

Acquisition by Keolis Amey Docklands Limited of the Docklands Light Railway Franchise

ME/6496-14

The CMA's decision on reference under section 33(1) of the Enterprise Act given on 14 November 2014. Full text of the decision published on 27 November 2014.

Please note that [X] indicates figures or text which have been deleted or replaced in ranges at the request of the parties for reasons of commercial confidentiality.

Summary

1. Keolis Amey Docklands Limited (**KADL**), a joint venture established by Keolis UK Limited and Amey Rail Limited (together, the **Parties**), has been awarded (the **Franchise Award**) the Docklands Light Railway Franchise (the **DLR Franchise**) by Docklands Light Railway Limited (**DLRL**), a subsidiary of Transport for London (**TfL**).
2. The Competition and Markets Authority (**CMA**) considered whether the Franchise Award will result in enterprises ceasing to be distinct and constitute a relevant merger situation under section 23 of the Enterprise Act 2002 (the **Act**).
3. The Franchise Award entails the lease by KADL of the DLR rolling stock and infrastructure, as well as the granting of a licence for the use of the DLR brand and related IP rights. Further, the current workforce of the DLR will be transferred to KADL under the TUPE regulations. This will be for the duration of the DLR Franchise of around seven years (with a possible extension to nine years). The CMA could therefore not exclude the possibility that the DLR Franchise constitutes an enterprise.
4. However, the CMA also found that TfL and DLRL retain control over the commercial aspects of the DLR Franchise, including price levels, operational service levels, customer-facing activities, marketing, and long-term asset management. In addition, KADL faces a performance regime that covers the regular monitoring by DLRL of a range of performance metrics and includes potentially serious financial consequences of missing targets.

5. Taking these factors in the round, the CMA decided the Franchise Award will not result in enterprises ceasing to be distinct. A relevant merger situation **will not**, therefore, be created and the Franchise Award does not qualify for investigation under the Act.

Assessment

Parties

6. KADL is a joint venture established by Keolis UK Limited (holding 70%) and Amey Rail Limited (holding 30%) for the purpose of operating the DLR Franchise. Keolis UK Limited is part of an international transport group, majority-owned by SNCF Group. In the UK it has holdings in joint ventures that operate the TransPennine Express, Southern, Southeastern, London Midland and TSGN (Thameslink, Southern and Great Northern) rail franchises, as well as the Nottingham tram system [see end note 1]. Amey Rail Limited forms part of the Ferrovial Group and operates in public services and infrastructure.
7. The DLR Franchise is owned by DLRL, a subsidiary of TfL. The Docklands Light Railway (**DLR**) is a light rail system operating in East and South East London. The DLR is currently operated by Serco Limited under a franchise agreement with DLRL, which ends in December 2014. The passenger revenues from the DLR Franchise were around £125 million in the year 2012/13.

Transaction

8. On 4 July 2014 TfL announced that it had awarded the DLR Franchise to KADL. The franchise will run until April 2021, with an option for an extension until 2023.
9. The anticipated fixed fee payable to KADL for operating the service is around £[~~8~~] million for the first part year (until March 2015) and around £[~~8~~] million per year thereafter. The total payments due will vary depending on a base service plan being carried out and KADL's performance against specified performance metrics.

Jurisdiction

10. The Parties submitted that their respective group turnovers meet the thresholds for notification under the European Merger Regulation (Council Regulation (EC) 139/2004) (**EUMR**). However, the European Commission informed the Parties that the Franchise award did not appear to constitute a

concentration within the meaning of Article 3 of the EUMR and that therefore there was no obligation on the Parties to notify the transaction under the EUMR. The CMA therefore considered whether it had jurisdiction to review the Franchise Award under the Act.

11. The CMA has jurisdiction to review a transaction if it is a relevant merger situation under section 23 of the Act. One of the elements of this definition is that two or more enterprises will cease, or have ceased, to be distinct, ie if they are brought under common ownership or control (section 26 of the Act).¹ The Parties submitted that the Franchise Award does not concern the transfer of an enterprise. The CMA has therefore considered whether, in the present case, the Franchise Award results in enterprises ceasing to be distinct or is more akin to a management arrangement.²

Enterprises

12. The CMA considers that several factors suggests that the DLR Franchise may constitute an enterprise.³ Although the Parties submitted that the Franchise Award does not result in the transfer of any key assets relating to the operation of the DLR, the CMA notes that the Franchise Award entails the lease by KADL of the DLR rolling stock and infrastructure, as well as the granting of a licence for the use of the DLR brand and related IP rights, for the duration of the DLR Franchise. Further, the current workforce of the DLR will be transferred to KADL under the TUPE regulations.⁴ The CMA considers that it cannot exclude the possibility that the duration of the DLR Franchise – nearly seven years, with a possible extension to nine years – means that the Franchise Award amounts to a sufficiently long-term transfer of these assets and employees to KADL for the DLR Franchise to constitute an enterprise.
13. However, it was not necessary for the CMA to conclude on whether the DLR Franchise constitutes an enterprise, because, as set out below, the CMA does not consider that the Franchise Award gives KADL a sufficient level of control over the DLR Franchise.

¹ See *Mergers: Guidance on the CMA's Jurisdiction and Procedure* (CMA2, January 2014), from paragraph 4.5.

² Section 66(3) of the Railways Act 1993 provides that the award of a rail franchise constitutes an acquisition of control of an enterprise. However, this does not apply to franchises awarded by TfL or its subsidiaries pursuant to the Railways (London Regional Transport) (Exemptions) Order 1994.

³ See *Mergers: Guidance on the CMA's Jurisdiction and Procedure*, paragraphs 4.6 to 4.11.

⁴ The Transfer of Undertakings (Protection of Employment) Regulations 2006.

Control

14. As noted above, enterprises cease to be distinct under section 26 of the Act if they are brought under common ownership or control. The ability to exercise material influence is the lowest level of control that may give rise to a relevant merger situation. When making its assessment, the CMA focuses on an acquirer's ability to materially influence policy relevant to the behaviour of the target entity in the marketplace, including the strategic direction of the target entity and its ability to define and achieve its commercial objectives.⁵ The CMA has therefore assessed whether in the present case the Franchise Award will give KADL material influence over the operation of the DLR.
15. The Parties submitted that they will not gain any material influence, since all decisions as to how DLR services are operated are under the control of TfL. The Parties stated that they are merely responsible for the DLR's train and passenger service operations and the maintenance of its infrastructure and trains, while all key commercial decisions are taken by TfL or its subsidiary DLRL, specifically:
- Ticket pricing is determined by TfL.
 - Timetabling and frequency of DLR trains are set at minimum levels in the franchise agreement between KADL and DLRL, which includes base service plans that determine maximum intervals between trains and the minimum length of each train, and specifies the days upon which passenger services must be operated and the times of the first and last trains on each line.
 - Ancillary services such as customer service activities (including responding to complaints), marketing, advertising and estate management are undertaken by TfL.
 - Decisions regarding capital investment and the long-term asset management and renewal strategy are taken by DLRL.⁶
16. The Parties also noted that all passenger revenues are recouped by DLRL and that KADL's fee for operating the DLR is in no way related to passenger numbers or revenues. The Parties stated that, as a result, they have no commercial incentive to increase ticket revenues.

⁵ *Mergers: Guidance on the CMA's Jurisdiction and Procedure*, paragraph 4.14.

⁶ The Parties also noted that DLRL is the 'Infrastructure Manager' for the purposes of health and safety legislation.

17. The Parties' submissions in this respect were supported by information provided to the CMA by TfL and set out in a paper for TfL's Finance and Policy Committee of 5 June 2014. This paper states, for example, that the franchise agreement 'will not transfer the responsibility for the matters that influence revenue outcomes (such as investment decisions, marketing and so on)'.⁷
18. The CMA considered whether, notwithstanding the fact that, as set out above, several commercial decisions are in the control of TfL, KADL will have the ability to exercise material influence over the DLR Franchise through KADL's operational control of the assets and employees associated with operating the DLR. The CMA considers that, for example, if KADL has this ability, it may have an incentive to use this operational control to degrade any DLR services that overlap with the Parties' existing public transport services. This incentive could arise because the Parties would gain revenues from passengers switching from the DLR to their existing services (since DLRL takes the DLR revenue risk).
19. The Parties stated that under the franchise agreement for the DLR Franchise, KADL's fee will be adjusted depending on its performance against key performance indicators (KPIs) set by DLRL, with bonuses for good performance and abatements if KPIs are missed. The franchise agreement sets out a range of performance metrics covering operational and customer facing targets, including metrics related to:
 - cancellations and delays (including a specific penalty for delays to passenger journeys of at least 20 minutes)
 - journey times and excess waiting times
 - short train formations
 - station closures
 - station and train cleanliness
 - station equipment requirements.⁸
20. The Parties submitted that KADL's performance will be regularly monitored and measured by DLRL. The franchise agreement provides that KADL will

⁷ Paper for TfL's Finance and Policy Committee, dated 5 June 2014, headed '[Item 10: Docklands Light Railway Franchise Procurement](#)' at paragraph 4.17.

⁸ This was supported by the paper for TfL's Finance and Policy Committee, paragraphs 4.20-22. The station equipment requirement regards the proper operation of equipment including ticket vending machine, lifts, escalators, CCTV and PA systems.

provide data on its operational performance to DLRL on a daily basis and will report to DLRL on its compliance with customer facing performance targets in each four-week period. In addition, the Parties submitted that under the franchise agreement DLRL will conduct regular customer satisfaction surveys to test passengers' views on cleanliness, train service, service information, staff, personal safety and overall satisfaction.

21. TfL considers that the monetary values ascribed to the bonuses and abatements that apply when KADL exceeds or misses targets, provide sufficient financial incentives and encourage KADL to correct any failures as soon as possible and to avoid repeated failures.⁹ The Parties further noted that, in addition to this bonus and abatement system, under the franchise agreement KADL will become subject to an enforcement regime if it repeatedly fails to meet its targets. This consists of remedial plans and warning notices with increasing levels of monitoring by DLRL. If a specific number of notices are given within a specific period, DLRL can 'step in' and take such action as it considers necessary to remedy any failure by KADL to perform its obligations. Ultimately a 'franchisee default' may arise and DLRL may terminate the DLR Franchise or suspend KADL's performance of part of it. These steps will have financial consequences for KADL, including, for example, an obligation to reimburse DLRL for the costs it incurred in taking action and in re-tendering the DLR Franchise.¹⁰
22. Based on the evidence regarding the performance regime that KADL is subject to – in particular the range of performance metrics, the regular monitoring by DLRL and the significant financial and other consequences for KADL of missing targets, including possible stepping in by DLRL and early termination of the DLR Franchise – the CMA considers that KADL's ability to degrade DLR services is not at a level that gives it material influence over the DLR Franchise.

Conclusion on jurisdiction

23. The CMA notes that, as set out above, KADL will use the assets, IP rights and employees associated with the DLR Franchise to provide DLR services for the duration of the DLR Franchise of around seven to nine years. However, the CMA also notes that TfL and its subsidiary DLRL retain control over commercial aspects of the DLR Franchise, including price levels, operational service levels, customer-facing activities, marketing, and long-term asset

⁹ *Idem*, paragraphs 4.23-27.

¹⁰ The Parties noted that KADL's liability is backed by a parent company guarantee and a £15 million performance bond. Its liability is capped at £60 million in most circumstances.

management. In addition, KADL faces a performance regime that covers the regular monitoring by DLRL of a range of performance metrics and includes potentially serious financial consequences of missing targets.

24. Taking all of the facts set out above into account, the CMA considers that, on balance, the Franchise Award will not result in enterprises ceasing to be distinct and that therefore a relevant merger situation will not be created.

Decision

25. Consequently, the CMA does not believe that it is or may be the case that arrangements are in progress or in contemplation which, if carried into effect, will result in the creation of a relevant merger situation.

Nelson Jung

Director of Mergers

Competition and Markets Authority

14 November 2014

End note 1: In relation to paragraph 6, the CMA clarifies that the TSGN rail franchise is not yet fully operational. In particular, the services that are currently part of the Southern rail franchise will become part of the TSGN rail franchise in July 2015.