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Llywodraeth Cymru
Welsh Government

Ein cyf/Our ref: KS/116/20

The Rt Hon Grant Shapps MP
Secretary of State for Transport

transportsecretary@dft.gov.uk

12 February 2020

Dear Grant,

Supporting Regional Air Connectivity by expanding the scope and funding of non-economic activities at UK airports.

I am writing in relation to the funding that is provided by the UK Government for activities in the public remit such as security and customs at UK airports. The proposals within this letter are intended to address the priority of regional connectivity (which you have clearly recognised with your welcome Flybe intervention) and provide a solution to the disproportional regulatory cost burden faced by regional UK airports. As set out below, the level of funding provided by the UK Government for such activities is low compared to other countries in Europe. This puts smaller UK airports at a significant disadvantage, and as a result, many regional airports in the UK are placed in a financially vulnerable position.

I would like to ask that the UK Government considers expanding the scope and the level of funding for these activities at UK airports such that they are in line with the other countries in Europe, a policy which would complement your recent approach to Flybe. As explained below, this expansion in scope should not be expected to lead to a significant additional burden on public resources as a result.

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Rydym yn croesawu derbyn gohebiaeth yn Gymraeg. Byddwn yn ateb gohebiaeth a dderbynnir yn Gymraeg yn Gymraeg ac ni fydd gohebu yn Gymraeg yn arwain at oedi.

We welcome receiving correspondence in Welsh. Any correspondence received in Welsh will be answered in Welsh and corresponding in Welsh will not lead to a delay in responding.

Scope of non-economic activities in the UK compared to other countries in Europe

Non-economic activities typically include regulatory costs such as security and customs at airports as well as activities to safeguard civil aviation against acts of unlawful interference, e.g. unlawful seizure of aircraft in flight.¹

In the UK, the current scope of non-economic activities is primarily limited to customs. In particular, this implies that all other regulatory costs, such as costs in relation to fire safety, police and environmental protection and sustainability, would need to be recovered by the airports through their commercial operations. This position places UK airports at a disadvantage, as airports in other European countries are compensated by the state for some of these costs. Table 1 below illustrates the difference between the scope of non-economic activities in the UK and other countries in Europe.

As these regulatory costs are usually fixed, i.e. the costs do not vary directly in relation to passenger volumes, airports with the fewest passengers, such as regional airports, bear the highest burden on a per passenger basis. Furthermore, due to the difficulties in the current aviation market in Europe², it is very difficult for regional airports to pass-through these regulatory costs onto the airlines. Similarly, regional airports may not be able to recover these costs from their non-aeronautical revenue streams, such as passengers' spending at airport shops, given the limited annual passenger throughput at these airports. As a result, regional airports are placed in a financially vulnerable position as a result of the UK Government's overly stringent definition of non-economic activities and the corresponding low levels of funding provided by the UK Government for such activities.

¹ As outlined in the European Commission's state aid aviation guidelines, the state, in its role of a public authority, is allowed to fund activities at airports that are considered non-economic, such as police and customs, without triggering state aid rules. European Commission (2014), 'Guidelines on State aid to airports and airlines', 4 April, paras. 34-37.

² IATA (2019), 'The state of the airline', March, available at: <https://www.iata.org/publications/economics/Reports/State-airline-industry-Europe-Apr-19.pdf>, accessed on: 12 November 2019.

Table 1 Classification of non-economic costs across selected countries in Europe compared to the UK

UK	Denmark	France	Germany	Ireland ¹
Customs	Fire safety	Fire safety	Fire safety	Air traffic control
	Air navigation	Security	Protection against acts of unlawful interference	Police
	Police	Protection against animal hazards	Air surveillance	Customs
	Customs	Environmental controls		Firefighting
		Air flight information service		
		Air navigation control equipment		

Note: ¹ These are some examples of non-economic activities that are funded by Ireland through its public policy remit programmes (namely, PPR-O and PPR-C). Therefore, it is possible that the full scope of the definition of non-economic activities in Ireland could be wider compared to the activities listed in the above table.

Sources: European Commission (2017), 'State Aid SA.44377 (2016/NN) – Denmark - Aarhus Airport', 9 August 2017, para. 31; European Commission (2015), 'Aides d'État SA.38936 (2014/N) – France - Régime d'aide à l'exploitation des aéroports français', 8 April, para. 9; European Commission (2018), 'State Aid SA.46945 (2018/NN) – Germany Erfurt-Weimar Airport', 27 June 2018, paras. 60, 61, 62-64 and 65; and Department of Transport, Tourism and Sport (2019), 'Policy Support for Regional Airports: Preparation of new Regional Airports Programme 2020 to 2024', 30 August, p. 9.

Financial impact of the UK government's current limited scope of non-economic activities on regional airports

Expanding the scope of funding for non-economic activities for UK airports would have a significant positive impact on airports in the UK, particularly, regional airports. In the short to medium term, the additional funding would help regional airports to build up financial reserves and place them in a better financial position against future uncertainties such as Brexit. More importantly, regional airports would have the financial resources to invest in traditional non-aeronautical infrastructures such as additional retail facilities at the airport's terminal, or more innovative projects such as the development of business parks.³ These initiatives would help regional airports to

³ For example, Humberside Airport is seeking to develop a business park. For further information, see Humber Local Enterprise Partnership (2016), 'Humber Enterprise Zone: Humberside Airport', 1 November, available at: <https://www.humberlep.org/project/humber-enterprise-zone-humberside-airport/>, accessed on 24 October 2019.

diversify their business model and achieve financial sustainability in the future in addition to creating jobs for the regions.

To illustrate, take the example of Cardiff Airport, the key commercial airport in Wales. In the financial year 2020, the airport expects a passenger throughput of 1.62 million. Over the same period, the airport expects to incur operating costs of £20.3m.⁴ In light of the UK Government's current limited definition of non-economic activities, the full amount of these costs need to be recovered from the airport's commercial activities. However, if, for example, the UK Government had funded those activities defined by the French Government as non-economic activities, Cardiff Airport's operating costs could have been reduced to £16.8m, representing a 17.3% in operating cost savings for the airport.⁵

Furthermore, it is likely that airports' regulatory costs will increase significantly over the next few years. In particular, as the UK Government has committed to cutting greenhouse gas emissions to almost zero by 2050,⁶ airports' environmental and sustainability related costs may increase materially.⁷

Therefore, the UK Government should consider expanding its scope and the level of funding for non-economic activities in order to minimise the increasing disadvantage to UK airports compared to airports in other countries in Europe.

Potential negative impacts of maintaining the status quo

Airports of all sizes play an important role in the UK economy. In a recent consultation on the future of UK aviation in 2050, the UK Government acknowledged that the aviation industry has helped the UK to foster international trade links and create vital domestic connections.⁸ It is estimated that the industry contributes at least £22 billion to the UK economy and is responsible for supporting 230,000 jobs each year.⁹ Going forward, the UK Government believes that the aviation industry has the potential to meet the needs of consumers and of a global, outward-looking Britain, by encouraging competitive markets and developing innovation, technology and skills to 2050 and beyond.¹⁰ Regional airports are expected to be key in delivering the Government's aviation strategy and vision.

⁴ Cardiff Airport.

⁵ The costs expected to be incurred by Cardiff Airport in 2020 in relation to environmental control, air navigation and police services amount to £3.5m.

⁶ BBC News (2019), 'Climate change: UK government to commit to 2050 target', 12 June.

⁷ Aviation is considered to be the largest carbon emitting sector in the UK by 2050.

Therefore, the Committee on Climate Change has recommended a variety of policy measures for the UK's aviation sector, including measures to manage growth in demand. For further information, see Committee on Climate Change (2019), 'Net-zero and the approach to international aviation and shipping emissions', 24 September, pp. 1, 5 and 13.

⁸ HM Government (2018), 'Aviation 2050 The future of UK aviation: A consultation', December, p. 6.

⁹ HM Government (2018), 'Aviation 2050 The future of UK aviation: A consultation', December, pp. 6 and 21.

¹⁰ HM Government (2018), 'Aviation 2050 The future of UK aviation: A consultation', December, p. 8.

In fact, the UK Government acknowledged that regional airports are hubs for growth within and beyond the regions in which they are situated.¹¹ For example, core and specialist aviation services, freight companies, logistics hubs and aerospace investments are often located close to airports. As a result, regional airports help to develop many non-aviation businesses in the regions.¹² Regional airports act as gateways to international opportunities for the regions of the UK and help to rebalance the UK economy by supporting regional growth.¹³ The UK Government has explicitly mentioned in its Aviation 2050 consultation that it wishes to maximise the benefits generated by regional airports.¹⁴ Additionally, the role of regional airports is only likely to become more important to the UK's future prosperity as the UK leaves the European Union and the UK Government has a duty to ensure that its regulatory framework is fit-for-purpose.

However, due to increases in regulatory costs and the low level of public funding available for non-economic activities, many regional airports face difficulties in achieving and maintaining commercial viability. The Airports Commission found that there are many financial pressures facing smaller airports.¹⁵ The relatively high regulatory costs, such as the costs of maintaining a minimum level of rescue and fire-fighting services and ensuring the security of the aerodrome perimeter, are considered to be one of the main drivers of the financial difficulties facing smaller airports.¹⁶ According to the Airports Commission, this could be one of the reasons why there were a number of airport closures in quick succession in the early to mid-2010s.¹⁷ Indeed, Bristol Airport has highlighted in its recommendations to the UK Government that the Government should act decisively to reduce the regulatory burden and costs for airports.¹⁸ As highlighted by Bristol Airport, additional regulatory costs would have a negative impact on airports' efficiency.¹⁹ The Welsh Government has also raised similar points in our response to the recent Aviation 2050 consultation that the fixed cost burden faced by regional airports in the UK is disproportionate and limits regional airports' potential to deliver socio-economic benefits.

¹¹ HM Government (2018), 'Aviation 2050 The future of UK aviation: A consultation', December, p. 86.

¹² HM Government (2018), 'Aviation 2050 The future of UK aviation: A consultation', December, p. 86.

¹³ HM Government (2018), 'Aviation 2050 The future of UK aviation: A consultation', December, p. 86.

¹⁴ HM Government (2018), 'Aviation 2050 The future of UK aviation: A consultation', December, p. 14.

¹⁵ Airports Commission (2014), 'Discussion Paper 06: Utilisation of the UK's Existing Airport Capacity', June, pp. 22 and 25.

¹⁶ Airports Commission (2014), 'Discussion Paper 06: Utilisation of the UK's Existing Airport Capacity', June, pp. 22 and 25.

¹⁷ Examples of airport closures include: Filton Airport (2012) and Plymouth City Airport (2011).

¹⁸ Bristol Airport (2013), 'Bristol Airport's recommendations for a balanced aviation policy', 15 February, p. 10.

¹⁹ Bristol Airport (2013), 'Bristol Airport's recommendations for a balanced aviation policy', 15 February, p. 10.

Going forward, Brexit and other macroeconomic fluctuations²⁰ are expected to have a significant negative impact on smaller airports in the UK, in particular. Unless the UK Government changes its position on the scope and the level of funding for non-economic activities, there is likely to be another wave of regional airport closures, which could lead to economic disruptions. The UK Government has already acted decisively to rescue Flybe to prevent this from happening to some extent. At a time when it is committed to levelling up the UK economy, could the UK Government afford to risk any further reduction in regional prosperity given the severe regional imbalances that already exist?

Conclusions and recommendations

Under the UK Government's current definition of non-economic activities, all airports in the UK bear a disproportionately large amount of regulatory costs compared to airports in other European countries. While the larger airports may be able to pass on the costs to the airlines operating from their airports or recover these costs through non-aeronautical activities, smaller airports are limited in the scope of changes to their revenue streams that could be implemented. As a result of the increasing regulatory costs, the prospect of many regional airports achieving commercial viability is under threat.

I should be clear – in making this case the Welsh Government is not arguing for any lowering of the vital regulatory standards that help make our airports some of the safest and most secure in the world, but simply to put the UK into the European mainstream in terms of government support. In order to avoid regional economic disruptions as a result of airport closures, and to align with your policy commitment to support and grow regional air connectivity within the new aviation strategy, I ask that the UK Government expands the scope and the level of funding for non-economic activities in the UK. This increase in scope would not artificially sustain unprofitable or inefficient airports as the cost of non-economic activities, including potential additions to the scope, would remain relatively small compared to the total costs of operating an airport.

I would welcome the opportunity to discuss this matter further with you.

I have copied this letter to Simon Hart MP, Secretary of State for Wales, and to Russell George AM, Chair of the National Assembly for Wales' Economy, Infrastructure and Skills committee, who I know has a particular interest in the success of Cardiff Airport.

Yours sincerely,



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Minister for Economy, Transport and North Wales

²⁰ Some regional airports in the UK depend on the volatile oil and gas market. For example, in 2018, Humberside Airport recorded a net loss due to lower offshore activity for oil and gas. Humberside International Airport Limited (2018), 'Directors' report and financial statements', 31 March, p. 4.