

LOCAL BUS SERVICES MARKET INVESTIGATION

Notice of possible remedies under Rule 11 of the *Competition Commission Rules of Procedure*

Introduction

1. On 7 January 2010, the Office of Fair Trading (OFT) referred the supply of local bus services in the UK (excluding Northern Ireland and London) to the Competition Commission (CC) for investigation. The reference was made under section 131 of the Enterprise Act 2002 (the Act).
2. In its provisional findings, a summary of which was published on 6 May 2011, the CC has provisionally found that features of relevant markets in the supply of local bus services in the UK (excluding Northern Ireland and London¹), prevent, restrict or distort competition. Hence, there is a provisional finding of an adverse effect on competition (AEC) within the meaning of section 134(2) of the Act. The provisional findings report identified those features that give rise to the AEC and the resulting detrimental effects on customers.
3. Where the CC finds that there is an AEC, it has a duty, under section 134(4) of the Act, to decide whether it should take action and/or whether it should recommend others take action to remedy, mitigate or prevent the AEC and any resulting detrimental effects. The CC must also decide what action should be taken and what is to be remedied, mitigated or prevented. In deciding these questions, the CC has a duty to achieve as comprehensive a solution as is reasonable and practicable to the AEC and any resulting detrimental effects, as set out in section 134(6) of the Act.
4. This Notice of Possible Remedies (the 'Notice') sets out and invites comments on possible actions which the CC might take, or which the CC might recommend be taken by others, in order to remedy, mitigate or prevent the AEC or any resulting detrimental effect on customers. Prior to deciding what, if any, action should be taken and by whom, the CC will take into account all comments received on this Notice and consult further. The parties to this investigation and any other interested persons are requested to provide any views in writing, including any additional or alternative remedies they wish the CC to consider, by 27 May 2011.
5. The CC is seeking to encourage the widest possible response to the Notice. The CC recognizes that for some parties it will be appropriate to address all the issues that are raised in the Notice, whilst for others only certain issues will be relevant. The CC also recognizes that there might be other important issues that parties may wish to bring to the CC's attention in addition to the issues set out in the Notice.

Provisional findings on AEC and resulting detrimental effects

6. The CC has provisionally identified two different aspects of bus markets where competition is being prevented, restricted or distorted (see Section 14 of the provisional findings).

¹Defined by section 137 of the Transport Act 1985 as the administrative area of Greater London as for the time being constituted.

7. Our first provisional finding is that competition to supply local bus services in a relevant market (whether defined as a flow or as a wider local area) is prevented, restricted or distorted where a combination of the three features identified below are present in that relevant market (see paragraphs 14.5 to 14.12 of the provisional findings):
 - (a) the relevant market exhibits high levels of concentration;
 - (b) one or more aspects of the relevant market act as a barrier to entry and expansion; and
 - (c) in relation to consumer conduct there are two aspects: first, some customers commit to a particular operator by purchasing a multi-journey ticket, and second, customers place a high value on time saved and certainty, relative to other factors such as price or quality. This means that for customers who are not already committed to an operator, there is a general preference to catch the first available bus when at the bus stop and to minimize waiting time.
8. Our second provisional finding is that competition for the tendering of supported local bus services in certain relevant markets is prevented, restricted or distorted by the way Local Transport Authorities (LTAs) design tenders and/or the limited number of potential bidders in local areas because one or both of these features can limit the number of operators bidding for the tender contract (see paragraph 14.13 of the provisional findings).
9. We have received at a late stage ahead of the publication of the provisional findings some further evidence which is relevant to the assessment of the theory of harm on coordinated effects. We shall continue to consider the possibility of coordinated effects after the provisional findings. We will consult separately at a later stage, including in relation to any implications for possible remedies, if we provisionally find that operators are coordinating their behaviour in local bus markets and that this coordination is preventing, restricting or distorting competition.
10. Detrimental effects arise where consumers have little or no choice of bus operator and the competitive pressure arising from operators that might begin offering directly competing services is limited. In these circumstances, incumbent bus operators are able to reduce the quality of service they offer to customers (being shorter hours of operation and / or less frequent services, or otherwise lower quality or reliability of services), or increase fares above the level that would otherwise apply. Higher fares may also increase the costs of concessionary fare reimbursement. We also provisionally found reduced choice and innovation, higher costs and/or reduced quality of service in relation to reduced competition for the tendering of supported services.

Criteria for consideration of remedies

11. When deciding whether any remedial action should be taken and, if so, what that action should be, the CC will consider how comprehensively possible remedy options—whether individually or as a package—address the AEC and/or its resulting detrimental effects, and whether they are reasonable and practicable. The CC will assess the extent to which different remedy options are likely to be effective in achieving their aims, including whether they can be made to work in practice—ie whether they are practicable. The CC will be guided by the principle of proportionality in ensuring that it acts reasonably in making decisions about remedies. The CC will therefore assess the extent to which different remedy options are proportionate, in particular whether a remedy option:

- (a) is effective in achieving its legitimate aim;
 - (b) is no more onerous than needed to achieve its aim;
 - (c) is the least onerous if there is a choice between several effective measures; and
 - (d) does not produce disadvantages which are disproportionate to the aim.
12. The CC may also have regard to the effects of any remedial action on any relevant customer benefits within the meaning of section 134(8) of the Act arising from a feature or features of the market giving rise to the AEC. Such benefits must comprise one or more of: lower prices, higher quality or greater choice of goods or services or greater innovation in relation to such goods or services.

Possible remedies on which views are sought

13. We are considering remedy options in relation to both local bus services and for the tendering of contracts to operate supported bus services.
14. In relation to local bus services, we are considering the following types of remedy:
- (a) Market-opening measures aimed at addressing the AEC by removing barriers to entry or expansion or other obstacles to effective competition wherever they arise. Specifically, we are considering measures in relation to ticketing, operator behaviour and access to bus stations. Details of these measures and the questions on which we are seeking views are set out in paragraphs 18 to 48.
 - (b) LTA-led interventions aimed at addressing the AEC or resulting detrimental effects in relation to local bus services. This would involve, for example, LTAs using their existing powers or suitably enhanced powers to introduce franchising in part or all of their local areas, or alternatively directly addressing detrimental outcomes for customers or facilitating competition through the use of partnerships with operators. We are considering whether, and in what circumstances, to recommend to LTAs that they should introduce franchising, or other suitable arrangements. Details of these measures and the issues on which we are seeking views are set out in paragraphs 49 to 65.
15. In relation to the tendering of supported bus services, details of the measures to address the AEC and the issues on which we are seeking views are set out in paragraphs 66 to 72.
16. We have considered alternative remedy options, which we are not currently minded to pursue, including divestiture of local operations, and these are set out in paragraphs 73 to 80.
17. The CC will consider submissions on these options and any other practicable alternatives proposed by the parties to the investigation or other interested parties, which they consider would effectively and proportionately address the AEC or resulting detrimental effects identified in the provisional findings.

Market-opening measures to facilitate entry or expansion

18. We have provisionally found that entry into and expansion in local bus markets is restricted by a number of barriers. The following remedy options are aimed at

reducing barriers to entry and expansion and obstacles to sustained competition and thereby increasing competitive constraints particularly on large incumbent operators.²

Ticketing

19. We have provisionally found that a large incumbent operator in an area, or on a route, can gain competitive advantages from its network strength and service frequency, and from its related ability to offer more attractive multi-journey tickets, including season tickets, than new entrants or smaller operators. This form of incumbency advantage can exist both in relation to individual routes and to networks of routes dependent on the travel patterns of passengers and other local characteristics. This form of incumbency advantage is likely to be of particular importance if no effective multi-operator ticketing scheme³ exists in the relevant market. Where such a scheme does not exist or is not effective—for example, if it is not actively promoted to customers or offers multi-operator tickets only on terms that make them unattractive to customers—the incumbency advantages enjoyed by large incumbent operators are greater and barriers to entry and/or expansion higher than if effective multi-operator ticketing schemes were available.
20. In this remedy option we consider measures to reduce the source of this incumbency advantage enjoyed by large incumbent operators over a new entrant or expanding operator in ways that seek to preserve and/or enhance any benefits that customers currently derive from the ability to purchase multi-journey tickets. There are a number of possible measures that could be introduced under this option which may be used either individually or in combination. These relate to:
 - (a) measures to increase the number of multi-operator ticketing schemes in existence (paragraphs 21 to 23);
 - (b) measures to increase the effectiveness of new and existing multi-operator ticketing schemes (paragraphs 24 to 28); and
 - (c) any additional measures necessary to prevent large incumbent operators from undermining the effectiveness of multi-operator ticketing schemes (paragraphs 29 and 30).

Increasing the number of multi-operator ticketing schemes

21. We are considering measures to increase the number of multi-operator ticketing schemes, or similar ticketing arrangements, in existence and thereby increase the availability to customers of multi-operator tickets (or other tickets that are interoperable between local bus operators). The existence of an effective multi-operator ticketing scheme in an area would encourage customers to use the services of new entrants, such that if they wish to make a return journey or a number of journeys over a period, they have the ability to purchase a ticket that they can use on any operator's services (ie a ticket that is interoperable between local bus operators) and thereby have increased flexibility. Through participating in such schemes, smaller

²For the purposes of this Notice, we use the term 'large incumbent operator' to refer to the leading operator or operators in a particular local bus market. This may or may not be one of the five Large Operators.

³We use the term 'multi-operator ticketing scheme' in the widest sense to include those types of arrangements which are possible now or could be conceived in future. In our broad scope such a scheme constitutes a written or binding agreement which allows interoperability in at least one ticket type (eg single, return, multiple trip or season ticket) and where such ticket covers a journey (or journeys) on one or more routes. Interoperability means the ability for a passenger to buy a ticket from one operator, or from a third party, that can be used to travel on a service run by another operator. Similarly, we use the term 'multi-operator ticket' broadly to include any ticketing product that could be provided under a multi-operator ticketing scheme.

operators would be able to meet the demand of those customers who value the ability to purchase network tickets. We also consider separately below some issues relating to the structure and operation of multi-operator ticketing schemes to ensure their effectiveness (see paragraphs 24 to 28).

22. There are potentially three ways in which the number of multi-operator ticketing schemes could be increased:
- (a) the CC could recommend that LTAs make statutory schemes which they could require operators to join; or
 - (b) where no statutory scheme currently exists or is proposed, operators could be required by the CC to enter into new schemes, which may therefore be operator-led rather than LTA-led; or
 - (c) operators could be required by the CC to facilitate the creation of a multi-operator ticketing scheme by any party, whether in the public or the private sector. Such requirements could include: providing such a party with information about the price of its own single tickets; marketing and selling multi-operator tickets on its own buses; accepting the tickets offered by the party on its own buses and not seeking reimbursement from the party above a given rate (eg at no more than the cost of its cheapest single fare); and assisting in the development of any common standards needed to make the scheme operational.
- *Issues for comment 1*

23. **The CC invites comments on these options, and in particular:**

- (a) **The appropriate geographic scope of this remedy option. Should we seek to introduce multi-operator ticketing schemes in all local markets, or should this remedy be focused on particular types of area (eg urban versus rural areas), on areas with particularly high levels of concentration or on particular parts of the reference area.**
- (b) **The costs and benefits of introducing a new multi-operator ticketing scheme to an area, including evidence from existing schemes and evidence of any negative impacts on competition of introducing new schemes.**
- (c) **The most appropriate structure for multi-operator ticketing schemes: eg statutory schemes run by the LTA, operator-run schemes or schemes run by a third party with cooperation from bus operators.**
- (d) **The extent to which it is necessary for operators to work together with each other and other stakeholders to develop common standards (including in relation to technology) to enable multi-operator ticketing schemes to work effectively and the appropriate structure in which such joint work should take place.**
- (e) **Whether an element of compulsion is necessary to ensure the development of new schemes and whether all operators in a particular area should be compelled to join multi-operator ticketing schemes or only the largest incumbent operator (or operators) in that area.**
- (f) **The barriers to establishing multi-operator ticketing schemes—including whether there are any issues arising from either the Ticketing Block**

Exemption or the relevant transport legislation—and if and how these can be overcome.

(g) How any remedy to increase the number of multi-operator ticketing schemes should fit with policy developments in this area. Relevant policy developments may include the Department for Transport’s Smart and Integrated Ticketing Strategy and similar strategies of the Scottish Government and Welsh Assembly Government.

Increasing the effectiveness of multi-operator ticketing schemes

24. In addition to widening the use of multi-operator ticketing schemes, we are considering measures to increase the effectiveness of multi-operator ticketing schemes, including the attractiveness of multi-operator tickets and their uptake by bus passengers.
25. We have provisionally found that multi-operator ticketing schemes, as currently operated, are generally insufficient to enable new or expanding firms to overcome barriers to entry and expansion associated with large incumbent operators’ network strength. We have provisionally found that the uptake of multi-operator tickets appears in general to be low. Tickets are often priced at a significant margin above operator-specific tickets. This appears to be largely as a result of the incentives on operators to introduce a price premium between multi-operator and operator-specific tickets, due to the increased number of services available on a multi-operator ticket. This premium might be achieved in part through the voting mechanisms that determine multi-operator ticket prices and the nature of the multi-operator products available, but we also note that individual operators are able unilaterally to introduce a premium by discounting their own season ticket. In addition, the zones over which multi-operator tickets are applicable can be broad, with the result that they may be less likely to be perceived as a close substitute for single-operator tickets covering narrower zones or individual routes.
26. The effectiveness of multi-operator schemes may also be restricted by a scheme’s governance arrangements. A particular concern is that, where a large incumbent operator (or a group of large incumbent operators in the area covered by the scheme) has influence over the operation of the scheme (eg if it has the ability to veto or otherwise exert influence over pricing or other proposals), it may have the ability and the incentive to take actions that reduce the competitive constraint posed by the scheme to its own local operations. Such actions may involve, for example, restricting the development of multi-operator tickets that would be close substitutes for its own tickets (eg by seeking to increase the price of the scheme’s tickets to ensure sufficient ‘headroom’ above their own prices, or by preventing the development of new ticket types under the scheme), or by restricting access to the scheme by smaller operators (eg by making it prohibitively expensive for smaller operators to join a scheme or by establishing principles of revenue allocation that favour larger operators).
27. We are therefore considering the following potential measures to change the nature of multi-operator ticketing schemes, including those currently in existence:
 - (a) Governance arrangements. We are considering whether to require voting and decision-making arrangements which limit the ability of large incumbent operators to exercise control over the scheme in relation to key decisions, for example those that relate to the pricing of tickets and the types of ticket offered under the scheme. Such arrangements may involve the distribution of votes between operators—for example, imposing a cap on the voting rights of the largest

operator or operators in a scheme—or giving parties other than bus operators (eg the LTA or passenger representatives) a greater say in scheme decisions.

- (b) Access to schemes. We are also considering what measures, if any, are required to ensure fair and open access to multi-operator ticketing schemes for all operators, including smaller participants and/or new entrants. Such measures may involve specifying the criteria for participation in a scheme, the allocation of costs relating to the funding of a scheme, the standards required for tickets to be interoperable and the means of reimbursement for journeys made within a scheme.
- (c) Principles for pricing, structure and/or promotion of multi-operator tickets. We are considering conditions to make multi-operator tickets no less attractive than single-operator tickets in terms of the areas (eg routes or zones) and time periods over which they are available; the inclusion of a maximum price premium over comparable single operator tickets (with an adjustment mechanism for cost increases); and the inclusion of principles relating to the promotion and availability of multi-operator tickets by scheme members or other parties such as LTAs.

- *Issues for comment 2*

28. **The CC invites comments on these options, and in particular:**

- (a) **What requirements, if any, are necessary for the governance of multi-operator ticketing schemes to ensure that they are effective and develop attractive and well-used products (for example, how might a cap on voting arrangements be set).**
- (b) **What would be the costs of changes to the governance arrangements of multi-operator ticketing schemes.**
- (c) **What requirements in relation to access are necessary to ensure that the objective of increasing competition is not defeated by restrictions on access to schemes, the cost of participating in schemes or the allocation of revenues between operators.**
- (d) **What principles should govern the price and specification of individual products offered within any scheme.**
- (e) **What would be the impact of imposing restrictions on pricing, and other aspects of multi-operator ticketing schemes. For example, are there any possible distortionary effects that could arise from such restrictions and, if so, how might such effects be avoided.**

Additional measures to prevent multi-operator ticketing schemes from being undermined

29. If remedies were implemented to increase the number and effectiveness of multi-operator ticketing schemes, there is a risk that large incumbent operators may seek to undermine the impact and viability of multi-operator ticketing schemes by changing their own multi-journey tickets. We are therefore also considering restrictions on the operation of single-operator multi-journey tickets which would be used in support of the measures above relating to increasing the number and effectiveness of multi-operator ticketing schemes. We are mindful of the potential intrusiveness of such additional measures which might restrict operators' ability to compete on price and

service or increase costs to customers. We would therefore need to be clear that the benefits to competition outweigh these factors before introducing such additional measures. These possible measures for consideration are:

- (a) Restrictions on the pricing of individual multi-journey tickets in relation to comparable multi-operator tickets. For example, the price of individual operator tickets by a large incumbent operator may not be permitted to be discounted by more than a certain percentage to multi-operator tickets.
- (b) Restrictions on the ability to issue particular types of ticket, especially where there is a similar multi-operator ticket in existence. For example, individual operators may be restricted from offering tickets for periods of a week or more where similar products are available for multi-operator tickets.

- *Issues for comment 3*

30. **The CC invites comments on these options, and in particular:**

- (a) **Whether restrictions on individual operator multi-journey tickets are necessary, in order for measures focussed on multi-operator tickets to be effective.**
- (b) **The circumstances under which such restrictions would be necessary. For example, should any restrictions apply only to the large incumbent operator (or operators) in any area and/or in the most highly concentrated local markets?**
- (c) **The extent to which any such restrictions on operators would be effective and in what circumstances these should be used.**
- (d) **The specification of any such restrictions and how these would be applied in practice.**
- (e) **The benefits and costs of any such restrictions to customers and operators, including any potentially distortionary effects associated with restricting single-operator multi-journey tickets.**

Restrictions on operator behaviour

- 31. There are several aspects of operator behaviour which we have provisionally found to be part of the AEC.
- 32. We have provisionally found that bus operators have an incentive to compete in ways which are likely to create overcapacity and to compete in a way that is aimed at promoting a rival's exit. This can be through deploying extra services or through changes to other aspects such as price, and can include a range of behaviours including intense competitive actions and reactions. The potential for such conduct by a large incumbent operator following entry or expansion on a route (or routes) can increase entry costs, risks and uncertainty and thereby act as a barrier to entry or expansion. We have also identified a category of 'cheap exclusion', which can distort competition and in addition act as a barrier to entry or expansion when engaged in by an incumbent operator.
- 33. We are therefore considering whether to introduce remedies to constrain the conduct of operators in ways that reduce barriers to entry and increase the likelihood of head-

to-head competition being sustained more often. This is a challenging area in which to consider remedy options, as there is a delicate balance to strike between restricting behaviour that prevents, restricts or distorts competition and 'chilling' legitimate competitive behaviour including investment that benefits consumers. Nonetheless, we have found that operator behaviour, particularly the anticipation of the intensity of post-entry competition which depends on the response by large incumbent operators in response to entry, contributes to the AEC that we have provisionally found. We are therefore considering whether to introduce constraints on the following aspects of behaviour:

- (a) large incumbent operators increasing service frequency in response to new entry;
- (b) large incumbent operators making substantial reductions in fares in response to new entry, especially those reductions that are specific to the routes on which entry has been experienced rather than network wide;
- (c) stand-blocking and other forms of 'cheap exclusion'; and
- (d) actions taken by an operator that undermine the viability of a municipal or independent operator during a sales process.

Increases in service frequency in response to entry

- 34. We are considering whether to recommend changes to the powers and duties of Traffic Commissioners that would enable them to intervene in situations where a large incumbent operator increases service frequency on a route, following new entry, and/or alters the timing of service to reduce headways ahead of the new entrant. In such situations, a Traffic Commissioner could be entitled, for example, to refuse to accept such changes to registrations, to restrict changes to frequent services or to refuse to accept subsequent changes (eg to reduce frequency on the route) following the exit or retrenchment of the new entrant.
- 35. These options would clearly entail a change in the focus of Traffic Commissioners' role, but could constitute an incremental addition to Traffic Commissioners' existing responsibilities in relation to registration and their duties to ensure fair competition and would draw on their local knowledge and monitoring capability and their relationships with local operators.

- *Issues for comment 4*

- 36. **The CC invites comments on these options, and in particular:**
 - (a) **The appropriate geographic scope of this remedy option. Should we seek to apply this remedy in all local markets, or should this remedy be focused on particular types of area (eg urban versus rural areas) or particular parts of the reference area, for example the most highly concentrated areas.**
 - (b) **Whether such an extension of the role of Traffic Commissioners would be effective in reducing barriers to entry associated with the expected response by a large incumbent operator.**
 - (c) **Whether Traffic Commissioners are the right bodies to be taking on this role, or whether some other body or bodies would be better placed to do so, and if so which.**

- (d) Whether any further powers and duties should focus primarily on the response of large incumbent operators or whether some constraint on the behaviour of entrants is required, either generally, or in specific circumstances.**
- (e) What would be the resource implications for Traffic Commissioners and the related monitoring agencies (eg VOSA) of taking on these additional powers and duties.**
- (f) What threshold, if any, should be set to determine whether an increase in service frequency following entry is sufficiently material to trigger the possibility of intervention.**
- (g) Whether the scope for intervention should focus on preventing the initial increase in service frequency following entry or any subsequent decrease in frequency in the event of exit or retrenchment by the new entrant.**
- (h) How such a remedy could be specified in relation to increases in frequency of services that are already registered as 'frequent'. For example, registrations for frequent services could be required to specify the number of buses that could be run per hour possibly expressed in a limited range (eg six to eight buses), or Traffic Commissioners could be given powers to intervene if there was evidence of a material increase in frequency on such a service following entry.**
- (i) The extent to which interventions should be 'rule based' (ie registrations would be automatically refused if they met particular criteria) or should allow for judgement based on particular local circumstances and what should be the relevant rules or principles to guide the application of judgement.**
- (j) The costs in terms of resources to operators and Traffic Commissioners associated with these potential changes to the Traffic Commissioners' role.**
- (k) Any potential unintended consequences of such a change and how they might be minimized.**

Substantial reductions in fares in response to entry

- 37. We are considering whether any restrictions are needed in relation to responses to entry that involve reductions by large incumbent operators in fares, rather than increases in frequency. Responses to entry can involve changes to both fares and frequency. If it becomes more difficult for large incumbent operators to respond to entry by increasing frequency or through cheap exclusion (see paragraph 40), as a result of other measures, then this may involve a more intense response in terms of fares.
- 38. The introduction of restrictions in relation to pricing behaviour is an area in which the balance between addressing this element of the AEC and restricting legitimate and beneficial competitive behaviour is especially delicate. We do not propose that Traffic Commissioners have a formal role in assessing or regulating responses to entry that take the form of fare reductions. This would be a very substantial change in their role and, in our judgement, issues relating to allegations of overly aggressive pricing behaviour are properly a matter for the competition authorities, in this instance the OFT. We are instead considering whether any measures could be taken to facilitate the OFT's ability to monitor pricing behaviour where this has the capacity to prevent,

restrict or distort competition. In particular, we are considering whether Traffic Commissioners should be empowered to bring concerns about operators' pricing behaviour to the attention of the OFT or whether large incumbent operators should be required to notify the OFT of substantial reductions in price following entry.

- *Issues for comment 5*

39. **The CC invites comments on these options, and in particular:**

- (a) Whether options that facilitated the OFT's ability to monitor bus operators' pricing behaviour in response to entry would be effective in reducing barriers to entry.**
- (b) What mechanisms for bringing such pricing behaviour to the OFT's attention are likely to be most effective.**
- (c) What would be the implications for Traffic Commissioners if they had an additional role in relation to bringing pricing behaviour to the attention to the OFT.**
- (d) What would be an appropriate threshold to set if large incumbent operators were required to report 'substantial' fare reductions following entry, and what considerations are relevant to setting such a threshold. For example, what percentage fare reduction should trigger such a report and should reporting obligations only apply if a fare reduction is targeted on an individual route or routes, as opposed to being applied across a wider network?**
- (e) Whether the code of conduct suggested in paragraph 40 should preclude a large incumbent operator in a concentrated market from reducing fares on one or more specific routes only (rather than a network-wide reduction) following entry/expansion of a competitor for a given period of time after entry; if so, what that time period might be.**

Cheap exclusion

40. We are considering remedy options in relation to 'cheap exclusion', which includes actions such as obstructing a rival's services, preventing them from using bus stops and stands, intimidating drivers, vandalizing vehicles and removing rival operators' publicity and timetables. Here, the balance between adverse and beneficial effects is much more clear-cut. This type of behaviour distorts the competitive process and we are considering whether additional measures are necessary to prevent such distortions. Some of these actions amount to criminal acts or torts and there may be other areas of recourse than to Traffic Commissioners for those affected. We also recognize that Traffic Commissioners already have some powers to address the worst behaviour and may be well placed to monitor such types of behaviour and the impact on local bus operators. However, Traffic Commissioners can have limited resources and currently rely on parties providing well-evidenced complaints. We are therefore considering the following options:

- (a) requiring operators to sign up to a legally-binding code of conduct precluding cheap exclusion and potentially other types of exclusionary behaviour; and**

- *making a recommendation to government to provide Traffic Commissioners with additional resources to assist them in monitoring and enforcing fair competition. Issues for comment 6*

41. **The CC invites comments on these options, and in particular:**

- (a) **Whether additional resources should be made available to Traffic Commissioners to monitor and enforce existing powers in relation to fair competition and the likely impact of any such increase in resourcing.**
- (b) **The costs and benefits of requiring operators to comply with a code of conduct.**
- (c) **Which operators should be subject to any code of conduct. For example, should the code only apply to large incumbent operators, or should it apply to all operators?**
- (d) **What types of conduct should be precluded by such a code. Should it only apply to what we have called cheap exclusion, or should other forms of behaviour be included?**
- (e) **How compliance with any code of conduct should be monitored and enforced.**
- (f) **What should be the consequences of any breaches of the code of conduct—for example, should breaches of the code of conduct be taken into account in decisions relating to operator licensing.**

Undermining the viability of an independent or municipal operator during a sales process

42. We are considering whether to recommend a change in the powers and duties of Traffic Commissioners to enable them to intervene in relation to large-scale entry against an independent or municipal operator, while it is subject to a sales process (see paragraphs 6.81 to 6.86 of the provisional findings). The purpose of this measure, which we would expect only to apply in limited circumstances, would be to prevent an AEC from being either established or exacerbated in such circumstances. The powers and duties involved would be similar to those set out in paragraphs 34 to 36 and paragraphs 37 to 39 in relation to frequency and pricing respectively.

- *Issues for comment 7*

43. **The CC invites any specific comments on this remedy option, including comments in relation to the issues set out in paragraphs 36 and 39.**

Access to bus stations

44. We have provisionally found that an inability to access bus stations on equal terms results in a barrier to entry or expansion in a local market where particular circumstances apply. The evidence has indicated that where bus operators both own and manage bus stations, or where they manage other privately-owned bus stations, charges for other operators are often higher than the notional internal charge for the operator that manages the bus station. There have also been some examples of restrictions to access. This puts other operators and new entrants at a disadvantage relative to the operator that manages the bus station and also means that they are

dependent on a competitor for access to an important facility. We note that local authorities have obligations to ensure fair access to any bus station that they own, operate or contract out management and we did not find any evidence of any systematic breach in these duties.

45. We are considering whether to introduce similar 'fair access' obligations in relation to privately-owned and managed bus stations to ensure that access to privately-owned and managed bus stations is available on fair reasonable and non-discriminatory (FRND) terms. Such obligations could include:
- (a) a requirement to manage the bus station at arm's length from the operator's local bus operations;
 - (b) a general prohibition on discriminating, directly or indirectly, against any other operator using or seeking to use the bus station;
 - (c) an obligation to publish a 'fair access' policy including details of how capacity within the bus station will be allocated, the costs of operating the bus station and any charges for use of the bus station;
 - (d) an obligation to set charges for bus station use on an FRND basis, for example a requirement that charges for third party use do not exceed the notional internal charge paid by the operator that manages the bus station; and
 - (e) a requirement to establish a mechanism for resolving disputes relating to the 'fair access' policy.
46. We are also considering how such fair access obligations could best be monitored and enforced to maximize their effectiveness and credibility. For example, we are considering whether LTAs would be well placed to monitor such obligations, given that LTAs are subject to similar obligations where they are the owner of the facility. We are also considering whether it would be appropriate for such obligations to be incorporated in operator licences.
47. At this stage, we are minded to pursue fair access obligations of the kind set out in paragraph 45 in preference to alternative approaches. However, should it not be possible to specify sufficiently robust and effective obligations, we may also consider more structural approaches, including:
- (a) a prohibition on the management of privately-owned bus stations by bus operators that use the bus station in question; and/or
 - (b) a prohibition on the ownership of bus stations by bus operators that use the bus station in question.
- *Issues for comment 8*
48. **The CC invites comments on these options, and in particular:**
- (a) **The appropriate scope of this remedy option. For example, should this option apply in relation to all privately-owned bus stations that are owned and/or managed by a bus operator which also uses the station? Alternatively, should it only apply if additional criteria are also met, and if so, what should these other criteria be.**

- (b) **The effectiveness of fair access obligations in addressing this barrier to entry and expansion.**
- (c) **The nature of any fair access obligations.**
- (d) **How such fair access obligations could best be monitored and enforced, for example whether a commitment to offer access on FRND terms should be in the code of conduct discussed in paragraph 40.**
- (e) **The likely costs of compliance with fair access obligations, including the extent to which there might be an effect on operators' incentives to invest in bus stations and the impact of this for operators and passengers.**
- (f) **The cost and other implications of prohibiting bus operators from managing privately-owned bus stations or a requirement on bus operators to dispose of some or all of the those bus stations which they currently own.**

LTA-led interventions—franchising and partnerships

49. We are considering LTA-led interventions as a remedy option. LTAs have local knowledge and a range of existing powers to intervene where necessary to achieve local policy objectives. We are considering whether existing or suitably modified powers could be harnessed to address the AEC or the resulting detrimental effects.

Franchise model

50. We are considering the possible application of a franchise model.
51. This is a different type of remedy from those already considered in relation to local bus services and takes a different approach by replacing 'in the market' competition with competition 'for the market' in relation to the services included within the scope of the franchise. A franchising model would therefore indirectly address an AEC in a market by creating a competitive process for operators for the market to win the franchise that would replace the current market model.
52. Depending on how franchising is specified, it could also increase 'in the market competition', as a market opening measure, in relation to nearby non-franchised markets. This could be the case where a proportion rather than all of the routes in an area are franchised. If the consequent franchise package were of sufficient scale, this could be attractive to operators who wish to expand within the local area. The franchise could allow them critical mass to become an effective potential competitor in routes or networks that have not been franchised should they be successful in winning the franchise.
53. In this remedy option local bus operators would compete against each other to win a franchise to run specified bus services for a period of time. The franchise would be awarded by the relevant LTA. Depending on circumstances, the franchise might cover a route, group of routes or a network in any given area. In some areas such as large urban areas, there might be a number of franchises applying to different routes or route groups within that urban area.
54. The opportunity of winning the franchise would provide an incentive for operators to compete vigorously by offering strong bids in relation to the value of the franchise, the fares to be charged to passengers, and the quality of the services to be offered in terms of frequency, hours and days of operation, and age and type of vehicle.

Bidders would also compete in seeking to improve on any minimum standards set in the contract.

55. Our general preference, in relation to local bus services, is for remedies that provide the basis for effective and sustained competition in the market compared with those that promote competition 'for the market'. Remedies that promote competition 'in the market', if effective, would provide a strong basis for ongoing rivalry and commercial innovation in relation to all aspects of bus operators' offer, including the dynamic benefits associated with new entry.
56. We recognize that franchising is an intrusive remedy that is most likely to be appropriate in specific local cases, where competition is particularly weak and is not delivering benefits to customers. However, it may not be possible to overcome the AEC in some markets without a more fundamental change to the way in which competition operates. In such circumstances, it might be preferable to introduce a new market model than to seek to make competition 'in the market' work more effectively and which may provide a platform for entry in an area.
57. There are a range of possible structures and incentive arrangements that could fall within such a model, and we recognize that the Quality Contract scheme framework provides an option although no such schemes are currently in place. We intend to explore the scope for this remedy option to address the AEC, both in terms of a general framework which can be applied by LTAs, and by reference to the experience in areas where franchising is, or has been, under serious consideration by the relevant LTA.

- *Issues for comment 9*

58. **The CC invites comments on this option, and in particular:**
 - (a) **Whether and in what circumstances it would be appropriate to introduce a franchise model.**
 - (b) **Whether a franchise model is more appropriate in particular types of local area than others. For example, it may be more appropriate to introduce a franchise model in larger urban areas (including PTE areas) as these areas are more likely to involve complex network structures where passengers use multiple routes.**
 - (c) **Whether there are any specific geographical areas that may warrant detailed consideration of this option and why.**
 - (d) **How a franchise model should be established and specified to ensure, in particular, that it generates effective competition 'for the market'.**
 - (e) **Whether the use of franchising could have wider market opening benefits, how these could be best achieved and what would be the impact on incumbents of limited franchising within an area.**
 - (f) **Whether the existing Quality Contract scheme framework provides a suitable basis for a franchising remedy and, if not, what changes are required. In this context, we are particularly interested in comments on:**
 - (i) **what issues might arise in the transition to a franchise model including issues relating to the ownership of infrastructure (eg depots);**

- (ii) **what costs are likely to be involved in establishing a franchise model and what are the ongoing running costs; and**
- (iii) **what are the wider benefits, costs and risks of moving to a franchise model and how should these be evaluated.**

Partnership approach

- 59. We described the operation and types of current partnership arrangements between LTAs and operators in Section 12 of the provisional findings.
- 60. We are considering whether to recommend wider use of partnerships between LTAs and operators as a means of addressing the resulting detrimental effects of the AEC and/or facilitating competition in bus markets.
- 61. The CC's general preference is for remedies that increase competitive pressures in markets and address the AEC and thereby also reduce or remove the resulting detrimental effects. By contrast, partnerships, whether statutory or voluntary, tend to focus on improving market outcomes and are typically used to deliver specific improvements to the outcomes for bus services in a local area and in helping to deliver local transport policy.
- 62. Given their focus on outcomes, we are considering first whether partnerships could be used to address detrimental effects resulting from the AEC, either on their own or in combination with some or all of the market-opening measures set out in paragraphs 18 to 48.
- 63. We note that the use of such partnerships is not generally aimed at improving competition in local markets and that the mandating of higher standards might, in some circumstances, make it more difficult for other smaller operators to enter a market, which is one of the factors to be taken into account in the use of the existing Competition Test (see Appendix 12.1, Annex 1, of the provisional findings).
- 64. However, we are also considering whether such partnerships could play a role in remedying certain aspects of the AEC. For example, we note that the signing of a partnership is one way in which a sustainable competitive outcome has been achieved in markets (see paragraph 6.124 of the provisional findings). We will consider whether there are other ways in which partnerships could be used to remove the barriers to competition that we have identified.

- *Issues for comment 10*

- 65. **The CC invites comments on this option, and in particular:**
 - (a) **The appropriate geographic scope of this remedy option. For example, should we seek to apply this remedy in all local markets?**
 - (b) **The extent to which partnerships could be used to address detriment directly or whether there are any ways in which they might be used to also help facilitate ongoing stable competition.**
 - (c) **In what circumstances the use of the remedy would be appropriate.**
 - (d) **The benefits and costs to customers, operators and others, including any potentially distortionary effects.**

- (e) **Whether any existing changes to current legislation, regulations or guidance would be required to facilitate the use of the remedy.**
- (f) **Whether there are any other potential actions that LTAs can or could take to address the AEC or the resulting detrimental effects. How would these be specified and what would be involved?**

Measures to address AEC in relation to the tendering of supported services

- 66. We have provisionally found that competition for the tendering of supported services is restricted by a lack of bidders for some service contracts.
- 67. We note that there are many aspects to a tendered service which it is not possible to change such as the location of the service and the time that it is run. These may mean that some services are inherently unattractive to most operators and for which there may be no effective remedy.
- 68. We have provisionally found that variations in the design of a tender can influence outcomes by encouraging more bidders and the possible entry of new operators into a local area (see Section 13 of the provisional findings). Relevant factors include the extent to which operators have a choice regarding whether to bear the revenue risk, the quality standards that are included and the extent to which services are bundled or not. However, we noted that the extent of the variation in the price of contracts that result from these factors is relatively modest although in some areas competition is very weak. In addition, many tendering authorities have told us that a conscious policy decision, for example not to take the revenue risk, has been taken which helps to ensure certainty of local funding commitments.
- 69. Moreover, winning a tender is seen by many operators as a way towards entering a local market for bus services. Therefore, we consider that those designing tenders should take every opportunity to encourage bids from operators who are currently not operating in the area affected by the proposed tender, as a means of stimulating competition or potential competition in the market for local bus services.
- 70. We have provisionally found that the nature of the decisions that LTAs need to make in tendering for contracts is covered in guidance available in England but that this guidance may need to be enhanced to take account of the additional analysis that we have undertaken. We note that there is no such equivalent guidance in Scotland or Wales. As a result we are considering:
 - (a) making a recommendation to the DfT that all LTAs in England are encouraged to follow the existing guidance on tendering and that the guidance be updated to take account of the findings; and
 - (b) making separate recommendations to the Scottish Government and Welsh Assembly Government that suitably tailored guidance be developed.
- 71. In addition, it can sometimes be difficult for tendering authorities to collect robust information about the revenue performance of a tendered service—particularly where this has previously been operated commercially without support. This means that an incumbent operator can have an advantage when bidding and/or means that tender prices are higher as little value is given by other bidders to an uncertain revenue stream. We are therefore also considering an information remedy which would provide tendering authorities with the ability to collect information about the revenue performance of tendered services, by placing an obligation on operators to provide this information. We are also considering whether and how such information should

be disseminated to other parties, for example potential bidders. We are considering whether any further dissemination of revenue information would need to be at an aggregated level, in light of the potential commercial sensitivity of detailed performance information. This obligation could extend to services that have been de-registered where the previous operator of the service will be required to provide this information to the tendering authority at the time of deregistering the service.

- *Issues for comment 11*

72. **The CC invites comments on these options, and in particular:**

- (a) **The appropriate geographic scope of this remedy option. Should we seek to apply this remedy throughout the reference area.**
- (b) **The proposal to encourage the application of the existing guidance and to enhance that guidance to take account of our findings and to introduce guidance where this is not in place.**
- (c) **The wider costs and benefits of using alternatives approaches to tendering (eg LTAs bearing the revenue risk on a tender in order to increase the likely number of bidders).**
- (d) **The costs and benefits of requiring operators to provide information about the revenue performance of tendered services to tendering authorities and of distributing this information to third parties, such as other potential bidders.**
- (e) **What restrictions, if any, should be placed on tendering authorities in relation to the further dissemination of information about the revenue performance of tendered services.**

Other possible remedies

- 73. The CC is willing to consider any other practical alternatives to the possible remedies outlined above that the parties to the investigation, or other persons, would like to propose and which they consider would effectively address the AEC or resulting detrimental effects identified in the provisional findings.
- 74. We have considered the following alternative remedy options, which we are not currently minded to pursue.
- 75. First, we have given careful consideration to whether to pursue divestitures of local operations as a remedy option.
- 76. We recognize that divestiture could contribute to remedying the AEC in particular markets for local bus services, by introducing an additional local competitor, or strengthening an existing smaller competitor, and thereby directly reducing concentration at a route and/or area level. This could increase the scope for potential competition to a large incumbent operator's routes within the vicinity of the divested operations and, over time, could also lead to increased head-to-head competition on routes. We also recognize, however, that there are risks to the potential effectiveness of any divestiture remedies in addressing the AEC that we have found, including the risk that the scope for potential competition does not translate into an increased competitive constraint, unless the other barriers to competition that we have identified are also effectively addressed.

77. We are minded to prioritize detailed consideration of the remedies set out in paragraphs 18 to 72 of this Notice which have the potential to improve the framework within which competition takes place. These remedies are potentially national in scope but are capable of being tailored at a local level according to local conditions. In our judgement, this approach is most likely to achieve as comprehensive a solution to the AEC as is reasonable and practicable, given the broad geographic scope of this reference, the widespread nature of the features that we have provisionally identified as giving rise to the AEC and the practicalities associated with evaluating and implementing divestitures in more than a small number of local markets.
78. Second, we have considered whether a direct control on outcomes (eg caps on fares or minimum requirements for frequency of services) determined by the CC and monitored by the OFT would be an effective remedy option in relation to the AEC that we have identified in relation to local bus services. The CC generally prefers remedies that deal with the causes of the AEC, rather than its resulting detrimental effects. In this particular context, we do not consider that direct controls on outcomes of this nature are likely to be practicable, given the very large number of bus routes in the reference area. While we have introduced measures to control outcomes as part of a merger remedy in relation to narrowly defined areas, the monitoring requirements associated with a more broadly-based control would be very substantial and in our view would make such a control impracticable within the current framework for monitoring and enforcing CC remedies. Local measures which may involve an element of control over outcomes, including as Quality Contracts and Quality Partnerships, are more likely to be workable solutions and we are considering these options (see paragraphs 49 to 65).

- *Issues for comment 12*

79. **The CC invites comments on these remedies options that it is not minded to pursue.**
80. **The CC also invites comments on whether there are other remedy options that are not set out in this Notice that would be effective in addressing the AEC and/or resulting detrimental effects.**

Packages of remedies

81. We are considering the measures set out in this Notice both individually and in terms of a potential 'package' of remedies.

- *Issues for comment 13*

82. **The CC invites comments on the extent to which the various measures in this notice are likely to be mutually reinforcing and what combination of measures would constitute a suitably comprehensive response to the AEC.**

Implementation, monitoring and enforcement

83. The CC will consider, in relation to each remedy option, how it may best be implemented and what arrangements should be made for effective monitoring and enforcement of any remedies. Where the CC implements remedies itself by means of making an Order or accepting Undertakings, the OFT will be responsible for monitor-

ing such remedies under the Act.⁴ Where the CC makes recommendations to others, it will be for these other bodies to implement, monitor and enforce the remedies.

84. We are considering whether, in addition to the OFT's general monitoring powers and/or the powers of other authorities to whom recommendations are addressed, bus operators should be made subject to additional reporting requirements to facilitate effective monitoring by the OFT or any other body. Such requirements could include information relating to compliance with specific remedy options or to consumer outcomes. We are considering varying the nature of any such reporting requirements according to the size of the party in question, which is a possibility that the CC will also consider in this investigation.

85. We are considering, in relation to any recommendations it might make in relation to LTAs or other authorities, what process should be in place for LTAs to report the steps taken to implement any recommendations.

- *Issues for comment 14*

86. **The CC invites comments on the nature of any reporting requirements that should be required of operators, whether such requirements should vary according to the size of the party in question and whether LTAs or other authorities should report on the steps taken to implement any CC recommendations.**

Relevant customer benefits

87. The CC may also have regard to the effects of any remedial action on any relevant customer benefits within the meaning of section 134(8) of the Act arising from the feature or features of the market concerned. Such benefits must comprise one or more of: lower prices, higher quality or greater choice of goods or services or greater innovation in relation to such goods or services. To be regarded as relevant customer benefits, the benefits must accrue as a result of the feature or features concerned and should be unlikely to accrue in the absence of the feature or features.

- *Issues for comment 15*

88. **The CC invites views on the nature, scale and likelihood of any relevant customer benefits within the meaning of the Act and on the impact of any possible remedies on any such benefits.**

The next steps

89. A copy of this notice will be posted on the CC website. The parties to this investigation and any other interested persons are requested to provide any views in writing, including any additional or alternative remedies they wish the CC to consider, by 27 May 2011 either by email to buses@cc.gsi.gov.uk or by writing to:

⁴Section 162 of the Act.

David Fowles
Inquiry Manager
Competition Commission
Victoria House
Southampton Row
LONDON
WC1B 4AD

90. If necessary, the CC may publish a supplementary notice requesting views on particular issues on remedies that emerge from consultation (see also Note below).

(signed) JEREMY PEAT
Group Chairman
6 May 2011

Note: This Notice of possible actions to remedy, mitigate or prevent the AEC and any resulting detrimental effects is given having regard to the CC's provisional findings, a summary of which was published on 6 May 2011 and which will be published in full on 10 May 2011. The parties to the investigation or other interested persons have until 1 June 2011 to respond to those provisional findings. In the light of any responses by the parties or by other interested persons, the CC's findings may change and the CC may consider other possible remedies, if appropriate.