Williams-Shapps Plan for Rail: legislative changes to implement rail reform consultation - response from the Competition and Markets Authority

Background

1. The CMA is the UK's principal competition and consumer authority. It is an independent non-ministerial government department with responsibility for carrying out investigations into mergers and markets and enforcing competition and consumer law. The CMA's statutory duty is to promote competition, both within and outside the UK, for the benefit of consumers.

2. The CMA has a role in providing information and advice to government and public authorities.[1] The CMA's advice and recommendations are made with a view to ensuring that policy decisions take account of the impacts on competition and consumers.

3. The CMA publishes materials such as the Competition Impact Assessment guidelines to help policymakers consider the impacts that policy proposals will have on competition.

4. This response to the Williams-Shapps Plan for Rail: legislative changes to implement rail reform consultation does not comment on the policy objectives themselves but focuses on the implications for competition in rail markets and for the CMA and its functions.

Response to Question 4 "Do you have any views on the proposal to amend Section 25 of the Railways Act 1993 to enable appointment of a public sector operator by Great British Railways by direct award in specific circumstances? (paragraph 2.18) Please explain."

5. The CMA recognises there may be specific circumstances in which a short-term direct award to a public sector operator may lead to better outcomes for

[1] Under Section 7(1) of the Enterprise Act 2002, the CMA has a function of making proposals, or giving information and advice, ''on matters relating to any of its functions to any Minister of the Crown or other public authority (including proposals, information or advice as to any aspect of the law or a proposed change in the law).'' Under Section 7(1A) of the Enterprise Act 2022, the CMA may carry out this function in form of a "recommendation to a Minister of the Crown about the potential effect of a proposal for Westminster legislation on competition within any market or markets in the United Kingdom for goods or services"

passengers and taxpayers. Such awards would necessarily not be subject to competition. Therefore, to provide clarity to the market on future competitions 'for the rail', government should consider whether to set a limit to how long such direct awards should last, and whether to require the length of the direct award to be declared at the point of the award. If there is an intention for the appointment to be returned to a private sector operator, the relevant timescale should be communicated to allow prospective bidders sufficient time to bid.

Response to Question 8 "Do you agree with the proposed recasting of ORR's competition duty to better reflect public sector funding? (paragraph 2.49) Please explain."

6. The CMA and Office for Road and Rail (ORR) have concurrent powers to apply competition law and consumer protection law. These concurrency arrangements see the CMA and other concurrent regulators discuss how competition and consumer enforcement cases should progressed and by which body. The CMA's understanding is that the changes to the ORR's competition duty, in the way they have been set out in the consultation, do not affect these concurrency arrangements in relation to competition law or the relevant prioritisation of cases or the application of competition law by the ORR or the CMA.[2] If this understanding changes, for example if the design of the proposal is altered, the CMA would need to engage further with the Department for Transport and ORR on the matter to understand its impact.

7. The CMA's understanding is that this change, to recast the competition duty, will similarly not affect the application, interpretation or enforcement of consumer protection law (including under concurrency arrangements). The legal rights of passengers afforded under general consumer protection law should not in any way be diminished or traded-off against other objectives as part of the proposals.

Response to Questions 9-11 "Do you support the proposal to include in legislation, a power for Great British Railways to issue directions to its contracted operators to collaborate with one another in circumstances where doing so could otherwise give rise to concerns under Chapter I of the Competition Act 1998, in particular, where this could lead to defined benefits to taxpayers and/or passengers? (paragraph 2.54)"; "Would Train Operating Companies be willing to share information and collaborate in the way envisaged without the proposed legislative provisions? What are the risks to them without the proposed legislation? Would the proposed legislative

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[2] This is on the basis that the ORR's duties set out under s.4(1)(d) of the Railways Act 1993 (as amended) do not apply (per s.4(7A)) to its Competition Act 1998 functions (which are set out in s.67(3)).

approach help to resolve these risks?"; "Are there any particular additional safeguards (in addition to the safeguards outlined in paragraphs 2.54 - 2.55) that you consider necessary to support the interests of third parties (including freight, open access and charter operators) or to otherwise protect passengers and/or taxpayers?"

Role of competition

8. Effective competition happens when businesses compete to win customers by offering them a better deal. When firms compete effectively with each other, they cannot raise prices, or cut quality and service, without losing business. When competition is weak or ineffective, firms do not face the same pressures to keep prices down; to keep quality up; to operate efficiently; or to innovate. This comes at a cost to consumers, other businesses and the wider economy.

9. Under the franchise system, train operating companies (TOCs) have largely competed 'for the market' through the franchise award process rather than 'on the rail' by providing directly competing services, albeit some exceptions exist.[3] The core premise of this system is that effective competition between TOCs will ultimately benefit passengers by delivering against their competitively tendered franchise agreement (within which TOCs set fares and take on revenue risk). Under the planned passenger service contract (PSC) model, this model of competition for the market would evolve with GBR taking the role of a guiding mind, setting fares and taking revenue risk. This means that the scope for competition 'on the rail' will likely be diminished.

10. However, the potential for GBR to delegate some fare setting responsibility to TOCs (or the presence of open access operators) means that there may be some competition 'on the rail' as passengers choose between services operated by different TOCs. Competition will also continue to be central in the wider market, for example through competing for the franchises and in retailing, freight markets and throughout the supply chain, or in adjacent sectors such as bus travel.

11. In facilitating collaboration between TOCs, the CMA would therefore strongly encourage that any proposals are designed solely to achieve the desired policy objective, with the minimum possible restriction of competition, and that they actively ensure the management and mitigation of competition law compliance risks.

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[3] For example, on overlapping franchises on a single main line (such as on the East and West Coast Main lines) or where a destination is served by more than one line (such as Oxford or Exeter to and from London).

Collaboration and competition law

12. The Competition Act 1998 (CA98) sets out two key prohibitions: Chapter 1 prohibits agreements that prevent, restrict or distort competition, while Chapter 2 prohibits the abuse of a dominant position. As the UK's lead competition authority, the CMA, alongside ORR, is responsible for enforcing competition law.

13. The proposals are designed to provide greater certainty to TOCs when collaborating and sharing information as a necessary part of management of the rail network. As noted in the consultation, some forms of collaboration between businesses might be found to be in breach of Chapter I of the CA98. However, there is no blanket ban on collaboration between rival businesses. The prohibition applies only where such collaboration harms competition. Even then, individual or block exemptions may apply if the collaboration fulfils specific criteria ensuring that consumers receive a fair share of the benefit and the agreement is indispensable to achieving its objectives.

14. It is not generally for the CMA, as an enforcer of competition law, to provide views or assurances on whether any particular activity is compliant with competition law, although the CMA does publish guidance as to how it applies competition law in general. It is for firms to self-assess (with the benefit of their own legal advice where appropriate) whether their arrangements raise competition law concerns.

15. In the consultation it is proposed that GBR would be able to set out directions that would require TOCs "*to share information and undertake other collaborative activities with each other in circumstances where doing so could otherwise give rise to concerns under Chapter I of the Competition Act 1998*". Without insight into the full breadth of types of arrangement that it is envisaged that TOCs would need to enter into, it is not possible to comment on the competition law risk. However, it is clear under existing applicable guidance that private exchanges between competitors of their individualised intentions regarding future prices or quantities are particularly likely to give rise to competition law risks.[4] The extent to which the proposed legislative approach will effectively remove such risks will depend on the exact detail of the legislation. However, a well-designed regime would potentially reduce such risks.

16. Absent a bespoke regime to facilitate any such collaboration, TOCs would have to self-asses the legal compliance of any collaboration or information

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[4] See paragraph 74 of the EC's 2011 Horizontal Guidelines.

sharing under CA98 and would be open to enforcement action should that collaboration or information sharing breach CA98. The CMA always recommends that businesses seek independent legal advice to help determine if any agreements may be in breach of competition law. Even with an amended regime TOCs may still need to obtain independent legal advice to seek comfort that their conduct falls within the scope of any direction, and that any direction itself was within the scope of the regime.

Safeguards under a directions model

17. Assuming the directions proposal does reduce competition law risk, the design should aim to provide a suitably narrow focus to ensure that collaboration does not extend beyond the minimum necessary. The wider any protections or exemptions from CA98 are made, the greater the risk that competition between TOCs will be reduced. We note that is typically far harder to unwind the effects of weakening competition after the fact than to prevent that reduction in the first place.

18. We also note that the intended effective ability to disapply competition law in certain circumstances would be granted to an active market participant (GBR) rather than a Minister, regulator or other authority.

19. The design of appropriate safeguards and checks and balances is therefore particularly important especially in the event that GBR directly manages a TOC (such as an operator of last resort) and thus is directly or indirectly setting itself directions to provide legal cover for otherwise anticompetitive conduct. Safeguards broadly relating to GBR's ability to apply and design directions could include:

    (a) Clear and limited circumstances in which GBR can make the directions. This may include applying directions only where certain defined benefits/objectives are being sought and where bilateral engagement between TOCs and GBR could not reasonably reach the same outcomes.

    (b) Requirements on the specificity of directions, for example directions could be required to include: the purpose of the direction; detail on the activities being enabled by the direction and clarifications on what is not being enabled; and the time period the direction applies for.

    (c) Requirements to explicitly consider the potential risks to competition and explain how the directions go no further than necessary as part of the accompanying 'appropriate reasoning' noted in the consultation.

    (d) Requirements to publish the directions with the accompanying 'appropriate reasoning' before coming into effect.

(e) A route for third parties to challenge or appeal a direction and for the direction to be lifted.

20. Much of the potential impact of the safeguards relies on there being some form of potential appeal process in relation to the directions and on what basis an appeal can be instigated and by whom.

21. Further, there are potential practical safeguards that could be put in place for the businesses complying with directions. The intention would be to reduce the risk of 'leakage' of commercially sensitive information within directed businesses. Such 'leakage' could result in reduced competition or collusive outcomes, including in areas of direct competition for TOCs (eg tenders) and more broadly (for example wider businesses of TOCs such as other forms of transport). Those practical steps could include:

(a) Requirements to keep records of information exchanged and minutes of meetings held under the direction. This could be further strengthened by requiring GBR oversight, for example notification of information sharing or meetings held under the direction or requiring/enabling GBR attendance at meetings held under the direction (to minimise the risk of discussion of information not covered by the direction).

(b) Requirements for directed TOCs to conduct a risk assessment before collaboration or information sharing begins under a direction. The assessment would intend to highlight what the risks of internal 'leakage' or conflict may be.

(c) Requirements to share information on a 'need to know' basis with appropriate restrictions.

Consumer protection

22. The CMA notes that there are no changes proposed to the application of consumer protection law and strongly endorses this position. The CMA would further suggest that there is explicit acknowledgement that GBR is subject to consumer protection law and acknowledgement that (in reference to question 2) consumer rights of passengers are not a 'balancing factor' that can be traded off against other objectives such as those relating to public sector funding.

Response to Questions 12 "How should we ensure that Great British Railways is able to fulfil its accountability for the customer offer while also giving

independent retailers confidence they will be treated fairly? (paragraph 2.61) Please explain."

23. Our understanding is that the proposals include provision for the continuing role of independent retailers and that the proposed structure of GBR will "*ensure that Great British Railways' online retailing activities are independent of its wider decision making about retail strategy, including licensing decisions, and to maintain a level playing field between its direct online retail business and independent retailers"*.[5]

24. The CMA agrees that there should be a level playing field, so that third party retailers can compete with GBR.

25. While ensuring that "*Great British Railways' online retailing activities are independent of its wider decision making about retail strategy*" may help with this, the detail of how that independence is achieved is important. Factors to consider around operational separation and the ability for third party retailers to compete with GBR include:

    (a) How genuinely independent decision making is implemented and protected. The design of this should include the governance structure including the incentives introduced for different parts of that structure, reporting structures and the extent of information sharing between the online retail activities and other functions.

    (b) The extent to which GBR's online retail activities are financially independent. This might include the extent to which cost structures are shared or different functions are cross-subsidised within GBR. This may also include decisions on whether GBR online retail function has to pay a transfer price for the GBR branding and any retail advertising. Transparency around this point might potentially be achieved through distinct accounts for GBR's online retail activities.

    (c) The case for an equal access principle for all retailers. This could include equal access for all retailers (both GBR and independent operators) to relevant GBR information, such as on planned travel promotions. This information might be shared, for example, on fair, reasonable, and non-discriminatory (FRAND) terms.

    (d) That all retailers should be subject to the same provisions for redress.

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[5] Paragraph 2.60, The Williams-Shapps Plan for Rail - A Consultation on Legislation to Implement Rail Transformation

(e) That there should be a transparent process for making any subsequent changes to the framework for or approach to retailing of tickets, to allow all relevant parties opportunity to influence decisions to ensure that innovation is not curtailed.

Response to Questions 13 "Does the proposed governance framework give Great British Railways the ability to act as a guiding mind for the railways, while also ensuring appropriate accountability? (paragraphs 3.13) Please explain"

26. The proposals include a new approach to licence modifications for GBR, which includes the removal of a role for the CMA in modifications to the Network Rail licence (with Network Rail's functions being absorbed by GBR). The CMA notes these changes reflect and respond to broader changes to the roles of GBR, ORR and the Secretary of State.

Competition and Markets Authority
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