cost of carrying out this work through the Eurocontrol route charges system. Section 11 means that most of the CAA's income (about £68 million) comes from the aviation community that it regulates. Some funding comes from the CAA's consultancy arm, CAA International, which is discussed further in Chapter 7 on the CAA's international work.

285. Under section 16 of the Act, the Secretary of State may require the CAA to provide advice or assistance in relation to the Secretary of State's own civil aviation functions (but outside the CAA's regulatory remit). The CAA is entitled to recover from the Secretary of State the cost of responding to such requests.

286. Work currently funded by Government includes the assistance that the CAA gives DfT in carrying out safety checks on foreign aircraft, legal enforcement work carried out by the CAA and the Department for Transport's recent request for advice on passenger experience.

287. It is not always clear whether a piece of work should be paid for by DfT or by the aviation community. The review offers guidance on this in the next section, which deals with payment for activities carried out at the request of DfT.

288. No witnesses argued that the taxpayer should fund all of the CAA's activities. But a number of stakeholders were concerned that the current arrangements resulted in the UK aviation community bearing more cost than other countries, where Governments fund most of the costs of aviation regulators. Funding is an important issue and it is right for the review to examine the main arguments for the CAA's statutory functions being funded by the aviation community.

289. The majority of UK regulatory bodies, including the Financial Services Authority, the Office of Communications (Ofcom) and the Office of Rail Regulation, charge a significant proportion of their costs to those that they regulate. In relation to aviation, the United States' Federal Aviation Administration is Government-funded. Similarly, aviation regulation in some European countries, such as France and Spain, is partially funded by the taxpayer. But the trend in the aviation world is increasingly towards the aviation community funding the regulator's activities. Notably, EASA was established on this footing.

290. Obtaining its income from the aviation community makes the CAA vulnerable to a reduction in the level of aviation activity. Nonetheless, it ensures that the regulator

is insulated from the effects of Government budgetary restrictions, and from the risk that if UK aviation grows, Government would not provide additional resources for regulation. The drive for the CAA to improve efficiency comes from its Board, Government and the aviation community, which provides a robust challenge to the CAA's charging schemes.

291. One could argue that financial dependence on the aviation community is not healthy for a regulator that must challenge that very community and enforce legislation and standards. But the CAA's statutory powers to set charges are central to its independence from both the aviation community and from Government. And at a time when strong arguments are being made for ticket prices to reflect the full costs of aviation, it would seem particularly inopportune for the regulatory costs of the aviation community to be subsidised by the taxpayer.

**292. I recommend that the CAA should continue to recover the cost of discharging its regulatory functions from the aviation community.**

#### **PAYMENT FOR ACTIVITIES DONE AT THE REQUEST OF DFT**

293. This section of the report deals with who should pay for activities done at the request of DfT. Evidence was presented querying the basis for the aviation community paying for the influencing and negotiating work that the CAA carries out mostly in Europe, but also in domestic forums. They argued that the Government should pay for all the CAA's representational work, as this work was contributing to the development of aviation policy.

294. The CAA's representational work in Europe includes going to European Union working groups, or lobbying the European Commission over its developing aviation policy. In these instances, the CAA could at one point in time be pursuing its regulatory role for aviation, but at the same time or shortly afterwards, be discharging a function in the national interest, i.e. on behalf of the Government. I am mindful that many members of the aviation community have pressed the point during this review that the CAA could be more effective in influencing Europe. Where the CAA is both pursuing its regulatory role and representing the national interest in Europe, it would be laborious to work out the precise split of costs between the CAA and the taxpayer. **Most of the representational work that the CAA carries out, mainly in Europe, is associated with its regulatory functions. I recommend that the costs related to this work should be covered by the CAA's usual charging mechanisms.**

295. It is usual for Government Departments to draft legislation, but there are areas of aviation such as safety where the CAA's technical expertise makes it better placed than DfT to write statutory instruments. As drafting legislation is not part of the CAA's statutory functions, it was agreed a couple of years ago that DfT should provide funding for this activity. This has not yet been implemented. **I recommend that the Department should at the earliest opportunity pay the CAA for drafting aviation statutory instruments.**

296. To help prevent any future doubt about who should fund what, the review has developed a general principle. If the CAA intends to carry out a piece of work in relation to its regulatory activities, it should recover the cost from the aviation community. This would apply to any unsolicited advice that the CAA provides to the Secretary of State. If the CAA would not otherwise do the work because it did not consider it to be in pursuit of its regulatory functions, and the only reason it was doing so was because of the Secretary of State's or DfT officials' request, DfT should pay.

297. Many organisations presenting evidence to the review wanted more transparency. **I recommend that the CAA and DfT should increase the transparency of what the Government pays for. When new arrangements are in place, they should test them with the aviation community that pays for the CAA's regulatory activities to see whether they are content.** By doing so, they are likely to reduce many of the concerns felt by the aviation community expressed during the course of the review.

298. DfT currently requests advice and assistance from the CAA under section 16 of the 1982 Act on a case by case basis. DfT and the CAA agree a charge for each piece of work, which the CAA invoices when the work is complete. **To assist both DfT and the CAA with their planning and budgeting processes, I recommend that they review the requirement for CAA advice and assistance for each forthcoming year and agree an overall outline budget to cover the work.**

### THE CAA'S REQUIRED RATE OF RETURN

299. The CAA's current financial target, set by the Government for 1998/9 onwards, is for it to achieve the higher of

- an annual 6% rate of return – defined as profit before interest and tax as a percentage of average capital employed<sup>15</sup> or
- break-even after charging interest and tax – i.e. a zero net profit.

The target applies to the CAA's regulatory and air navigation functions.

300. In evidence to the review, some witnesses said that it was inappropriate for the CAA to earn a profit from those it regulates. The financial projections published in the CAA's current corporate plan show that the CAA expects to make an operating profit of £2.0 million or less in each of the next 5 years for its regulated activities. To put this figure into context, it compares with total CAA charges of £75-85 million.

301. The net CAA position, after charging interest, tax and the EASA transition cost,<sup>16</sup> is a loss of approximately £0.5 million in each year of the plan. This means that although the CAA is achieving the 6% rate of return on regulated activities it is actually making a loss overall.

302. I am clear that the CAA should be required to recover through its charges the full costs of carrying out its functions. **I recommend that the Government should continue to require the CAA to make a return on the assets it employs to carry out its functions.**

303. One organisation stated that the 6% rate of return was significantly higher than that required of other regulators. The required capital charge on assets for Ofgem, Ofcom, the Competition Commission and the Office of Fair Trading is 3.5%. On the face of it, this appears to be less demanding than the CAA's 6%. But the basis of the CAA's and other regulators' rate of return targets are different and a proper comparison cannot be made. Notably, there are some important differences in funding and liability for corporation tax. Ofcom, Ofgem and the Competition Commission receive significant grants in aid from Government and so they are not totally dependent on charges to finance their activities. In contrast to the CAA, other

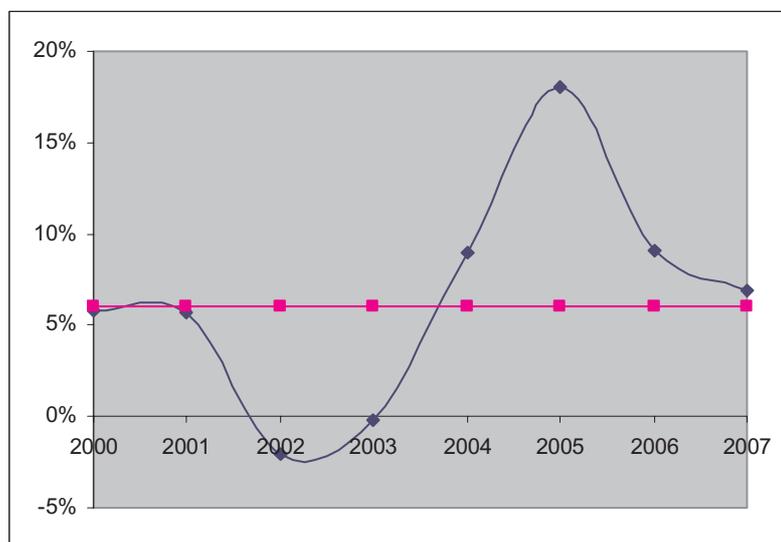
<sup>15</sup> Both profit and capital employed are calculated on a current cost accounting basis

<sup>16</sup> This is the extra cost to the CAA related to the transition of functions to EASA, which DfT has agreed should not be charged to the aviation community.

UK regulatory bodies either do not pay corporation tax (OfT, Ofgem) or only pay it on investment income or property surplus.

304. It was stated in evidence that the CAA had exceeded its allowed rate of return in recent years. The review has established that the main cause of this over-recovery was related to a sudden downturn in the CAA's income that occurred in the aftermath of the terrorist attack in the United States in 2001. The CAA was unable to achieve its rate of return and after consultation with the aviation community, requested dispensation from the Treasury from this requirement. The Treasury granted this request on the basis that the shortfall was made up in subsequent years. The graph below clearly shows periods of major under- and over-recoveries that this caused.

### The CAA's rate of return on its regulatory functions



305. The review notes that, such major impacts aside, it is difficult to fix charges for the various schemes for the coming year so as to produce a return of exactly 6% due to inevitable fluctuations of income and operating costs. The average rate of return for the regulated activities over the period 2000 to 2007 amounted to 6.5%. The 0.5% over-recovery is in the order of £0.2 million per annum on a regulated income of over £70 million.

306. The CAA said that once the EASA transition activities are complete (expected to be in about four years' time) the rate of return could be reduced by perhaps 1%. This would probably still allow the CAA as a whole to break even after interest and tax. The resulting reduction in charges to the aviation community would amount to about £0.4 million per year. But the reduction would increase the risk that the CAA would not actually break even. This suggests that there is limited scope for a change to the rate of return within the target as it is presently defined.

307. In its response to the Transport Committee in 2007 the Government committed to review the CAA's 6% target rate of return. **I invite the Government to discharge its commitment to review the CAA's financial target. At the same time it should consider the rationale for the differences in the treatment of corporation tax and VAT between the CAA and other regulators.** I do not expect the outcome materially to reduce charges to the aviation community.

## PENSIONS

308. The CAA offers its staff a defined benefit pension scheme which provides a pension payable at 60 years of age of up to 2/3 of final pensionable salary at an accrual rate of 1/59ths. The scheme also provides death in service cover of four times salary and a spouse's pension at a rate of 2/3 of the members' pension. The CAA pension is index-linked to the Retail Price Index. Part of the pension may be commuted as a lump sum

309. Given the scale and rate of change in pensions provision in recent years it is not surprising that we received evidence about the CAA pension scheme from companies whose payments fund the CAA, including its pension costs.

310. There is some resentment in industry that they are funding a better pension scheme for the CAA's staff than they feel that they can afford for their own staff.

311. The CAA's pension scheme is valued by its members. We believe that its quality is also taken into account by potential recruits and helps the CAA to recruit and retain staff of the right quality, although its salaries arguably do not match those paid by private sector companies who need staff with the same skill sets as those sought by the CAA.

312. The assets of the CAA's own pension scheme are currently valued at about 112% of liabilities. This healthy position came about largely because the CAA decided to move its assets from equities to bonds just before the dotcom bust. This was done to reflect the separation of NATS from the CAA and the altered risk profile of the pension scheme. The result is that the CAA is able to contribute 6% to employees' pensions – a relatively low figure for a defined benefit scheme. This is matched by a similar contribution from scheme members. An objective and professional assessment, carried out by the scheme's actuary on behalf of the trustees, is that the present arrangements are sustainable without increased payments for at least the next 20 years.

313. A recent survey conducted by the Association of Consulting Actuaries shows that expected employer costs (as a proportion of earnings) in the long term average over 7% for defined contribution schemes and 17% for defined benefit schemes. Thus, although the benefits from the CAA scheme may be better than those provided by the aviation industry in general, the scheme is an important part of the total remuneration package and the costs are well below those expected for defined benefit schemes.

314. Changing to a defined contribution scheme would probably require the CAA to put in much more than 6% on behalf of employees. The CAA would also need to make up for the reduced value of their scheme by offering significantly higher salaries. Moving away from the present arrangements is therefore likely to cost charge-payers more.

315. In short, I believe that the evidence I received criticising the CAA's pension arrangements is based on a series of misunderstandings. It has made sense for many organisations to close a defined benefit pensions scheme to new members and there may be others whose circumstances make the change inevitable in years to come. In the case of the CAA's scheme, there are good reasons for keeping the status quo

- the costs are below average
- an average alternative scheme would cost more and

- the scheme helps the CAA to recruit good quality staff at salary levels below those prevailing in the sector generally.

**316. I recommend that the CAA's current pension scheme should be retained.**

### **COST-EFFECTIVENESS**

317. The review received few comments on the CAA's cost-effectiveness. With a view to reducing costs, a number of stakeholders suggested that the CAA could outsource more of its activities, such as its provision of maps and charts or the administration of its ATOL scheme. The CAA provided the review with many examples of services it had already outsourced, or intended to outsource. In the case of maps and charts, while sufficient expertise must remain within the organisation to allow it to oversee the activity, the CAA intends to pass over the majority of the work to a third party, leading to a possible saving of nine full time equivalent staff. It has outsourced internal audit, payroll, taxation and the provision of facility services, amongst other functions. In line with many other organisations it plans to bring key aspects of IT back in house. Chapter 8 on passengers discusses the possibility of outsourcing the administration of the ATOL scheme.

318. Other stakeholders suggested that regulatory activities could be devolved to third parties or even deregulated. For example, it was proposed that the safety of foreign aircraft (SAFA) inspections the CAA currently conducts for Government could be conducted under a commercial contract to the Government. Some from the general aviation community wanted the CAA to devolve more of its oversight of safety regulation to general aviation associations. The review heard that DfT and the CAA had investigated outsourcing SAFA inspections, but that it had been more cost-effective to continue with the current arrangements. The CAA explained that it had deregulated the airworthiness of microlights. It had devolved or had plans to devolve a number of activities such as national private pilots' licences, permits to fly, aeromedical examiners and instrument flight procedure design. The CAA said that the activities it had outsourced, devolved or deregulated to date had saved about 150 full time equivalent staff.

319. The CAA also indicated that it had a range of processes in place to improve its cost-effectiveness. Chapter 4 on corporate governance sets out in more detail the arrangements for internal audit and value for money. The CAA has initiated two specific projects to improve value for money – e-business and implementing a SAP system for finance and HR. It gave two examples of benchmarking. First, a joint CAA and aviation community review on safety regulation costs and charges included a benchmarking exercise against other European regulators. This showed that the CAA compared well on a number of fronts, including its proactive approach to safety regulation, customer services and productive use of its inspectors and support staff. Second, the review included an independent benchmarking of the support services, which showed that the CAA had performed well. The CAA said that it constantly reviewed its regulatory approach and procedures with the aviation community, citing the reform of ATOL bonding as an example.

320. The CAA seems to have made good progress to date in respect of cost-effectiveness. It appears to have the mindset, backed up by a range of initiatives, to continue these improvements.

## RECOMMENDATIONS

As explained earlier, the starting-point for my report is that the CAA is a world-class regulator. It follows that the recommendations set out below are not concerned with rescuing a failing organisation. They are intended to help a good organisation to become even better.

### ROLE AND STATUS

- 1) It is clear to me that the CAA has to date managed safety and economic regulation without conflict. There are significant advantages to having both functions in the same organisation. I recommend that the two functions remain with the CAA. (Paragraph 42)
- 2) I believe that giving the CAA a general role to promote aviation would be incompatible with its duties as a regulator. The CAA is responsible for safeguarding the general public interest, which is broader than the aviation community. I recommend that the Department for Transport propose an amendment to the Civil Aviation Act 1982 to remove the current ambiguity. (Paragraph 46)
- 3) I recommend that the Department for Transport work with the CAA to develop and propose amendments to address the specific issues identified in the report to bring the legislative framework up to date. (Paragraph 56)
- 4) I recommend that the CAA's current status as a public corporation be retained. (Paragraph 64)
- 5) I recommend that the CAA's sponsorship statement should reflect the need for systematic discussion between the CAA and DfT on strategic objectives, policy changes and the legal framework. (Paragraph 78)
- 6) I recommend that the principles the review has developed governing the boundary between DfT and the CAA be incorporated into the CAA Sponsorship Statement. (Paragraph 86)
- 7) I recommend that the CAA sponsorship statement be revised at the earliest opportunity to reflect current requirements, to emphasise the need for constructive relationships and to explain that there will be instances where complete openness is simply not possible. (Paragraph 93)

### CORPORATE GOVERNANCE

- 8) Having considered the advantages and disadvantages, I recommend that the Secretary of State appoints a full-time Chief Executive to the CAA. I recommend that, once a Chief Executive is in place, the responsibilities and time commitment of the Chairman should be reduced. (Paragraph 112)
- 9) I recommend that key decisions should be made by the Board as a whole. This is not to say that important preparatory work, for example on airport price

review decisions, should not be undertaken by a smaller group consisting of or including members of the Board. (Paragraph 118)

- 10) I recommend that the CAA work in a way that ensures that, whilst the non-executives are adequately briefed, they are not overly involved in working level formulation of policies and decisions in regulatory panels and policy committees. (Paragraph 125)
- 11) I recommend that the Secretary of State keep the current arrangements whereby the Assistant Chief of the Air Staff from the Ministry of Defence is appointed as a non-executive director of the CAA. (Paragraph 130)
- 12) The statutory requirement for the Treasury to approve the CAA members' remuneration and pensions is an anomaly. I recommend that the Department for Transport seek to amend the legislation so that the responsibility lies solely with the Secretary of State. (Paragraph 136)
- 13) In light of the CAA's existing audit arrangements and the opportunity to build on them in the way I have described, I see no need for the National Audit Office to be involved directly with the CAA. I recommend that the current arrangements be retained. (Paragraph 141)

#### **APPEALS**

- 14) I recommend that the current appeals procedures involving the non-executives are left in place. The CAA should review other regulatory tribunals to incorporate any relevant best practice into its own procedures. (Paragraph 160)
- 15) I recommend that the CAA and the Government consider changing the route of appeal for fitness of character decisions so that they are made by the general regulatory tribunal instead of the County Court. (Paragraph 161)

#### **ENVIRONMENT**

- 16) I recommend that the CAA should have a general statutory duty in relation to the environment. (Paragraph 177)
- 17) The CAA should not be given a general duty in statute without a clear policy framework from Government. The Secretary of State should be responsible for providing a framework which offers guidance to the CAA on how to strike the balance on the inevitably difficult issues where there is a trade off to be made between the environment and other considerations. The framework should make clear the boundary between the roles of the CAA, the Government and other stakeholders. It must give enough of a steer to allow the CAA to make a decision that is aligned with Government policy. But at the same time the framework must not be overly prescriptive. (Paragraph 178)
- 18) I recommend that the Department for Transport propose the repeal of section 5 of the 1982 Act. (Paragraph 182)

- 19) The Secretary of State's guidance on environmental objectives in relation to the CAA's air navigation functions is now nearly six years old. I recommend that it be reviewed to ensure that it continues to be up to date. (Paragraph 183)

## **INTERNATIONAL**

- 20) I recommend that DfT should stay in the overall lead on European engagement, in particular liaising with the European Commission over emerging policy and on high-level negotiations. DfT should be resourced to fulfil this, with CAA support as necessary. But there will be a range of activities in the middle ground where either DfT or the CAA could take the lead. In areas that are technical and without wider policy implications, DfT may see fit to cede full responsibility to the CAA. Whichever of them is in the lead, it is imperative that the CAA and DfT continue to work in partnership, using the rules of engagement that I go on to propose. (Paragraph 202)
- 21) There is a useful contribution already made by two or three members of staff whose expertise is in the fields of policy and international negotiation. I recommend that the CAA consider increasing this number to about half a dozen and maintaining it at around that level. (Paragraph 209)

## **PASSENGERS**

- 22) I recommend that the CAA examine the case for a merger of its Economic Regulation and Consumer Protection Groups in 2013 and bring it about if the savings are no longer outweighed by the risks. (Paragraph 230)
- 23) I recommend that the CAA keep Consumer Protection Group's ATOL work under consideration to identify potential efficiency savings from further outsourcing within the next three to five years and that the Department ask the CAA for progress reports in September 2011 and September 2013. (Paragraph 238)
- 24) I recommend that the CAA should continue to carry out its oversight of the financial fitness of air carriers along current lines. (Paragraph 245)
- 25) I recommend that the CAA should continue its work on developing consumer policy. (Paragraph 247)
- 26) I recommend that the Department for Transport propose legislation to put the status and functions of the AUC as a specific aviation consumer body on a firm statutory basis. (Paragraph 252)
- 27) I recommend that in developing legislation for the AUC, more weight should be given to its existing role as consumer advocate. It would make sense for the AUC to retain its present responsibility for handling complaints. The Secretary of State should be responsible for approving the CAA's appointment of the AUC's Chairman and Council members. The Chief Executive would be nominated by the Council and approved by the CAA. To avoid any perception that the organisations are too close, the AUC should work from its own premises. (Paragraph 253)

- 28) I recommend that the AUC's funding arrangements remain the same and that the CAA should continue to set the level of funding in response to business plans from the AUC. The new legislation should give the AUC the right to appeal to the Secretary of State if it wishes to challenge the CAA's view of the proper level of funds. The AUC should produce accounts. (Paragraph 255)

#### **ECONOMIC REGULATION**

- 29) I recommend that the DfT review of the economic regulation of airports should consider whether the CAA's current duty towards users should be amended to give greater weight to passengers or consumers. (Paragraph 272)
- 30) I recommend that the Department propose amending the existing legislation to remove the automatic statutory reference to the Competition Commission in the setting of airport price caps and establish this organisation as the appellate body. (Paragraph 274)

#### **STAKEHOLDER ENGAGEMENT**

- 31) I recommend that the CAA should consult its stakeholders periodically on its overall objectives and plans. (Paragraph 277)
- 32) I recommend that the CAA should review its various costs and charges consultation processes to identify best practice across the organisation and to implement it in a way that is consistent with the size and complexity of the charges involved. (Paragraph 278)
- 33) I recommend that the CAA seek to identify where there are gaps in stakeholders' knowledge about the CAA's role and activities. It should focus its communications resources to address these. (Paragraph 280)

#### **FINANCING AND COST-EFFECTIVENESS**

- 34) I recommend that the CAA should continue to recover the cost of discharging its regulatory functions from the aviation community. (Paragraph 292)
- 35) Most of the representational work that the CAA carries out, mainly in Europe, is associated with its regulatory functions. I recommend that the costs related to this work should be covered by the CAA's usual charging mechanisms. (Paragraph 294)
- 36) I recommend that the Department should at the earliest opportunity pay the CAA for drafting aviation statutory instruments. (Paragraph 295)
- 37) I recommend that the CAA and DfT should increase the transparency of what the Government pays for. When new arrangements are in place, they should test them with the aviation community that pays for the CAA's regulatory activities to see whether they are content. (Paragraph 297)
- 38) To assist both DfT and the CAA with their planning and budgeting processes, I recommend that they review the requirement for CAA advice and assistance

for each forthcoming year and agree an overall outline budget to cover the work. (Paragraph 298)

- 39) I recommend that the Government should continue to require the CAA to make a return on the assets it employs to carry out its functions. (Paragraph 302)
- 40) I invite the Government to discharge its commitment to review the CAA's financial target. At the same time it should consider the rationale for the differences in the treatment of corporation tax and VAT between the CAA and other regulators. (Paragraph 307)
- 41) I recommend that the CAA's current pension scheme should be retained. (Paragraph 316)

## ANNEX A – SIGNIFICANT EVENTS IN THE CAA’S HISTORY

1969	The Edwards Report on the British Civil Aviation industry recommends that all aspects of civil aviation regulation be brought into a civil aviation authority, established as a statutory corporation
1971	The Civil Aviation Authority is established by the Civil Aviation Act 1971.
1972	On April 1, the CAA comes into existence. Price controls preventing charter flights from charging less than scheduled fares are abolished.
1973	The Air Travel Organisers’ Licensing (ATOL) scheme is introduced, solving the problem of ‘bucket shops’ that offered passengers no financial protection.
1975	The CAA certifies Concorde to enter commercial service after 12 years of development and testing.
1976	A comprehensive Mandatory Occurrence Reporting System is introduced, covering incidents and defects.
1979	The UK adopts the first European Joint Airworthiness Requirement, covering standards for large transport aircraft.
1982	The CAA becomes fully self-financing. A new Civil Aviation Act (1982) comes into force.
1983	The Government seeks the CAA’s advice on the implications of British Airways’ privatisation on UK airline competition.
1984	The CAA’s review of airline policy generates the ‘most heated debate in history of British civil aviation’.
1985	Fire destroys a British Airtours Boeing 737 aircraft at Manchester airport. A range of new requirements to improve cabin safety are introduced.
1986	In preparation for BAA privatisation, the Airports Act 1986 makes the CAA responsible for regulating user charges at Heathrow, Gatwick and Stansted airports as well as at Manchester. Highland and Islands Airports was formed.
1987	British Airways and BAA are privatised.
1988	The CAA begins a consultation on ways of accommodating air traffic increases in the south east up to 2005.
1990	The Monopolies and Mergers Commission Report on the CAA is published, focusing on the supply of navigation and air traffic control services.

<b>1993</b>	The European Third Package of Liberalisation came into force. The CAA makes recommendations for maximising the benefits of European airline competition.
<b>1994</b>	The CAA launches Safety Awards for General Aviation. Government proposes the privatisation of National Air Traffic Services.
<b>1995</b>	Highland and Islands Airports Ltd was transferred to the Secretary of State for Scotland.
<b>1996</b>	National Air Traffic Services Ltd was formed, still under the CAA's direction. CAA Strategic Business Group was sold to the private sector.
<b>1997</b>	A review of general aviation fatal accidents leads to wide-ranging measures to enhance the safety of light aviation in the UK.
<b>1998</b>	ICAO Assembly adopts mandatory universal safety oversight audit programme.
<b>2001</b>	National Air Traffic Services Ltd is part-privatised. The CAA is restructured to become the UK's specialist aviation regulator. Attacks on 11 September result in temporary airspace restrictions in the USA and the UK.
<b>2002</b>	A new national private pilots' licence is introduced for leisure pilots.
<b>2003</b>	The European Aviation Safety Agency is established. The Government publishes its white paper on the Future of Air Transport. The CAA's Aviation health unit is set up. Air Safety Support International is established to ensure compliance with ICAO's safety standards in the UK Overseas Territories. Concorde is retired from service.
<b>2004</b>	Together with the aviation community, the CAA sets up a joint review of charges for safety regulation.
<b>2005</b>	The CAA publishes its first review of UK regional air services.
<b>2006</b>	The Office of Fair Trading publishes a market study into UK airports. The CAA publishes two reviews of the General Aviation sector. The Transport Committee publishes a report on the work of the CAA.
<b>2007</b>	An EU-US Aviation Agreement liberalising trans-Atlantic flights is signed. UK regulation of air fares is ended. The Competition Commission follows up the OfT study, focusing specifically on BAA's London airports.
<b>2008</b>	Manchester airport is de-designated by the Secretary of State. The ATOL scheme is reformed.

## **ANNEX B – LIST OF WITNESSES**

### **ORAL EVIDENCE**

*\* indicates that written evidence was also submitted*

**Air Accident Investigation Branch** – David King, David Miller

**Air Transport Users Council** \* – Tina Tietjen, Simon Evans

**Aviation Environment Federation** \* – Tim Johnson

**BAA** \* – Stephen Nelson, Kyran Hanks

**bmi** \* – Nigel Turner, Robert Palmer, Captain Ian Mattimoe

**British Air Transport Association** \* – Danny Bernstein, Roger Wiltshire

**British Airways** \* – Willie Walsh, Maria da Cunha, Paul Ellis, Isobel Knox

**British Business and General Aviation Association** \* – Guy Lachlan, Marwan Khalek, Iain Young, Robert Wilson

**Competition Commission** – Christopher Clarke, John Banfield

**Campaign for the Protection of Rural England** \* – Lawrence Wragg, Michael Nidd

**Conservative Party** – Julian Brazier MP TD, Andrew Williams

**Eurocontrol** – David McMillan

**European Aviation Safety Agency** – Patrick Goudou, Dr Daniel Holtgen

**European Commission** – Daniel Calleja

**easyJet** \* – Andy Harrison, Captain Dave Prior, Andrew Barker

**The Honourable Gwyneth Dunwoody MP** (Chair of the House of Commons Transport Committee, 1997-2008)

**Health and Safety Executive** – Geoffrey Podger, Christine Barringer

**International Air Transport Association** \* – Laurie O’Toole, Gerry O’Connell

**London First** \* – Baroness Jo Valentine, John Dickie, Rob Fox

**Manchester Airports Group** \* – Geoff Muirhead, Dr Jonathan Bailey

**National Audit Office** \* – Ed Humpherson, Chris Shapcott

**NATS** \* – Paul Barron, Ian Hall, John Connolly, Andrew Picton

**Ofcom** – Lord Currie, Peter Phillips, Dominic Morris, Michael Richardson

**Office of Fair Trading** – Nick Allen, David Ruck

**Office of Rail Regulation** – Chris Bolt

**PPL/IR Europe** \* – Paul Draper

**Prospect** – Garry Graham

**Rolls Royce** \* – Colin Smith, Vic Szewczyk, Alan Eccleston

**Sir Malcolm Field** (Chairman of the CAA, 1996-2001)

**Society of British Aerospace Companies** – Martyn Graham, Gary Clinton, Alan Eccleston, John Saunders, David Barnes, Ron van Manen, Sarah Macken

**Virgin Atlantic** \* – Barry Humphreys, Nigel Milton, Georgina Kwaszenko

**Civil Aviation Authority****Department for Business Enterprise and Regulatory Reform****Department for Environment Food and Rural Affairs****Department for Transport****HM Treasury****Ministry of Defence****UK Permanent Representation to the European Union**Dialogue Event 1 – Aviation in 2020 and its regulation by the CAA

Brian Lewis	Air Display Association Europe
Ann Reynolds	Airport Operators Association
Kyran Hanks	BAA *
Guy Lachlan	British Business and General Aviation Assn. *
Jim McAuslan	British Airline Pilots' Association *
Roger Wiltshire	British Air Transport Association *
John Clark	Civil Aviation Authority
Chris Gadsden	easyJet *
Charles Henry	General Aviation Awareness Council *
John Levesley	Guild of Air Traffic Controllers
Dr Jonathan Bailey	Manchester Airports Group *
Doug Johnson	Met Office
Paul Draper	PPL/IR Europe *
Frank Pullman	Thomas Cook
Eddie Redfern	TUI Travel *

Dialogue Event 2 – The CAA's responsibilities

Rob Siddall	Airport Operators Association
Tim Johnson	Aviation Environment Federation *
Mike Carrivick	Board of Airline Representatives UK
Guy Lachlan	British Business and General Aviation Assoc. *
Padhraic Kelleher	Civil Aviation Authority
Michael Nidd	Campaign for the Protection of Rural England *
Chris Gadsden	easyJet *
Roger Hopkinson	Light Aircraft Association
Rob Fox	London First *
Glyn Jones	Luton Airport
Ian Parker	NATS *
Andrew Walters	Regional Airports Limited *
David Rowland	Royal Aeronautical Society
Laura Simpson	Strategic Aviation Special Interest Group
Nigel Milton	Virgin Atlantic *

Dialogue Event 3 – The CAA’s responsibilities towards passengers

Rob Siddall	Airport Operators Association
Simon Bunce	Association of British Travel Agents
Noel Josephides	Association of Independent Tour Operators *
Alan Bowen	Association of ATOL Companies
Cptn John Marriott	British Airline Pilots Association *
Mike Carrivick	Board of Airline Representatives UK
Nick Fincham	Civil Aviation Authority
Michael Nidd	CPRE *
Chris Gadsden	easyJet *
Andy Cooper	Federation of Tour Operators *
Eddie Redfern	TUI Travel *
Nigel Milton	Virgin Atlantic *

Dialogue Event 4 – The way the CAA operates

Martin Robinson	Aircraft Owners and Pilots Association UK
David Marshall	Association of British Travel Agents
Roger Wiltshire	British Air Transport Association *
Carolyn Evans	British Airline Pilots Association *
Isobel Knox	British Airways *
Brian Humphries	British Helicopter Advisory Board *
Simon Baker	Civil Aviation Authority
Chris Gadsden	easyJet *
Andy Cooper	Federation of Tour Operators *
Roger Hopkinson	Light Aircraft Association
Elliott Renton	Luton Airport
Mark Asquith	NATS *
Paul Draper	PPL/IR Europe *
Nigel Milton	Virgin Atlantic *

**WRITTEN EVIDENCE**

In addition to those marked with an asterisk above, the following organisations and individuals submitted written evidence to the Review

Association of Licensed Aircraft Engineers	John Dobui
Armageddon Associates	John Milner
Ashmansworth Parish Council	Lee Everett
Brian Oke	Martin Philcox
Brian Robinson	Mike Smith
C Cauwood	Nick Davis
Chris Draper	Nick Scott
CPRE West Midlands	Peter Kynsey
David Cartwright	Rita White
De Havilland Support Limited	Robert Forster
flybe	Ryan Smith
Dr Garry Bonsall	Ryanair
Guild of Airline Pilots and Navigators	Simon Clifton
	SRFAC

Harry Hopkins Historic Aircraft Association Hunter Flying Ian Cran Jim Norman	Stansted Airline Consultative Committee Steve Noujaim Steve Papi Stop Stansted Expansion
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## ANNEX C – TRENDS AND SIGNIFICANT DEVELOPMENTS

- C1. Notwithstanding current uncertainties, long-term growth in UK and global aviation was expected to continue, with the increasing demand for travel in the rapidly growing economies of China and India an important source of demand.
- C2. There was consensus that concerns about the environment, whether in terms of noise, local emissions or climate change will only increase, as will the impact on aviation of measures to address them. But the general view was that neither this, nor increasing demands on a constrained supply of infrastructure, was likely to eliminate growth in UK aviation in the foreseeable future.
- C3. The liberalisation of airline ownership and routes, together with the success of low fare models of operation, has led to strong competition between airlines in Europe and elsewhere. This was expected gradually to be adopted more widely across the world. It was accepted that some areas of aviation could not be as susceptible to competition as airlines, and would remain either as monopolies or with significant market power. This meant that economic regulation of some kind would continue to be appropriate in certain areas (for instance, in respect of some airports and en route air traffic services).
- C4. There would be increasing competition for the use of the available airspace by a wide range of users with differing requirements. Resolving the competing interests of existing airspace users, including military, civil air transport and the many types of user within General Aviation, would become increasingly difficult.
- C5. In recent years, regulation of aviation in the UK and elsewhere in Europe has been increasingly driven by the European Union rather than nationally, albeit within a global framework set by the International Civil Aviation Organisation. Chapter 7 on the CAA's International work provides more background on the EU and ICAO. All the evidence to the Review was that this move to a European lead would continue in all aspects of regulation – safety, airspace, economic and consumer protection.
- C6. Responsibility for the regulation of safety will increasingly be shared with the European Aviation Safety Agency (EASA), established by the EU in 2003. EASA is expected to take over all rulemaking, perhaps within the next five years. But there would be a continuing need for National Aviation Authorities to oversee the implementation of EASA regulations and rules. Rapid growth in Very Light Jets and Unmanned Aerial Vehicles could add to the challenge of improving safety.
- C7. The EU has established programmes to drive major changes in the use of airspace and to develop a new European air traffic management system through the Single European Sky and SESAR programmes. The aims of the programmes are to increase the capacity to move aircraft safely, so as to reduce delays and the impact on the environment, whilst improving cost-effectiveness. The Community has already legislated to require the separation of the provision and the regulation of air traffic services.
- C8. The EU will continue to seek agreements with other regions in order to promote competition on air services and to develop the regulation of European airports and air traffic services.
- C9. In recent years Europe has introduced consumer protection regulation which gives air passengers more rights, notably through legislation on Unfair Commercial

Practices, Persons of Reduced Mobility and Denied Boarding Compensation. The drive from Europe on consumer rights is expected to continue.

C10. It was expected that there will be increasing pressure to reduce the regulatory burden and to increase the transparency of the regulatory decision-making process (whether by Government or regulator). This will be particularly the case on decisions that affect competing interests, whether within aviation, or between aviation and the general public or specific groups.

## ANNEX D – EASA AND THE CAA: DIVISION OF RESPONSIBILITIES

	Airworthiness of aircraft and products		Operation of aircraft	Licensing of flight crew	Air traffic services	Aerodromes
<b>Rulemaking &amp; standardisation</b>						
<b>Approval of aircraft &amp; products</b>	Type certification and continuing airworthiness management (design)	Annex 2 aircraft* & continuing airworthiness (operations & maintenance)	/ / / / / / / /	/ / / / / / / /	/ / / / / / / /	/ / / / / / / /
<b>Approval and continuing oversight of organisations</b>	Design & non-EU production** and continuing airworthiness management	UK production, continuing airworthiness management and training organisations	Aircraft operations	Training organisations	UK air navigation service providers	UK aerodromes
<b>Licensing of individuals</b>	Maintenance engineers		/ / / / / / / /	Professional & private pilots	Air traffic controllers	/ / / / / / / /

	EASA Current
	EASA Future
	CAA
/ / / / / / / /	Not Applicable

\* Annex 2 aircraft – historic, ex-military, amateur built and very light aircraft

\*\* Production organisations – EASA also approves EU production organisations if requested by the member state