

# 5 Views of third parties

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## **Introduction**

5.1. We invited views from the DOT, LTB, bus operators, local authorities, trade unions, consumer groups and other interested organizations. The evidence submitted is summarized in this chapter.

## **Department of Transport**

5.2. The DOT had concerns about the merger which are summarized below. But it also noted aspects which might benefit the overall quality and image of bus services. It was preferable that the assets of British Bus, rather than being divided between the two largest players, FirstBus and Stagecoach, were used to expand a lower ranking group. In contrast with the lack of transparency in the affairs and accounts of British Bus, Cowie appeared to have a stable financial base and might tackle the problems that had affected some British Bus subsidiaries.

5.3. The DOT did not have concerns about the merger at the national level. Before the merger, Cowie operated only in London, east Hertfordshire and west Essex. There was therefore no overlap between the parties in Wales, Scotland, the provincial areas north of the Midlands and the separate Southend and Colchester operations. The DOT saw no objection to the merger on grounds of overlapping services in these areas. The purchase by Cowie of North East Bus following the merger did not alter this, because North East Bus had no overlap with Cowie's operations.

5.4. There was, however, some overlap between the operations of the parties in and immediately outside London.

5.5. Outside London there was overlap in only one area, near Stevenage. That occurred between Cowie's County Bus at Harlow and LDT Limited, trading as The Shires, the British Bus subsidiary based at Luton. But this overlap was minor and the Blazefield Sovereign company partly lay between the two. The merged Cowie operation was contained by Go-Ahead (Oxford/Wycombe) to the west, Stagecoach (United Counties/Cambus) to the north and FirstBus (Essex Buses) to the east, so there was adequate potential for competition.

5.6. As Cowie SLT had no routes outside London, there was no overlap to the south and south-east of Greater London. However, the effect of the reinforcement of the existing British Bus operations by the addition of Cowie SLT was a matter of concern. The domination already enjoyed by the linked British Bus companies operating in south London, Surrey, north Sussex and west Kent appeared to the DOT to be unacceptable when these operations became part of a more substantial financial group with existing operations relatively close by. The DOT felt that, south of London, there was an extensive geographical monopoly stretching westward from Sittingbourne to Guildford. The more extensive such a monopoly, the more difficult it was for a small operator to start to secure county council subsidized routes.

5.7. The question of whether divestment of part of the British Bus operation to the south of London might be desirable should be considered in the light of the probable effect of the merger inside London.

5.8. The DOT was particularly concerned about south London. In other areas of the capital, its first impression was that at least some of the smaller companies were able to cope with the switch to net cost tendering. In the first round of net cost tendering, two fairly small operators, Harris Bus and Limebourne, had successfully won routes from larger ones. Other operators in London which were not formed from former LT subsidiaries, for example Capital Citybus and Metrobus, though probably not invulnerable to take-over, were so far not losing contracts.

5.9. Cowie was one of the three dominant operators in the LTB network area. The merger (by percentage of scheduled mileage on 7 July 1996, but without taking account of subsequent changes) gave Cowie 26.3 per cent in that area.

5.10. The DOT did not regard as sacrosanct the guideline that purchasers should not be permitted to acquire a company if that increased their share of the total London scheduled route mileage to more than 25 per cent. But it was concerned when an operator became particularly dominant in a smaller area of the London market.

5.11. [

*Details omitted. See note on page iv.*

]

5.12. Recent mergers in London had reduced the number of separate groups available to bid independently for LTB contracts. Furthermore, the average number of bidders to LTB per tender had fallen substantially since privatization, notably in the south London area. In view of this, and particularly the competitive situation along the A23 corridor, the merger might well operate against the public interest in the long term.

5.13. The DOT referred to percentages of total mileage operated in the boroughs of Lambeth and Croydon by the major companies. For example, on the basis of allocating routes between the operating areas according to where they principally operated at the time that the subsidiaries of LBL were privatized in 1994/95, shares of total mileage were estimated to be: Cowie 75.6 per cent, British Bus 6.7 per cent (combined 82.3 per cent), Stagecoach 8.1 per cent and Go-Ahead 7.3 per cent. LTB had said that the figures in 1995 and 1996 were likely to be similar. It was probably also true that the concentration of the merged Cowie operations was higher at the southern end, particularly around Croydon and Purley.

5.14. Under the terms of the guidance about the privatization procedures issued by the DOT to LTB in consultation with the OFT, there would be no objection to a particular company acquiring two ex-LBL subsidiaries provided that these were non-contiguous and that the total market share was less than 25 per cent. By the acquisition of British Bus, Cowie breached the latter condition-albeit only marginally-and although there were usually a sufficient number of operators competing for the contracts let by LTB, in south London these were now appreciably below the average number of bids for London as a whole. In view of that and the DOT's unease over the domination of the combined operations through Surrey and west Kent, action should be taken to constrain the effects of the merger.

5.15. To summarize, the DOT's view was that the merger would lead to no significant diminution of competition in the deregulated market north of the River Thames. However, the combined operation would exceed 25 per cent of the regulated market in Greater London, with particular impact in south London along the A23 road and the immediately adjoining area in north Surrey. Some divestment was necessary to maintain an adequate level of competition in the south London area. A number of illustrative options were suggested:

- (a) Cowie to divest its SLT company (with 430 buses) bringing the combined market share down to 19.3 per cent. This appeared to be an extreme solution and a likely option only if Cowie itself volunteered it.
- (b) Cowie to divest the Londonlinks company (with 180 vehicles) which would bring the market share in London down to 23.1 per cent. Although there were quite likely to be bidders for Londonlinks, there were companies which should not be allowed to bid (Stagecoach and Go-Ahead for reason of both size and location).
- (c) Cowie to divest Londonlinks plus selective other operations to make a viable package.

5.16. When we asked the DOT if LTB had a statutory duty to promote competition, it told us that the 1984 Act did not explicitly impose such a duty although it required LT to have regard to efficiency and economy of operations.

5.17. The promotion of fair and sustained competition was one of the objectives set by the Secretary of State for the sale of the LT bus subsidiaries. Although this was devised to ensure good management of the sale process, clearly the rationale was that the success of the regulatory regime in London would depend on the continuation of competition.

5.18. Decisions about procurement of bus services in London were a matter entirely for LT. However, the financial targets set for LTB by the Secretary of State ensured that it sought best value for money from route tendering. Among the criteria used for evaluating tenders, price would be very important but not necessarily decisive. The DOT would expect LT to take some account of the medium/ long-term implications for the general competitive situation in the London market, but it was for LT to weigh up these factors.

## **London Transport Buses**

### ***Introduction***

5.19. This section presents the views of LTB, the division of LT responsible for procuring bus services in London. As explained in Chapters 3 and 4, the London bus market is different from the other markets considered in this inquiry, as it is the only remaining regulated bus market in Great Britain.

### ***LTB's statutory framework and objectives***

5.20. LTB explained that LT had been established by the 1984 Act to be the public body responsible for the provision or procurement of public passenger transport services for Greater London. Under section 6 of the Act, bus services were to be secured through competitive tendering. LT was also responsible for the provision and maintenance of the capital's infrastructure of bus stations, bus stops and bus shelters. Furthermore, LT (through its division LTB) was responsible for revenue inspectors, for marketing the network and for providing passengers with travel information.

5.21. In addition to those operational objectives, LTB had to achieve financial objectives which were set for it by the Secretary of State for Transport, under section 16(5) of the 1984 Act.

5.22. Under section 8 of the 1984 Act LT was responsible for determining the general level and structure of fares to be charged for public passenger transport services provided by LT and, in respect of bus services, the general structures and frequency of services.

5.23. It also had to take into consideration the amount of revenue support which it received from the Government. This had been progressively reduced over the last ten years from £265 million in 1984/85 to £118 million in 1987/88 and to £13 million in 1996/97 (all at 1996/97 prices). Over the same period the level of mileage had gone up slightly faster in London than the 25 per cent increase in the unregulated areas of the UK.

5.24. LTB explained that an exception to its achievements had been that it would be unlikely to meet many of the quality of service indicators that had been recently set for it by the Government. The reason for this had been mainly because London suffered dramatically from traffic congestion. Over the last few years London had suffered from insufficient investment in bus priority lanes, traffic lights which give priority to buses and the prevention of illegal parking.

5.25. LTB was responsible for procuring public bus transport mainly in the same geographical area which had once been administered by the Greater London Council. However, it also had a duty to take people who lived in London across the boundary into the shire counties.

### ***Geographical constraints and the road system in London***

5.26. The river had only a limited number of crossings and effectively divided London in two. The road network was also an important consideration. In south London this was less efficient than that in the north, mainly because the arterial roads and motorways in south London were not as open for traffic flow. Furthermore, north of the Thames there was a comprehensive underground network which complemented the bus services. Such integrated inter-modal travel was essential for the effective use of travelcards. South of the Thames, there was a more limited underground system and the area was more dependent on the surface railway system.

### ***LTB's view of the nature of competition in London***

5.27. LTB explained the nature of competition in the London bus market. Unlike the rest of the UK where there was competition on the roads, in London competition to provide bus services was through tendering for contracts, which ran normally for five years. LTB issued tenders on the basis of individual routes, although it did on suitable occasions accept bids for groups of routes in addition to an offer for the single route.

5.28. Bearing in mind what had happened in the rest of Great Britain, it had always expected that there would be some mergers and take-overs after privatization. However, it had not anticipated the speed with which this had happened. It believed that these take-overs and mergers had been driven primarily by the bus companies seeking market opportunities. However, economies of scale had arisen following subsequent restructuring of the companies.

### ***Guidance at privatization***

5.29. LTB referred to a letter from the OFT, in September 1993, which had set out guidance to LTB, which was made available to prospective purchasers on the objectives and procedure for privatization (paragraph 5.14 also refers). That guidance had reflected four particular areas of concern over the need to preserve competition in the London bus market: first, that no one company should purchase more than two of the LT subsidiaries; secondly, that no one company should purchase geographically contiguous London Transport subsidiaries; thirdly, that no company should purchase an LT subsidiary which had an area of operation contiguous with the company's operations outside London; and fourthly, that no company should buy a London Transport subsidiary if it already provided substantial contract services within that subsidiary's primary operating area. LTB confirmed that the privatization process had observed those concerns.

5.30. LTB did not have a monopoly of bus services in London. Although the majority were procured by LTB, through the tendering regime, there was a small element of less than 2 per cent of bus operations, which it described as commercial services. Predominantly, those routes ran cross-boundary from the shires into London and were of two types. In the first, operators approached LTB with a proposal to provide a commercial service. If it believed such a service would not damage its own network, or would enhance its services, LTB would agree to the proposal and enter into a contract with the service provider consistent with its powers under section 3(2) of the 1984 Act. In consequence, the operator of such a commercial service would receive a proportion of off-bus income.

5.31. The second type of commercial service was called a London local licence. An operator had to seek permission to run the service from the Traffic Commissioner and not from LTB. If permission was granted, the service received no share of the off-bus revenue scheme. If LTB considered that the service enhanced its own network, it would ask the operator to seek authority through an application under section 3(2). Both types of commercial bus services could be run by any operator, including those with LTB contracts.

### ***LTB's concerns arising from the acquisition***

#### ***A perceived duopoly***

5.32. LTB had a number of concerns arising from the acquisition. It was particularly concerned about the effects of the take-over in the south London area of Lambeth and Croydon, resulting in a perceived duopoly between Cowie/British Bus and Go-Ahead, which had recently acquired London General and had already been operating in south London with London Central. After the merger of Cowie and British Bus the combined market share of Cowie and Go-Ahead was over 80 per cent in the south London area of Lambeth and Croydon.

### *The significance of depots*

5.33. LTB took the view that the location of depots was an important element in giving an incumbent operator a significant advantage when submitting bids, particularly when the routes being tendered for passed close to its home garage. It was very concerned about the availability of garages in the Lambeth and Croydon area and the effect it would have on competition. In the core operating area of SLT, the merger had brought together Cowie's garages at Thornton Heath, Croydon, Brixton and Norwood, with British Bus garages in Croydon and Walworth. LTB was concerned that such a control of depots by one operator would have deterred other bidders, particularly if those bidders had had garages well outside the route areas; the amount of 'dead mileage' which might be incurred by new prospective tenderers through congested parts of London would be a deterrent to competitive bidding. On balance, LTB considered it to be easier for an operator to obtain a site for a new garage in the fringe just outside London than within it.

5.34. There were problems in opening new garages in London generally. What had been apparent over the last few years was that very few new sites had been opened. The one exception had been the depot opened by CentreWest in Orpington. However, that was only after difficulties in finding a suitable site and obtaining planning permission, and after operating on a temporary basis from a satellite site. LTB explained that LT, not LTB, owned the property portfolio. In the disposal of depots still owned by LT, LT worked to rules determined in conjunction with the Treasury, by which once an asset had become surplus to operational requirements it would be disposed of at the maximum price. It was not LT's obligation to own garages for the sole purpose of letting them to bus companies and LT's property portfolio was not for the purpose of promoting competition.

### *Decline in the number of bidders*

5.35. LTB expressed a further concern as a result of the Cowie and British Bus merger. Over the last few years, the number of bidders per tender had reduced, largely as a result of acquisitions. The average number of bids per route for Greater London as a whole since privatization was 4.5. However, a downward trend was evident with an average of 6.3 between January and June 1995, reducing to 6 between July and December 1995, 3.9 between January and June 1996 and 2.6 between July and December 1996. In SLT's core operating area three routes had been offered for tender since privatization in January 1995, all of which had been retained by SLT. In each case the number of bids received had been three, four and four respectively.

5.36. In certain circumstances where LTB had expected strong competition this had not happened. This trend was particularly marked in south London, where LTB considered that the number of effective competitors had been reduced to two: Go-Ahead, with London Central and London General; and Cowie, with SLT, Kentish Bus and Londonlinks. It was the combination of the reduction in the number of tenderers and the location of garages operated by the new Cowie Group that led LTB to consider that a duopoly practically existed in the south of London. That new situation was of particular significance to LTB when it took into account the programme of the routes that would be coming up for tender during the period from April 1997 to December 1998, a large number of which were currently operated by British Bus or Cowie. Ownership, or occupancy, of depots gave the incumbent a significant advantage.

5.37. Since privatization, the number of independent operating companies had steadily reduced from 34, which included the former LBL subsidiaries, to 20. Only two small independent operators had successfully entered the London market since January 1995: Harris Bus and Limebourne had both won small routes, by LTB's criteria, on a tendered net cost basis. Other small operators, Crystals and Armchair Travel, although not new to the London market, had also won routes and other new, but small, operators had applied from time to time. No significant interest had been shown by any large external operator.

5.38. LTB acknowledged that Metrobus and one or two smaller operators were active in the market, but it considered that those companies had not been effective competitors to the major operators. Furthermore, it would have expected other major national bus operators, such as FirstBus, to be more active in competing for tenders in London.

5.39. It confirmed that the combined Cowie and British Bus operations currently operated 26 per cent of the total LTB network and Cowie plus Go-Ahead, Stagecoach and CentreWest accounted for approximately 70 per cent. In the south London area of Lambeth and Croydon, Cowie and British Bus had 44 per cent, Go-

Ahead had 38 per cent and Stagecoach, through Selkent, had 15 per cent. This concentration caused LTB's high level of concern about what it described as almost a duopoly position in that part of London. It believed that, without the merger of Cowie and British Bus, there would have been a better degree of competition in the south London market-place.

5.40. Before the merger British Bus had been an effective competitor throughout the whole of London. Particularly in south London, the merger had removed British Bus as a potential competitor, which led to LTB's view that the acquisition was against the public interest.

5.41. LTB had no evidence of collusion between the major independent operators in London. However, the number of tenderers had reduced and only two new independent operators had entered the London market successfully since privatization. This left LTB with the impression that major companies were content not to compete.

5.42. LTB was less concerned about the effects of the merger in the north, the north-east and the east of London, areas of the capital where it considered that effective competition had existed between Cowie's Leaside and County Bus and Stagecoach/East London Group, Capital Citybus, the small operation of Thamesway, Docklands Transit and others. It was satisfied that competition had existed between strong operators running competent, quality services in those parts of London.

### *Other barriers to entry*

5.43. LTB considered that in addition to difficulties in acquiring depots, smaller operators faced other barriers to entering the London market, which were not so readily faced by larger operators. These included: more difficult access to capital funding, particularly for the purchase of new vehicles, the cost of setting up new operations and less purchasing power than that possessed by the large groups (as a result of their economies of scale), possible difficulties in attracting, training and retaining staff and the need to own, or lease, a large number of vehicles to operate routes which had a high PVR.

5.44. LTB observed that some major operators stated that the barriers to entry to the London market were low, as there were certain routes requiring a low PVR for which small operators would be able to tender. However, many major trunk routes in London required substantial PVRs of between 30 and 50 buses, a number which would be beyond the scope of a small operator to bid for. LTB regarded a route with a PVR of ten, or fewer, buses as small and routes with a PVR of 20 to 25 routes as medium-sized.

### *LTB's views on the post-acquisition situation in Surrey and Kent*

5.45. LTB explained that although it had had no direct involvement in bus services in Kent and Surrey, it had indirect concerns over which companies controlled garages to the south of LTB's territory, as such control might have precluded potential competition from companies which operated from those garages.

5.46. When it had begun to privatize the LBL subsidiaries, it identified one of the advantages for those companies and their management teams as the opportunity to enter the market-place in the shire counties. An example had been London United, which had fought for, and won, routes from British Bus in south-west London and in Surrey. However, as the majority of the companies which operated in Surrey and Kent, along the LTB boundary, were part of British Bus, the merger had adversely affected competition in both Surrey and Kent.

### ***Remedies***

5.47. LTB considered that suitable remedies to alleviate what it viewed as a serious public interest issue in south London should be structural rather than behavioural. Its view was that Cowie should make a significant divestment, such as SLT, or Londonlinks and a combination of depots, thus reducing its dominance in south London.

### *LTB's views on the success of privatization*

5.48. LTB considered that, to a limited extent, it had achieved the objective of the London regulatory system to develop 'local' operators to challenge the larger operators. It cited a number of examples of smaller operators gaining new routes. It had initially been encouraged by the willingness of small operators to put in bids but examination had shown that the bid prices they were submitting were substantially higher than those of other bidders. LTB had accordingly taken steps to encourage these operators to sharpen their bids to match prevailing price levels, with some success. It told us that one small operator, Harris Bus, had recently won several routes after a number of previously unsuccessful attempts, as a result of putting in much keener bids. It stressed that it was essential to its responsibilities as a tendering authority for it to maintain such small companies to challenge the large operators. It had seen such a strategy as particularly important in recent months when LTB had seen contract prices hardening and even increasing in certain areas.

5.49. It was concerned that the reduced level of competition would jeopardize the intentions of the Secretary of State for Transport. The main non-statutory objective of the privatization of buses in London in November 1993 had been to manage the sale of the LBL subsidiaries in order to promote and sustain fair competition in the provision of bus services.

5.50. As it knew anecdotally, and as previous MMC inquiries had mentioned, there had not been as much evidence of competition between the major groups as it would have expected. Without the smaller operators, LTB considered that it would be difficult to sustain an effective, competitive market-place. In the London regulated market the position was particularly acute, as the nature of competition was one of competition for individual, five-year contracts, rather than 'on-the-road' competition, which existed in the deregulated market. LTB explained that its statutory obligation was to provide and secure public transport services for Greater London. Consequently, one of LTB's main responsibilities was to maintain effective competition in the London market, rather than allow the development of local duopolies or oligopolies.

### **Traffic Commissioner for North Eastern Traffic Area**

5.51. The Traffic Commissioner for the North Eastern Area of England told us that the merger was unlikely to have any significant effects on the road safety standards of the companies concerned.

### **Bus operators**

#### ***Armchair Passenger Transport Co Ltd***

5.52. This operator, a member of the Mundy Group, told us that competition should be maintained in the industry's long-term interests. No one company, therefore, should achieve more than 25 per cent of bus operations in London.

#### ***Crystals Coaches***

5.53. Crystals had recently been awarded three routes by LTB, all run from its existing Dartford premises. It had not had to open any new facilities to operate the new routes. It told us that it would continue to tender for routes, both within and outside its operating area. In total it operated 13 vehicles on five routes.

5.54. It told us that it was satisfied that there was very healthy competition in London before the merger. It feared, however, that the effect of the merger might be a retrograde step towards the old monopoly situation of the 1980s.

#### ***Fuggles of Benenden***

5.55. Fuggles of Benenden operates local bus services in the Tunbridge Wells area in competition with M&D, a former British Bus subsidiary.

5.56. In its view, the acquisition would have no effect either on competition in the supply of commercial or tendered bus services or on the level of fares and range and quality of services in the area.

### ***The Go-Ahead Group PLC***

5.57. Go-Ahead informed us that it viewed the acquisition positively, as it would lead to greater stability and consistency in the delivery of services to bus users and should lead to improvement in the quality of the British Bus fleet.

5.58. It knew, from its direct involvement, that the London market remained vigorously contested. It thought no service was possible except through the five-year contracts awarded by LTB. Given that an average of 20 per cent of the network was subject to tender each year, Go-Ahead did not believe there was any cause for concern if the initial market share of the merged group exceeded 25 per cent by a small amount.

5.59. It did not consider the merger to be against the public interest and could see positive public interest benefits. No safeguard was necessary beyond that already provided by the LTB tender regime. There was no case for requiring Cowie to divest parts of British Bus.

### ***London Central and London General***

5.60. These two companies are part of Go-Ahead and our respondent replied as Managing Director of both. He stated that there were currently 32 operators running contract services for LTB and although some were in common ownership, 21 different owners remained across London. This ensured that reasonable price competition would continue. It might look as if the level of competition varied in different geographical areas. However, there was nothing to stop operators bidding for work anywhere in London, as was shown by the award of a large proportion of work in the Orpington area to CentreWest. He believed the merger would not adversely affect the level of competition for LTB tendered work.

### ***Harris Bus Company Limited***

5.61. Harris Bus, based in Grays in Essex, informed us that it had no objection to the merger. It believed in free enterprise. Cowie had several companies around its own operational base, but it was no different from any other competing company.

5.62. Harris Bus had recently won five net cost competitive tenders from LTB, one of which was previously operated by British Bus.

### ***Lucketts of Watford***

5.63. Lucketts of Watford told us that at this stage the merger would not seriously affect its business. It hoped that the good but competitive relations which it had enjoyed with all the predecessors of British Bus would continue.

### ***Lynton Travel Group Limited***

5.64. Lynton Travel Group Limited had no objection to the merger and thought it would have no adverse effect on the business carried out by bus and coach operators in Essex.

### ***Metrobus***

5.65. Metrobus told us that it had no problem with the merger under the present regulated framework in London, with LTB acting as 'policeman'.

### ***Reading Buses***

5.66. Reading Buses, a division of Reading Transport Limited, saw no reason to object to the merger. It thought the change would have no material effect on either the supply of commercial and tendered bus services in the area or the level of fares and range and quality of services. The merged group only impinged on Berkshire in relation to competitive tendering in the south-eastern corners of the county.

### ***Reg's Coaches***

5.67. Reg's Coaches, based in Hertford, considered that the merger would not make a substantial difference, if indeed any, to the supply of commercial and tendered bus services in the area.

5.68. It was unable to comment on the level of fares and range and quality of services.

5.69. Whether or not the merger would be in the public interest could only be assessed in terms of business strategy, investment in vehicles, reliability and continuity of services, realistic fares structure and so on.

### ***H R Richmond Limited***

5.70. As a small local operator in Surrey, trading as Epsom Buses, Epsom Coaches, Epsom Tours and Epsom Travel, H R Richmond Limited (Richmond) was concerned about the impact of a large group and its effect on the competitive bus market.

5.71. Its principal concern was the former British Bus subsidiary, London & Country, which, it believed, currently provided around 55 per cent of bus services in Surrey. In the past that company's services had been tendered and run at what could be considered below cost. Richmond assumed that a certain degree of cross-subsidization applied in this situation, with the more profitable and long-established routes subsidizing the less profitable ones. Alternatively, London & Country might have been able to combine certain route sectors and contractual work with existing commitments. These were not options open to an operator with a small fleet of 18 buses.

5.72. Any move to introduce predatory services or further take-overs, where the number of services operated by London & Country and associated Cowie companies might increase their percentage share of the market for bus services in Surrey, particularly in the Epsom area, would cause concern. The present level of service provided within Richmond's operating area was adequate for all present operators to run commercially viable services whilst still providing a choice for the travelling public, with competitive fares.

5.73. Many of the present bus stops were owned by London & Country, for historical reasons. Although some stops had been adopted by the County Council and were therefore available to the company for the display of its timetables, this was not the case in respect of many others. For practical reasons it was not possible to relocate stops, and in any case the local authority would be unlikely to give approval for relocation.

5.74. Richmond suggested that the merged company's total percentage share of the Surrey bus market be restricted (or possibly reduced) to the level currently enjoyed by London & Country.

### ***Stagecoach Holdings PLC***

5.75. Stagecoach told us that it did not see the merger as necessarily against the public interest but that it had a number of concerns. It had been widely understood at the time of the 1993/94 privatization of LBL that the OFT would not consider British Bus an acceptable acquirer of LBL companies since it already owned much of the former London & Country Bus operations and Kentish Bus. Cowie, however, had been successful in acquiring two companies, the maximum number permitted to any one bidder. The recent merger of Cowie and British Bus therefore raised the same concerns as in 1994.

5.76. There was clearly an issue about the regulated London market and the surrounding deregulated market in parts of Surrey and Kent. If a company which encircled London in the unregulated market then had a very large share of the regulated market, the adverse effects of cross-subsidy could result.

5.77. Stagecoach believed our inquiry should also include the north-east of England. The MMC's monopoly report in 1995 on bus services in the north-east of England showed that North East Bus and British Bus would have a combined market share of over 25 per cent in that area. Cowie had acquired North East Bus in July 1996 and Stagecoach was concerned about the potential effect on competition. It was also very concerned at the OFT's failure to take further its March 1995 report on the behaviour of United Bus Services Ltd in operating bus services in Darlington. That company was now part of Cowie.

5.78. Turning to non-competitive issues, Stagecoach said that, according to its Stock Exchange announcement, Cowie had paid at least £89 million for British Bus with net liabilities at the date of its most recent audited accounts of £65 million. The implied goodwill of at least £154 million (and there might be additional consideration and goodwill of up to £20 million payable by way of deferred consideration, plus the expenses of a one-for-three rights issue) was by far the largest in the history of the UK bus industry.

5.79. It could be argued that excess goodwill payments must result in less investment and more pain for both passengers (through higher fares necessary to sustain the price paid or to service the additional borrowing incurred for investment) and employees (through increased pressure to reduce costs).

5.80. Another concern was that British Bus, in its own acquisitions, had a long history of including an element of short-term 'earn out-based' deferred consideration to provide incentives to management at acquired companies. The terms of the Cowie offer included up to £20 million of deferred consideration. The seller's management usually continued to work for the company and might be biased towards postponing the realization of efficiencies and towards raising fares, as a way to improve short-term, post-acquisition profitability. Such managers were often shareholders and thus it was in their interests that restructuring costs were postponed or camouflaged.

5.81. Stagecoach said that it would expect us to consider behavioural undertakings in respect of fares and frequency of services as one remedy. The more drastic option of partial or total divestment would seem to require either a break-up of British Bus or a separate listing based on a demerger of separate units.

5.82. Stagecoach's overall view, however, was that, certainly as far as London was concerned and possibly on a national level too, the merger was not necessarily against the public interest. Cowie would be required to invest considerable resources in reducing the average age of the British Bus fleet, which perhaps made it a less formidable competitor to smaller operators. A lot of resources had already been diverted to the former shareholders of British Bus and North East Bus.

#### *Stagecoach Selkent (South East London and Kent Bus Company Ltd) and Stagecoach East London (East London Bus and Coach Company Limited)*

5.83. The Chairman of these two companies (both part of the Stagecoach group) pointed out that the operation of bus services in south and east London by Cowie subsidiaries had all been won by competitive tender, for which Stagecoach had had an equal opportunity to compete.

5.84. Stagecoach Selkent intended to compete with Cowie subsidiaries for certain contracts when they were offered by LTB at renewal. It did not currently operate any commercial services outside the LTB area, but would not feel constrained in any way should it decide to do so.

#### ***Tillingbourne***

5.85. Tillingbourne informed us that in Surrey and surrounding counties (West Sussex and north-east Hampshire) the number of bus operators had been seriously reduced over the past few years.

5.86. Surrey had recently lost two small independents, Blue Saloon and Eurotravel, and the fleet of other operators had been reduced. Tillingbourne had managed to retain a market share and operated 60 buses and coaches in Surrey, West Sussex, Hampshire and Berkshire.

5.87. It seemed that with the merger, Cowie had an overwhelming monopoly, particularly in mid and east Surrey. Whilst there was some competition in east Surrey (with East Surrey Buses) it was not possible to ascertain how independent East Surrey Buses was, because of the number of London & Country buses it had on hire. With the enlarged Cowie, it seemed that cross-subsidy could exist. Where there was little competition, high prices were tendered, but in the few areas where there was competition, lower prices were submitted, often below an economic rate.

5.88. Until recently Tillingbourne had had a good relationship with local managers of London & Country as well as Stagecoach.

5.89. Because of Cowie's power and influence, Tillingbourne felt it could possibly be intimidated, although that had not yet happened. Cowie's fare levels did not seem to have changed but Tillingbourne had always had a reputation for keeping fares at a reasonable level, which often meant that its rates per mile were lower than others.

## **Local authorities**

### ***London boroughs***

5.90. We received views on the merger from five London boroughs, the local authorities in LTB's area.

#### *Hillingdon Borough Council*

5.91. We were told that Hillingdon Borough's Transportation Group was engaged in promoting public transport in general and buses in particular. It was concerned about the trend towards London bus routes being owned by a very small number of very big bus companies. Only a few companies, rapidly reducing in number, were now eligible to bid for London bus services.

5.92. The reduced number of bus operators reduced competitiveness and the number of alternative operators available to LTB if a contractor failed to deliver.

5.93. Mergers could potentially undermine the quality and cost of London bus services, which would be against the public interest.

#### *Royal Borough of Kingston upon Thames*

5.94. Because of the small proportion of buses operated in the borough of Kingston upon Thames by Cowie, the borough felt unable to comment on any effects the merger might have. The former Cowie Group had operated no routes in the borough and only 17 routes, representing just 23 per cent of departures from Kingston town centre, were operated by British Bus.

#### *Newham Borough Council*

5.95. Newham Borough Council was not directly affected by the merger because Cowie operated only one bus route (which had been won by another operator as from March 1997) and British Bus had none. However, the Council was concerned about the trend of smaller bus companies being taken over by a decreasing number of giant bus operators.

5.96. Previous experience indicated that terms and conditions relating to staff employment were detrimentally affected by such a merger. The ever-increasing trend of minibus routes replacing double-decker and full-size single-decker routes should not be used as means of depressing staff wages. Moreover, traffic congestion in cities such as London had reached barely tolerable levels. Drivers should be given realistic

running schedules; more recovery time should be incorporated at both ends of the journey to allow for late running. Professional driving in urban areas was a particularly stressful occupation.

5.97. The Council noted that because bus routeings, frequencies and bus fare levels in London were determined by LTB, this had given the network a degree of stability that had not been possible in the deregulated regime in other parts of the country.

### *Southwark Borough Council*

5.98. The London Borough of Southwark had no objection in principle to the merger, subject to a guarantee that it would in no way result in any deterioration of local bus services.

### *Wandsworth Borough Council*

5.99. Wandsworth Borough Council pointed out that of the 43 routes in the borough, only 12 were operated by Cowie. Of these, six were operated by Cowie South London and another six by former British Bus subsidiaries (Kentish Bus, Londonlinks and London & Country).

5.100. By contrast, London General operated 25 routes and London Central a further two (both in the Go-Ahead Group).

5.101. It was therefore hard to argue that the merger would produce unacceptable concentration of services in the hands of one operator in the borough. It would, however, result in Cowie having a very high concentration of the routes in neighbouring boroughs, such as Croydon, which might be problematic.

5.102. The success of the London tendering system in recent years, which had been effective in reducing costs to the taxpayer and improving quality of service to passengers, had been based on a high level of competition for contracts. Any developments which resulted in a significant level of reduction in competition in the London bus market would therefore be viewed with concern.

## ***Outside London***

### *Canterbury City Council*

5.103. We were told that it was unlikely that the Council would be opposed to the merger.

5.104. Bus services in the Canterbury area were provided by Stagecoach East Kent Ltd and there had been little competition between M&D (a former British Bus subsidiary) and that company. There were some small operator services in rural areas which were not run in competition with Stagecoach.

5.105. In addition to public bus services the Council provided an all-year-round park and ride service from two sites which so far had carried over 2 million passengers and operated on a five-year contract. There had been difficulties in gaining suitable contractors to tender; consequently the Council was usually faced with Stagecoach East Kent and a series of small contractors who had difficulties in funding the high service standards required. It was thought that the merger might provide a welcome addition to the Council's tender list and help to ensure that contracts were obtained on a best value basis.

5.106. M&D had very limited services within the district and the merger would not have any direct impact upon the current level of service.

### *Colchester Borough Council*

5.107. Colchester Borough Council had no views on the merger. However, it considered that there was adequate provision of bus services within the borough as another major operator, Eastern National, operated in direct competition with Colchester Borough Transport Limited (formerly part of British Bus). If one operator withdrew from Colchester the other would no doubt benefit and the public would still have an adequate bus service.

### *Darlington Borough Council*

5.108. Darlington Borough Council informed us that the vast majority of bus services in Darlington were operated either by Stagecoach or North East Bus (Cowie). Six other routes were operated by five separate companies.

5.109. The merger would not therefore affect the competitive balance of bus operations in the borough and it would not be appropriate to offer any comments.

### *Durham County Council*

5.110. Durham County Council informed us that it did not wish to make representations either in favour of, or in opposition to, the merger.

5.111. The effect of the merger in north-east England was to create an operator with territorial interests similar to those of the United Automobile Company when it was a subsidiary of the NBC. Go-Ahead's current territorial interests were also very similar to those covered by the Northern General Transport Company (the other NBC subsidiary in the North-East). It therefore appeared that the merger would have a neutral effect on bus services in County Durham.

### *Harrogate Borough Council*

5.112. We were informed that Harrogate Borough Council was unable formally to take a view within our time-scale. However, the Council's leading group was opposed to the merger on the grounds that it further diminished competition and would lead to reduced service and loss of jobs.

5.113. It said that when the Government chose to deregulate bus services it did so to drive down prices, create competition and improve levels of service. None of these objectives had been achieved. What the Council now saw was the re-amalgamation of small bus companies into what ostensibly were going to be a small number of nationally-based groups without any true relationship with public bodies.

### *Hertfordshire County Council*

5.114. Hertfordshire County Council pointed out that by virtue of this merger, the group controlling LDT Limited (The Shires) and County Bus would form the largest operator in the county with about 50 per cent of total mileage (LDT Limited had about 40 per cent of the market and County Bus 10 per cent). The group would have a dominant position in all areas of Hertfordshire except the districts of Welwyn Hatfield, Hertsmere and St Albans.

5.115. However, the Council did not necessarily see this as an adverse development because:

- (a) There was little overlap between these companies and it had been rare for them to compete against each other either commercially or for contracts.
- (b) The level of investment required to offset the years of uncertainty (at the time of deregulation and privatization) and to meet future requirements could probably only be achieved through economies of scale.

- (c) There was no evidence that companies were using their size to force up contract prices. If anything, these continued to fall slightly, even with specifications for higher-standard vehicles. Because the Council was a large customer of these companies, it offered grants for facilities on buses for elderly and disabled people, and there was close liaison on bus priority and other schemes to promote the use of passenger transport.

5.116. Whilst there was always a danger that large companies would use their competitive muscle in an unfair manner, the Council's view was that such tactics should be dealt with on a case-by-case basis on their merits. This might possibly require a tougher regulatory framework. The Council did not oppose the merger.

### *Kent County Council*

5.117. In principle, Kent County Council did not object to the merger. The British Bus subsidiaries included the Invictaway Group, owner of M&D and Kentish Bus. The Council had enjoyed a productive relationship with Invictaway and hoped that the new group would provide a stable basis for the development of a quality bus service for Kent.

5.118. There were advantages in dealing with large companies. Their operations were tidier and more integrated and they opened up the possibility of planning on a large scale and over a number of years. The merger might provide opportunities for substantial investment. On the other hand, Cowie's strong financial position might lead it to acquire more operations rather than investing in existing services.

5.119. The reliability of certain M&D services had been very poor recently, particularly in the Medway area. The Council was considering removing certain work because of M&D's failure to meet quality standards. Evidence was being laid before the Traffic Commissioner about its shortcomings.

5.120. 20 per cent of all bus services provided in Kent were subsidized, provided under contract to the Council. If Cowie continued to acquire small bus operators there would be no competition for supported bus services on either price or quality. Nor would there be the threat to M&D of other operators introducing new commercial services. Largely as a result of competition between large and small operators, some small companies had gone bankrupt or had been taken over. In recent months, several small companies had ceased to operate, most recently Mercury Passenger Services, which had been acquired by M&D in October 1996.

5.121. At present the Council had about nine small operators in the area served by the Invictaway Group who were available for local bus service contract work. If this number fell further, the competitive position could be perceived as a drift towards monopoly.

5.122. Operators had to have a commercial base in order to tender for Council work. There was already difficulty in attracting bidders, and the Council's impression was that the number of applicants per tender had been reduced.

5.123. The Council did not look on large companies based outside Kent as being major potential entrants to the market. Large operators based in Greater London were more likely to devote resources into winning more LTB contracts than tendering for small contracts, such as evening operations. School contract work was generally the domain of smaller operators. Moreover, much of Kent was well out of reach of existing depots in the Greater London area in terms of position, mileage and so on.

5.124. There was also a concern about having 'all one's eggs in one basket': the risks of a large, single operator failing to sustain its services. There was a need for a strong second force of operators to ensure effective competition.

5.125. In summary, the Council saw benefits in the merger but it was concerned that Cowie should make no further acquisitions of bus operations in Kent.

### *Northumberland County Council*

5.126. Northumberland County Council said that the merger appeared to have virtually no negative implications, at least in the short to medium term. If Cowie were strengthened financially and operationally, this might counterbalance the other national groups on Tyneside: Stagecoach and Go-Ahead.

5.127. There might well be benefits. The greater financial power of larger groups enabled more cost-effective capital investment and purchasing, cheaper borrowing rates and the development of a longer-term philosophy, rather than the short-termism that had tended to dominate the insecure period after deregulation.

5.128. From the point of view of competition in the area, Northumbria and Cowie's United Automobile Services had virtually no overlapping services in the Tyneside area but were complementary, particularly for services operating from Newcastle.

### *Surrey County Council*

5.129. Surrey County Council told us that some 68 to 70 per cent of bus mileage in Surrey was accounted for by commercial services. Tendered routes accounted for 65 per cent of the total number of routes operating in the county, but such routes were typically much shorter and less frequent than commercial routes.

5.130. Even before the merger the Council had been concerned with the competitive situation so far as it related to British Bus subsidiaries, whose acquisitions had been reducing competition, particularly in the east of the county. As a result, few companies were left in the market to tender for the Council's contracts. In the east Surrey area, the average number of bids per tender for tendered routes had fallen and in 1995/96 was only 3.5. In August 1996 a small operator, East Surrey Buses, had terminated a contract, partly because of proposed competition from London & Country, a British Bus subsidiary. Of 29 invitations to bid sent out for a replacement, only one was returned and that was from London & Country, to whom the Council had to award the contract.

5.131. The Council was therefore very concerned about the future competitive tendering process for local bus services and the possibility of relatively small companies feeling threatened by the presence of large ones. There had been an example in 1991/92 of London & Country competing with a smaller rival, Tillingbourne, on routes which the latter found profitable, presumably to try to destabilize its profitability.

5.132. Until recently, British Bus had not had a good record of investing in new stock. There had been signs that this was changing, but, given the high price that Cowie had paid for the group, the Council was concerned that there might be fewer new vehicles.

5.133. As far as remedies were concerned, an acceptable option would be for one of the Cowie subsidiaries, that is London & Country, Kentish Bus, Londonlinks or SLT, to be sold to another operator. This would restore an element of competition in east Surrey.

### *Tandridge District Council*

5.134. Tandridge District Council told us that it supported Surrey County Council's concerns about the effect of the merger in terms of competition and monopoly of local bus services.

### *Teesdale District Council*

5.135. Teesdale District Council informed us that it had no direct locus in this matter as Northumbria, which it understood was the only company in north-east England involved in the merger, did not operate in Teesdale.

5.136. However, it was concerned about the emergence of large groups such as Go-Ahead (which had recently taken over OK Motor Services, a significant operator in Teesdale) and North East Bus. This seemed drastically to reduce scope for independent operators and therefore competition, which ran totally counter to the objectives of the 1985 Act.

### *Tynedale District Council*

5.137. Tynedale District Council told us that it had no objection to the merger.

### *Watford Borough Council*

5.138. Watford Borough Council was not opposed to the merger. It realized that, in the present climate in the bus industry, there were economies and efficiencies in having large-scale operations, which could benefit local services. The operator concerned in their area (The Shires, a former British Bus subsidiary) had concentrated day-to-day management at local depots, with company-wide interests being dealt with only by head office. This gave a good balance between strategic and local requirements and there seemed no reason to think that the merger would change this manner of management.

5.139. The Council also believed that the number of other operators of local bus services provided adequate competition, which seemed set to continue for the foreseeable future. It also noted that the privatized London bus operators were becoming active in establishing operations outside their traditional areas and that in due course this could lead to an increasingly competitive situation in Watford.

## **Associations**

### ***Association of Local Bus Company Managers***

5.140. In the Association of Local Bus Company Managers' (ALBUM's) view the merger made little difference to the practical operating situation. Both Cowie and British Bus were formerly significant operating groups in their own right and the merger of the two companies would do little more than change the legal ownership of British Bus.

5.141. However, ALBUM considered that the growth of the significant and major bus operating groups would eventually lead to a monopolistic situation in which bus public transport within the UK would be controlled by a very small number of providers.

5.142. Such large groupings obviously presented a potential threat to the smaller operators that were still in existence. Events in towns such as Lancaster, Darlington and now Burnley were demonstrating the continuing dominance of major bus groupings.

### ***Kent Chamber of Commerce***

5.143. The Kent Chamber of Commerce informed us that the merger would not affect competition within the county because, although British Bus owned both the Kentish Bus and M&D bus services, the former Cowie Group had not operated any services in Kent.

5.144. However, it was concerned that the concentration of the market on a smaller number of large companies was already having an adverse effect on competition and service levels. For example, there were fewer back-up vehicles to cover breakdowns. If there were any reasons for thinking that the merger would lead to further loss of competition, that would be of great concern.

### ***London Regional Passengers Committee***

5.145. LRPC informed us that it had difficulty considering our questions because, as a lay committee, it did not have all the facts about the real impact of the merger on the London bus market.

5.146. LTB did not publish any information about bids it received for the bus routes which it put out to tender. LRPC did not therefore know whether, following the merger, there remained adequate competition, either in the area as a whole or in any part of it.

5.147. If it became clear as a result of our investigations that a monopoly supplier had been created by the merger, suitable conditions should be imposed on that supplier to redress that position.

5.148. LRPC believed that Cowie had paid much attention to quality of service on routes in the London area. The record of British Bus, however, was less enviable; indeed, LRPC had had to press LTB to take firm action against one of its subsidiaries. If the merger resulted in a higher quality of service on routes formerly operated by British Bus, that would be to London's advantage.