

Completed acquisition by Arriva Rail North Limited of the Northern Rail Franchise

Decision on relevant merger situation and substantial lessening of competition

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.

The CMA's decision on reference under section 22(1) of the Enterprise Act 2002 given on 12 May 2016. Full text of the decision published on 14 June 2016.

ME/6591/16

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SUMMARY

1. On 9 December 2015, the Department for Transport (**DfT**) announced that the Northern rail franchise (the **Northern Franchise**) had been awarded to Arriva Rail North Limited (**ARN**) (the **Franchise Award**), a wholly-owned subsidiary of Arriva plc (**Arriva**), which itself is a wholly-owned subsidiary of Deutsche Bahn AG. In this decision, Arriva, ARN, and the Northern Franchise are together referred to as the **Parties**.
2. The Competition and Markets Authority (**CMA**) has assessed the Northern Franchise under the merger control provisions of the Enterprise Act 2002 (the **Act**). The Northern Franchise qualifies for investigation under those provisions since ARN is considered to be acquiring control of the Northern Franchise by virtue of section 66(3) of the Railways Act 1993, and the turnover test is met. ARN's operation of the Northern Franchise commenced on 1 April 2016. The CMA therefore believes that it is or may be the case that a relevant merger situation has been created.
3. Consistent with the CMA's previous decisional practice relating to the assessment of rail franchise awards, in assessing the Franchise Award, the CMA has considered whether it is or may be the case that the Franchise Award has resulted, or may be expected to result in a substantial lessening of competition (**SLC**) as a result of horizontal unilateral effects, in relation to competition for the market (ie competition for rail franchises) and competition in the market (ie at the level of bus-on-rail and rail-on-rail overlaps).
4. In terms of assessing competition for the market at a national level, the CMA considers that the Franchise Award does not reduce the number of likely bidders for future franchises and considers that the Franchise Award does not provide the Parties with an incumbency advantage that would raise concerns for future franchise awards. The CMA therefore considers that there is no realistic prospect of an SLC for rail franchises as a result of the Franchise Award.
5. As regards competition in the market, the Parties overlap in the supply of public transport services in the UK, ie bus and rail services. On a cautious basis, the CMA considers the supply of each mode of transport separately in its assessment, noting that, as a starting point, a service is likely to compete more closely with another service of the same mode than a service of a different mode of transport. The CMA considers that passenger demand is for travel between two specific points (ie an origin and destination). Consistent with previous cases, the CMA assesses the impact of the Franchise Award on competition on a flow-by-flow basis, where a 'flow' is defined as a connection between two such specific points. The CMA has also considered the effects of

the Franchise Award in the context of routes as well as flows. In the present case and consistent with previous cases, the CMA did not have sufficient evidence to suggest that private transport, including transportation by car, is a sufficient constraint on any of the overlapping flows it considered.

6. When analysing the competitive effects of mergers involving a large number of local overlaps, it is common practice for the CMA to apply relevant filters¹ during a typical Phase 1 investigation in order to quickly and practically exclude overlaps where the CMA believes that there are no competition concerns, and to focus its Phase 1 analysis on those remaining local markets that are more likely to give rise to competition concerns.
7. In the present case, the CMA has applied a number of filters on a cautious basis, which when taken together, have identified flows which do not give rise to a realistic prospect of an SLC and, as such, have been excluded from further analysis. Flows which remain after application of these filters, and therefore raised *prima facie* competition concerns, have been subjected to a more detailed assessment in order to determine the strength and/or magnitude of these concerns.
8. With regard to bus-on-rail overlaps, the CMA found that 45 routes (183 bus-on-rail flows) remained to be assessed following the application of filters. Given the large volume of routes, and related difficulties with data gathering, the CMA initially received from Arriva a prioritised set of data for 14 of these 45 routes on the basis that these overlaps were *prima facie* more likely to raise competition concerns. For these 14 routes, the CMA undertook a detailed flow-by-flow assessment (as set out in Annex 1²) following which it concluded that the Franchise Award gives rise to a realistic prospect of an SLC on 13 of those routes (104 bus-on-rail flows). With regard to the other 31 routes which remained after application of the filters³, the CMA concluded that it cannot exclude that the Franchise Award gives rise to the realistic prospect of an SLC.
9. With regard to rail-on-rail overlaps, the CMA found that the Franchise Award gives rise to 54 rail-on-rail flows which remain after application of the filters and therefore raise *prima facie* competition concerns. For these 54 flows, the CMA undertook a detailed assessment of additional factors (as set out in paragraphs 101 -103) following which the CMA considered that competition

¹ The CMA and its predecessor bodies have generally considered filters when assessing franchise awards based on: the relative importance of overlapping flows, countervailing competition and flows of relatively little importance (*de minimis*). See, for example, Competition Commission, [Review of methodologies in transport inquiries](#), May 2007, paragraph 26.

² See Annex 1 for the CMA's detailed assessment of 14 routes with bus-on-rail overlaps.

³ See Annex 2 for the list of 31 routes with bus-on-rail overlaps raising competition concerns.

concerns could be ruled out for a further 16 flows. With regard to the 38 rail-on-rail flows which remained, the CMA cannot rule out that there is a realistic prospect that the Franchise Award has resulted or will result in an SLC.

10. In light of the above, the CMA believes that it is or may be the case that the Franchise Award gives rise to the realistic prospect of an SLC as a result of horizontal unilateral effects in relation to bus-on-rail overlaps on 44 routes and 38 rail-on-rail flows.
11. The CMA considers that the aggregated annual value in the UK of the market(s) concerned (ie the markets for which the CMA concludes that there is a realistic prospect of an SLC) is in excess of £10 million. Consistent with the CMA's policy not to apply the *de minimis* exception in circumstances where the size of the markets concerned exceeds £10 million, the CMA finds that it would not be appropriate to consider this exception in this case.
12. Given the CMA's conclusion that the Franchise Award gives rise to a realistic prospect of an SLC as a result of horizontal unilateral effects in relation to bus-on-rail overlaps on 44 routes and 38 rail-on-rail overlapping flows, the CMA is considering whether to accept undertakings under section 73 of the Act. Arriva has until 19 May to offer an undertaking to the CMA that might be accepted by the CMA. If no such undertaking is offered, then the CMA will refer the Franchise Award pursuant to sections 22(1) and 34ZA(2) of the Act.

ASSESSMENT

Parties

13. Arriva is a public limited company which operates passenger transport services both in the UK and in Europe. Arriva currently operates:
 - (a) three rail franchises⁴ under:
 - (i) Cross-Country Trains Limited (**XC**) – XC rail services span the UK from Aberdeen in the north to Stansted Airport, Plymouth and Penzance in the south;⁵

⁴ Franchised rail operating companies (TOCs) operating rail franchises are awarded the right to run specific services within a specified area for a specific period of time, in return for the right to charge fares and, where appropriate, to receive financial support from the franchising authority (now the Rail Group in the DfT). See CMA [Competition in passenger rail services in Great Britain](#), March 2016, paragraph 2.5.

⁵ This franchise agreement is due to expire in October 2016 although discussions regarding a direct award to extend the franchise up to November 2019 are on-going.

- (ii) Arriva Trains Wales (**ATW**) – ATW rail services are provided predominantly within Wales, with some services in Northern England;⁶ and
 - (iii) The Chiltern Railway Company Limited (**Chiltern**) – Chiltern rail services operate between Birmingham Snow Hill and London;⁷
- (b) two rail concessions⁸ under:
- (i) DB Region Tyne and Wear Metro Limited (**DBTW**) – Arriva operates DBTW under a Concession Agreement with Nexus, the Passenger Transport Executive (**PTE**) for the Tyne and Wear region;⁹ and
 - (ii) London Overground Rail Operations Limited (**LOROL**) – a joint venture between Arriva and MTR Corporation (of Hong Kong) which operates the LOROL Concession on behalf of Transport for London;¹⁰
- (c) two open access¹¹ rail services:
- (i) Grand Central Railway Company Limited (**GC**) – GC provides high speed train services between London and Sunderland and between London and Bradford (calling at various intermediate stops);¹²
 - (ii) Alliance Rail – Alliance Rail is not currently providing rail services but it intends to become an open access operator providing passenger services between London and Blackpool; and
- (d) local bus services around the UK - Arriva operates bus services in the area covered by the Northern Franchise through the following companies:
- (i) Arriva Durham County Limited;
 - (ii) Arriva North West limited;

⁶ This franchise agreement is due to expire in October 2018.

⁷ This franchise agreement is due to expire in December 2021.

⁸ There are a few rail services which are exempt from the franchising provisions of the Railways Act 1993 and are operated by the private sector on behalf of a public sector body. Most of these services are in London and are let as concession agreements by Transport for London.

⁹ DBTW's Concession Agreement is due to expire in March 2017 although it could be extended to March 2019.

¹⁰ The LOROL Concession Agreement is due to expire in November 2016.

¹¹ Open access operators (OAOs) operate on a commercial basis with no subsidy and are required to apply to the Office of Rail and Road (ORR) and Network Rail for the necessary access rights to run their proposed service. Unlike franchises, fares set by OAOs are not subject to fare regulation; however, OAOs have the same general ticketing obligations as franchised TOCs, other than with respect to ticket offices. See CMA [Competition in passenger rail services in Great Britain](#), March 2016, paragraphs 2.15 and 2.16.

¹² GC's track access agreement with Network Rail will expire in November 2026.

- (iii) Arriva Northumbria Limited;
- (iv) Arriva Tees & District Limited;
- (v) Arriva Yorkshire Limited; and
- (vi) Yorkshire Tiger Limited.

14. The Northern Franchise rail service provides inter-urban, commuter and local services across the whole of northern England. The turnover of the Northern Franchise in 2014 was around £529 million in the UK.¹³

Transaction

15. On 9 December 2015, the DfT announced that ARN was the successful bidder for the Northern Franchise. On 22 December 2015, the DfT (Secretary of State for Transport) and ARN entered into a franchise agreement and associated agreements confirming the award of the Northern Franchise to ARN. The Northern Franchise commenced on 1 April 2016 for a term of nine years, expiring on 1 April 2025 (subject to a possible extension of up to one year).

Jurisdiction

16. The award of a rail franchise constitutes an acquisition of control of an enterprise by virtue of section 66(3) of the Railways Act 1993. The Northern Franchise and Arriva have therefore ceased to be distinct.
17. The UK turnover of the Northern Franchise exceeds £70 million, so the turnover test in section 23(1)(b) of the Act is satisfied. The CMA therefore believes that it is or may be the case that a relevant merger situation has been created.
18. The Franchise Award meets the thresholds under Council Regulation (EC) 139/2004 (the **EC Merger Regulation**) for review by the EU Commission (the **Commission**). The Parties submitted a reasoned submission to the Commission on 18 December 2015 requesting pre-notification referral to the CMA under Article 4(4) of the EC Merger Regulation. The CMA informed the Commission that it agreed with the referral request and considered the Franchise Award capable of being reviewed in the United Kingdom under the

¹³ In the year to 3 January 2015.

Act. On 27 January 2016, the Commission announced its decision to refer the Franchise Award to the CMA for review.¹⁴

19. The preliminary assessment period for consideration of the Franchise Award under section 34A(2) of the Act started on 28 January 2016, an issues meeting was held with the Parties on 12 April 2016 and the statutory 45 working day deadline for a decision is 12 May 2016 (including an extension to the preliminary assessment period under section 34A(5) of the Act).

Background

20. The Northern Franchise is currently the largest train franchise in Britain in terms of the size of the network and the number of services run. It is one of the most extensive franchises in the UK providing inter-urban, commuter and local services across the whole of Northern England, serving 526 stations and operating over 15,000 local and regional services per week.¹⁵ The population of the area served by the franchise is around 15 million people and around 90 million journeys were made in 2012/13.¹⁶
21. The Northern Franchise rail service operates over most rail routes in Northern England, from Chathill in the north to Stoke and Nottingham in the south of the region, and from Liverpool in the west to Hull in the east. Services provided by the Northern Franchise include:
 - (a) longer-distance regional services which connect major urban centres (eg Nottingham – Leeds; York – Blackpool and Sheffield – Doncaster – Hull);
 - (b) urban services, eg commuter services around the main northern cities such as Leeds, Liverpool, Newcastle, Sheffield and Manchester. 18 of the top 20 passenger flows by volume start or finish in Manchester or Leeds; and
 - (c) rural services, eg routes along the Cumbrian Coast from Carlisle to Barrow in Furness and the route from Hull to Scarborough in the East.¹⁷
22. Arriva UK bus, which is part of the Arriva group owned by Deutsche Bahn AG, is a major bus operator in the UK. It is the third largest operator in the regional bus market, operating around 5,900 buses in London, the North East, North West and South East of England as well as in Yorkshire, The Midlands and

¹⁴ Case M.7897 – ARRIVA RAIL NORTH / NORTHERN FRANCHISE

¹⁵ The TransPennine Express franchise provides inter-urban services between the major cities in the regions of the Northern Franchise and other franchised and OAOs also provide services which enter or cross the regions.

¹⁶ Northern Prospectus, Department for Transport, June 2014, pages 7, 20 and 37.

¹⁷ Northern Prospectus, Department for Transport, June 2014, page 38.

Wales.¹⁸ Arriva's UK bus services are operated by individual operating companies. The relevant bus operating companies for the purposes of the CMA's review are Arriva North West and Wales, Arriva Yorkshire and Arriva North East. In some regions, premium services are operated under the Sapphire brand and inter-urban express services are operated under the Max brand.

Overlapping services

23. Arriva identified 1,041 flows where existing Arriva bus services and Northern Franchise rail services provide overlapping services and 167 flows where Arriva's rail services overlap with the Northern Franchise.
24. Arriva also submitted that its subsidiary responsible for applying for open access rail opportunities, Alliance Rail Holdings Limited (**Alliance Rail**), will continue to pursue open access rail opportunities¹⁹, although it is currently focussed on supporting the launch of the West Coast services, following receipt of approval of its access rights from the Office of Rail and Road (**ORR**) on 7 August 2015²⁰; and, as such, there were no current plans with regards to future application opportunities.²¹
25. The CMA notes that Alliance Rail has made further applications to operate services on the East Coast Main Line between London King's Cross and Edinburgh calling at Newcastle, and between London King's Cross and West Yorkshire/Lincolnshire.²² The CMA believes that this indicates that Alliance Rail has been pursuing, and will continue to pursue, rail services opportunities and as such considers that additional overlapping services and flows could be identified as a result of overlaps between planned open access services under Alliance Rail and the Northern Franchise.

Counterfactual

26. The CMA assesses a merger's impact relative to the situation that would prevail absent the merger (ie the counterfactual). For completed mergers, the

¹⁸ <https://www.arrivabus.co.uk/about-us/arriva-group/> and <http://www.arriva.co.uk/countries/uk/uk-bus>

¹⁹ Including services on the East Coast Main Line between Edinburgh and London. See <http://www.alliancerail.co.uk/gner/>

²⁰ The application to operate six return train services each day, including weekends, was submitted by Great North Western Railway (GNWR), an Arriva company and a sister company of Grand Central, which already operates successful passenger services between the North East and West Yorkshire to London. ORR approved Alliance Rail's access rights in relation to these services on 7 August 2015 and the new services will start in 2018.

²¹ Final Merger Notice, paragraph 20.

²² <http://www.alliancerail.co.uk/journal/>

CMA generally adopts the pre-merger conditions of competition as the counterfactual against which to assess the impact of the merger.²³

27. However, in rail franchises, the pre-merger situation cannot be the appropriate counterfactual, as the existing rail franchise is coming to an end and a new franchise must be awarded to one of the short-listed bidders. The CMA therefore treats the appropriate counterfactual as the award of the franchise to a train operating company (**TOC**) that raises no competition concerns or where any concerns could be remedied through undertakings in lieu (**UILs**) of a reference to Phase 2.²⁴ Accordingly, in so far as the operation of the Northern Franchise is concerned, the CMA will assess the Franchise Award against a counterfactual whereby the Northern Franchise is awarded to a TOC raising no competition concerns or where any competition concerns could be remedied through UILs.

Frame of reference

28. The CMA considers that market definition provides a framework for assessing the competitive effects of a merger and involves an element of judgement. The boundaries of the market do not determine the outcome of the analysis of the competitive effects of the merger, as it is recognised that there can be constraints on merger parties from outside the relevant market, segmentation within the relevant market, or other ways in which some constraints are more important than others. The CMA will take these factors into account in its competitive assessment.²⁵

Product scope

Competition for the market

29. As regards competition for the market, the CMA considers that the relevant product frame of reference is the award of rail franchises.

²³ [Merger Assessment Guidelines](#) (OFT1254/CC2), September 2010, from paragraph 4.3.5. The [Merger Assessment Guidelines](#) have been adopted by the CMA (see [Mergers: Guidance on the CMA's jurisdiction and procedure](#) (CMA2), January 2014, Annex D).

²⁴ See ME/6506/14 Intercity Railways Limited/ICEC Franchise, CMA (2014), paragraph 22; ME/6470/14 Govia Thameslink Railway Limited/Thameslink, Southern and Great Northern Rail Franchise, CMA (2014), paragraph 34.

²⁵ [Merger Assessment Guidelines](#), paragraph 5.2.2.

Competition in the market

30. The Parties overlap in the provision of public transport services, including bus services and rail services.
31. Arriva submitted that the relevant product market could, on a cautious basis, reflect previous decisions by the CMA and its predecessor bodies.
32. In line with previous decisions, the CMA has in the present case considered, on a cautious basis, public transport as a separate product market to private transport.²⁶ The CMA has in this case considered the provision of all public transport services as a starting point for the purpose of assessing the competitive effect of the Franchise Award but notes that the precise product scope varies on a flow-by-flow basis.
33. The CMA and its predecessor bodies have noted that passengers make choices between various modes of public transport (eg rail, bus, coach) that are available for a particular journey.²⁷ Where passengers face multiple travel options, either of the same mode or different modes of transport, their choices are driven by a range of factors, such as travel to/from the station/stop, journey time, service frequency, fares and general service quality.²⁸ Given that these factors may vary between flows, the extent to which different travel options are close substitutes may also vary across flows.
34. The CMA has therefore considered the substitutability between different modes of public transport relevant to this case (ie rail and bus) on a flow-by-flow basis. However, the CMA considers as a reasonable starting point that a service competes more closely with another service of the same mode of transport on a flow than with a service using a different mode of transport. The CMA did not receive evidence suggesting that a departure from this practice in previous cases was appropriate in the present case.
35. The Competition Commission (**CC**) previously distinguished leisure travel from business travel and commuting due to different sensitivities in price, journey time and duration.²⁹ The CMA does not consider it necessary to conclude on whether leisure and business passengers should be considered

²⁶ See, for example, CC [Review of methodologies in transport inquiries](#); ME/6470/14 Govia Thameslink Railway Limited/Thameslink, Southern and Great Northern Rail Franchise, CMA (2014), paragraph 24; ME/6506/14 Intercity Railways Limited/ICEC Franchise, CMA (2014), paragraph 32.

²⁷ ME/6506/14 Intercity Railways Limited/ICEC Franchise, CMA (2014), paragraph 33.

²⁸ The combination of these service factors is known as 'generalised cost'. See CC [Review of methodologies in transport inquiries](#), May 2007, paragraph 12.

²⁹ CC [Review of methodologies in transport inquiries](#), May 2007. See also ME/6506/14 Intercity Railways Limited/ICEC Franchise, CMA (2014), paragraph 34.

in separate product markets since it has not received submissions in this case on this potential distinction.

Geographic scope

Competition for the market

36. In line with previous decisions, the CMA has considered competition for the award of rail franchises on a national basis.³⁰

Competition in the market

37. As passengers travel between a specific point of origin to a specific point of destination (ie a point-to-point journey), the demand is therefore for travel between two points. Consistent with previous cases, the CMA assesses the impact of the Franchise Award on a flow-by-flow basis, where a 'flow' is defined as a connection between two specific points. Furthermore, the CMA has considered the effects of the Franchise Award in the context of routes as well as flows.³¹
38. Arriva submitted that bus stops and train stations could be treated as overlapping where there was a distance of no more than 1,600 metres between them, noting that this was a conservative approach considering previous decisions.
39. In previous rail franchise cases, for flows involving travel to or from an urban area (either at one or both ends), bus stops and train stations were treated as overlapping where there was a distance of no more than 1,200 metres between them.³²
40. The CMA considers that existing Arriva rail and/or bus services overlap with the Northern Franchise services where they provide:
- (a) journeys between the same two rail stations;
 - (b) journeys where the catchment area of a bus service overlapped with the catchment area of the nearest rail station (ie where there was a distance of no more than 1,600 metres between bus stops and train stations);

³⁰ ME/6506/14 Intercity Railways Limited/ICEC Franchise, CMA (2014), paragraph 31.

³¹ See CC [Review of methodologies in transport inquiries](#), May 2007, paragraphs 5-7.

³² See CC [Review of methodologies in transport inquiries](#), May 2007, paragraph 20 and ME/6506/14 Intercity Railways Limited/ICEC Franchise, CMA (2014), paragraph 41.

- (c) journeys between the same two settlements, even where different stations or bus stops in the same settlement are used; and
 - (d) journeys to a main commuter city (such as Manchester) from two alternative stations or bus stops in nearby towns or villages.
41. Arriva provided information on overlaps using the approaches set out under paragraphs 40(a) and 40(b). Arriva submitted that:
- (a) in relation to rail-on-rail overlaps, its approach accounted for the journeys under paragraphs 40(c) and 40(d) above, since it included all stations within a given settlement where there is more than one station.³³ Arriva also submitted that due to the extensive network of the Northern Franchise, no additional overlaps arose through a wider definition of a catchment area as described under paragraph 40(d);
 - (b) in relation to bus-on-rail overlaps, its definition of the catchment area for identifying overlaps (see paragraph 38) was wider than that employed in previous CMA cases (see paragraph 39). As such, the majority of the overlaps should be captured, provided that the bus and rail stations have their origins and destinations in reasonably central locations. Arriva noted that for overlaps arising under paragraph 40(d), passengers would require access to private transport in order to travel to the alternative station. Given the prevalence of park and ride facilities in the commuter cities served by the Northern Franchise, Arriva noted that private transport exerts a significant competitive constraint on public transport options.
42. For the purpose of its Phase 1 investigation, the CMA's assessment has focussed in the present case on the relevant overlaps identified using the approaches set out under paragraphs 40(a) and 40(b).

Competitive assessment

Horizontal unilateral effects

43. Horizontal unilateral effects may arise when one firm merges with a competitor that previously provided a competitive constraint, allowing the merged firm profitably to raise prices or degrade quality on its own and without needing to coordinate with its rivals.³⁴ Horizontal unilateral effects are more likely when the merger parties are close competitors. The CMA assessed whether it is or may be the case that the Franchise Award has

³³ For example flows to/from Wakefield include Wakefield British Railway Station, Wakefield Westgate and Wakefield Kirkgate.

³⁴ [Merger Assessment Guidelines](#), from paragraph 5.4.1.

resulted, or may be expected to result, in an SLC in relation to unilateral horizontal effects in the provision of public transport services, including bus services and rail services.

Competition for the market

44. Consistent with the CMA's previous decisional practice relating to the assessment of rail franchise awards,³⁵ the CMA has been mindful of the impact of the Franchise Award on competition for the market (ie competition for rail franchises) in conducting its review. The CMA recognises the benefits of a sufficient number of credible bidders for the DfT's rail franchise award programme which awards franchises after a competitive tender process.
45. The CMA considers that competition for the market could be affected by the Franchise Award if it could lead to a reduction in the number of bidders available for future bids, or provide the Parties with an incumbency advantage relative to other bidders in future bids for franchises.
46. Arriva submitted that the award of the Northern Franchise will have no impact on competition for the award of future franchises. More specifically, Arriva submitted that:
 - (a) the award of the Northern Franchise to Arriva would not reduce the number of bidders for future franchises;
 - (b) Arriva would not obtain incumbency advantages for future franchises³⁶ through the acquisition of the Northern Franchise; and
 - (c) the combined share of franchises and the increment obtained through the Northern Franchise are not significant. Arriva estimates that the Franchise Award increases its share of UK rail franchises to no more than 25%, with an increment of less than 10%.³⁷
47. No third parties raised concerns about the impact of the Franchise Award on competition for the market.

³⁵ See, for example, ME/6473/14 National Express Group/Essex Thameside Franchise, CMA (2014), paragraph 25; ME/6470/14 Govia Thameslink Railway Limited/Thameslink, Southern and Great Northern Rail Franchise, CMA (2014), paragraph 35; ME/6506/14 Intercity Railways Limited/ICEC Franchise, CMA (2014), paragraph 46.

³⁶ Arriva submitted that franchise processes are arranged so as to eliminate incumbency advantages. For example after the award of a franchise, the new franchisee would take over most of the staff and many of the assets to allow the operation of the franchise.

³⁷ This is based on (i) combined share of franchise revenues of around 12.2% (increment of around 4%); (ii) combined share of franchise track miles (based on 100% timetable operation) of around 22.4% (increment of around 8%); and (iii) combined share of number of franchise licences around 22.5% (increment of around 5%).

48. Given the above, the CMA therefore considers that there is no realistic prospect of an SLC for rail franchises as a result of the Franchise Award.

Competition in the market

Theories of harm

49. In relation to competition in the market, the CMA has considered whether the Franchise Award could result in unilateral horizontal effects on:
- (a) overlapping Arriva bus services and the Northern Franchise rail services (**bus-on-rail overlaps**); and
 - (b) overlapping Arriva rail services (XC, ATW, GC and DBTW) and the Northern Franchise rail services (**rail-on-rail overlaps**).
50. For completeness, the CMA notes that the Parties' individual services may interact in the form of transport network tickets offered by Arriva and the Northern Franchise. For the purpose of its Phase 1 investigation, the CMA's assessment has focussed in the present case on the individual bus-on-rail and rail-on-rail overlaps between the Parties. The two theories of harm relating to bus-on-rail and rail-on-rail are therefore considered in detail below.

Bus-on-rail overlaps

51. Arriva currently operates local bus services around the UK, some of which overlap with the Northern Franchise (in line with the geographic scope set out in paragraph 38 above).
52. The CMA considered whether the Franchise Award could provide Arriva with the incentive and ability to worsen its offering to passengers on overlapping services. Therefore, the CMA has considered whether the Franchise Award could lead to an increase in fares and/or a reduction in other aspects of its offering (including impact on journey time, frequency of service and service quality) on either Arriva's local bus services (since customers lost as a result could switch to the Northern Franchise) and/or on the Northern Franchise service (as lost customers could switch to Arriva's local bus services).³⁸
53. The CMA has focused its assessment on whether there is a realistic prospect that the Parties could profitably weaken local bus services following the

³⁸ The Parties may have the incentive and ability to increase fares or withdraw dedicated fares and/or degrade quality/service levels in order to encourage switching from one mode to the other, taking into account the closeness of competition between the Parties' services, the constraint provided by other operators, the effects on other connected flows, and regulatory constraints.

Franchise Award, through an increase in fares and/or a reduction in other aspects of its offering. This is because local bus services are not subject to the same degree of regulation as rail services and therefore there is a greater degree of flexibility for the operator. Arriva would therefore benefit from higher fares or lower costs on affected buses to the extent that passengers continue to use the Arriva bus service, and would also recapture some passengers who switch to using Northern Franchise services.

54. The CMA has seen evidence suggesting that some details of the competition between Arriva bus services and the Northern Franchise were likely to change because of planned changes in service offerings. More specifically, the CMA notes that:

(a) there were planned changes to Arriva's existing local bus services pre-Franchise Award, through the introduction of additional premium bus services (Max and Sapphire) on existing routes.³⁹ The Arriva Max and Sapphire range provide premium services, including fast and frequent travel between major conurbations in the areas that the Northern Franchise operates in; and

(b) the Franchise agreement includes provisions for re-mapping of services and other changes to the Northern Franchise services.⁴⁰ Some of the planned changes under the Franchise Agreement involve increasing service frequencies, extending the rail route and other changes to the Northern Franchise.

55. For completeness, the CMA notes that the Franchise Award may impact on planned changes to Arriva bus and Northern Franchise rail services and these planned changes may impact on competition between the Parties' services. For the purpose of its Phase 1 investigation, the CMA's assessment has focussed in the present case on the existing overlaps between Arriva bus services and Northern Franchise rail services.

Submissions by Arriva

56. Arriva submitted that it does not have the ability or incentive to raise prices or degrade services on its bus services. In relation to ability, Arriva generally has the ability to flex its bus timetables but these timetable changes must be

³⁹ See for example planned introductions of additional Max routes: <https://www.arrivabus.co.uk/about-us/max--new-inter-urban-express-services-from-arriva/>

⁴⁰ As from January 2018, Trans-Penine Express will take over some of the services currently provided under the Northern franchise. Certain services and stations within the current TPE franchise will also be remapped into the new Northern franchise immediately prior to the commencement of the new TPE Franchise. These service reconfigurations have not been taken into account in the filtering analysis described above.

notified with a 56 day public notice period. Arriva told the CMA that it would have no incentive to reduce frequency of bus routes overlapping with Northern Franchise rail services as this would drive customers to take alternative transport options (ie competing bus operators, trains, cars and taxis) and Arriva would only capture a proportion of these on its overlapping rail service. Also, Arriva submitted that there is a profit share mechanism which requires ARN to pay the Secretary of State for Transport a proportion of the profits on the Northern Franchise above certain thresholds.⁴¹

57. The CMA considers that the methodology detailed below takes into account constraints from third-party competitors (both through the filtering methodology and the detailed assessment) and, in principle, even a small diversion to rail could render a price increase or reduction in service quality profitable.⁴² The CMA notes that Arriva has not submitted specific evidence on the impact that the profit-share mechanism has on its incentives to divert bus passengers onto overlapping Northern Franchise rail services.

Filtering approach

58. Arriva identified 1,041 flows (150 routes) where existing Arriva bus services and Northern Franchise rail services overlap using the methodology set out in paragraph 42 above.⁴³ Arriva submitted that the use of filters would be very useful in this case as a tool to narrow down the number of overlaps to be assessed, and that flow-by-flow analysis should be required only for flows which remain after application of the filters.
59. In relation to bus-on-rail overlaps, the filters which the CMA has applied are summarised below:
- (a) **Relative importance of overlapping flows filter (10% filter):** The CMA and its predecessor bodies have previously used the relative importance of overlapping flows as a filtering approach for identifying the most significant overlapping flows, and have previously excluded from further analysis those bus-on-rail overlapping flows where the revenue derived

⁴¹ Final Merger Notice, pages 49 and 50.

⁴² For example because reducing frequency would be profit-neutral absent the Franchise Award, or because the incremental profit on diverted rail passengers is significant in comparison to bus services. This could be the case for diversion between bus services and rail services, since the latter typically has proportionately lower variable costs, such that additional revenues from diverted passengers would not result in significant additional costs.

⁴³ Arriva submitted that overlap flow information for its North-West and Yorkshire divisions is provided separately for each direction of travel (that is travel between A – B is considered separately from B – A). For its North-East bus division, overlap flow information is combined into a single bi-directional entry. The CMA considers that the latter approach is more appropriate as it removes the risk of double-counting flows or reducing the apparent scale of the overlap. However, Arriva adjusted the flow information, prior to the filters, such that the approach is consistent with bi-directional flow analysis.

from the bus service on those flows (or number of passengers) combined accounts for less than 10% of the overall bus route revenue (or passengers on the route).⁴⁴ The CMA considers this approach to be appropriate in this case.

A total of 545 flows (95 routes) were filtered out by applying the 10% filter, since overlap flow revenues on these services account for less than 10% of total route revenues. A further 469 flows (55 routes) remain after application of the 10% filter because overlapping flows account for at least 10% of total route revenues. This indicates that overlaps between these bus services and the Northern Franchise rail services which remain after application of the filter are non-trivial and therefore cannot be excluded from further analysis on the basis of overlapping revenues alone.

- (b) Effective competitor filter: The CMA and its predecessor bodies have previously taken into account the presence of competition to filter out flows from further analysis.⁴⁵ In this case, the CMA believes that overlapping flows where there is effective competition from a third-party competitor service, typically defined as a service offering at least half the frequency of the overlapping Arriva bus service and on the same mode of transport, would not raise competition concerns.⁴⁶ A total of 110 additional flows (8 routes) were filtered out by applying the effective competitor filter.
- (c) De minimis filter: The CMA and its predecessor bodies have also previously applied a de minimis filter which excludes overlapping flows where annual revenues are low. In this case, the CMA considers that, where revenues generated by the relevant flow are sufficiently low, Arriva would not have a requisite incentive to divert passengers onto the overlapping rail service (given the costs of planning and implementing such a change).

60. In relation to the de minimis filter, Arriva submitted that the CC had in previous cases involving bus-on-rail overlaps, excluded flows from detailed analysis where they accounted for less than £10,000 in annual revenues.⁴⁷ The CMA does not consider that a de minimis filter of £10,000 is appropriately cautious in the present case. This is because a de minimis filter set at this level could exclude routes where there are a number of flows each with revenues below

⁴⁴ See CC Local bus services market investigation, 2011, Appendix 11.2; ME/6229/13, Stagecoach/East Midlands rail franchise; paragraph 28 and ME/6229/13, First/Finglands, OFT (2014), paragraph 46.

⁴⁵ See CC [Review of methodologies in transport inquiries](#), May 2007, paragraph 26.

⁴⁶ The CMA tested whether the results were sensitive to segmentation according to service frequency during weekdays, Saturday and Sunday. This did not have an impact on the flow filtering in this case.

⁴⁷ See for example [CC report on the acquisition by FirstGroup plc of the Greater Western Passenger Rail franchise](#), paragraph 5.40.

£10,000, but where the combined revenues of these flows and the potential for harm to passenger interests could be significant.⁴⁸ In such cases, the CMA notes that further consideration of the effect of the Franchise Award on competition may be appropriate.

61. The CMA has, however, focused its analysis on routes where there is at least one overlap flow with annual revenues of at least £5,000. The application of such a filter is appropriate in the present case, since it does not exclude from further analysis any routes where the combined revenues of flows on a route and/or the incentives to degrade services are significant and as such could raise *prima facie* competition concerns.
62. Following application of these three filters, 45 routes (183 bus-on-rail flows) remained for detailed analysis and for which the CMA could not dismiss competition concerns on the basis of filtering. The CMA also considers it appropriate that, for routes with at least one flow remaining after the application of the proposed filters, its detailed assessment considers all overlap flows (that is overlap flows which could be excluded by one of the filters above are also considered as part of the route-level assessment), since those flows could be affected by route-level changes.

Further filters considered

63. Arriva submitted that a further filter should be applied, which identified significant asymmetries in passenger use of overlapping bus and rail services. Arriva submitted that such a filter had been used in a previous CC case and this filter circumvented the need to consider significant differences in particular features of the service. Arriva submitted that, instead, where there appear to be strong preferences for one of the services, measured by the share of revenues accruing to that service, then passengers can be assumed to have a strong preference for that service. As a result, Arriva submitted, competition between the two services is likely to be limited.⁴⁹
64. The CMA has some reservations as regards the application of this proposed filter in the present case:
 - (a) Asymmetry of revenues between transport modes may arise as a result of competitive interaction between rail and bus services, rather than an indicator of passenger preferences. For example, where bus services have a significant share of revenues, this may be because the bus

⁴⁸ By way of example, the largest route that is excluded by using a £10,000 de minimis threshold (but not under the £1,000 or £5,000 de minimis thresholds) has total route revenues of around £695,000.

⁴⁹ Arriva note of 14 March 2016

operator has lowered fares or reduced journey times, in order to compete with the overlapping rail service. Excluding such flows from the analysis may not be appropriate, since the common ownership of the two modes may provide incentives to increase fares or increase journey times (by for example altering the route of the bus service) where some passengers may consider the two to be close alternatives. Therefore, it is not clear that such an asymmetry, alone, would be sufficient to rule out the realistic prospect of an SLC.

- (b) Filtering on this basis would be most useful in cases where the asymmetries (indicated by significant differences in mode share of flow revenues) are similar across the whole overlapping segment of the route, ie the filter excludes multiple flows and possibly the route from the analysis because the two modes are not close alternatives across the route. If this is not the case, flows remain for further analysis. The filter proposed by Arriva would not have a significant impact on the number of routes to be assessed in detail.
- (c) Related to point (b) above, many aspects of the service offer to passengers are set at the level of the bus route (or restricted by other parts of the service), excluding some flows on a route from the analysis with others remaining does not exclude the possibility of competition concerns across the route.
- (d) The de minimis filter described in paragraph 61 above would already exclude flows where the bus service is a weak alternative and generates relatively small revenues (below £5,000).

65. Given the above, the CMA concluded it would not be appropriate to apply the asymmetry filter proposed by Arriva. The CMA has however considered the extent to which overlapping Northern Franchise and Arriva bus services are good alternatives across a number of factors (for example fares, frequency, journey times) as part of its detailed route level analysis.

66. The CMA has set out below the framework for the flow-by-flow assessment.

Framework for flow-by-flow assessment of bus-on-rail overlaps

67. For its detailed flow-by-flow assessment, the CMA has considered the following factors:

- (a) the extent to which the services are important alternatives from the passenger perspective and whether they compete closely. This could be for example because they provide travel to the same destinations and are

similar in terms of their offer (such as fares, frequencies and/or journey times);

- (b) whether the removal of the constraint could significantly affect the incentive to maintain services. This could for example be because the overlapping services are particularly close alternatives and would be expected to have competed particularly strongly and/or because there is limited third-party competition;
- (c) other evidence available to the CMA, such as internal documents on closeness of competition, third-party submissions or other analysis; and
- (d) submissions made by Arriva on mitigating factors such as barriers to entry or potential competition.

68. Arriva submitted the following information in relation to bus-on-rail overlaps:

- (a) Arriva submitted information that allowed the CMA to apply the filters described above for the 1,041 flows (150 routes) where existing Arriva bus services and Northern Franchise rail services overlap.⁵⁰ Following application of the filters described above, 45 routes (183 flows) remained for which the CMA could not dismiss competition concerns.
- (b) Of these routes, Arriva initially submitted detailed data⁵¹ for a subset of 14 routes on the basis that these overlaps were *prima facie* more likely to raise competition concerns.⁵² For these 14 routes, the CMA undertook a detailed flow-by-flow assessment using the methodology set out in paragraph 67 above.
- (c) For the remaining 31 routes for which Arriva submitted detailed data at a later date⁵³; in the 45 working day statutory timetable for its investigation, the CMA was unable to undertake a detailed flow-by-flow assessment, but looked at the features of these routes to determine whether they raised *prima facie* competition concerns (see paragraph 76 below).

69. The detailed flow-by-flow assessment of whether the Franchise Award could result in an SLC for the flows (and routes) covered by Paragraph 68(a) is set out in Annex 1.

⁵⁰ Data submission of 5 April 2016.

⁵¹ Data submission of 4 February 2016.

⁵² The subset of the most significant overlapping flows for a detailed competitive assessment were identified on the basis that these were (a) routes/bus services where revenues on overlapping flows were the largest; (b) overlapping flows where there are limited or no third party competitors to act as a constraint; and (c) bus services selected in each of Arriva's geographic areas of operation.

⁵³ Data submission of 5 April 2016.

Internal documents

70. The CMA considers that, where available, documents produced by the Parties and third parties in the ordinary course of business provide important insights on the level of competition on overlap flows or services. The CMA has considered the views of the Parties in relation to competitive conditions in the areas in which they operate and the extent to which the Parties view each other as close competitors based on their internal documents.
71. The internal documents showed that competitive conditions varied between bus routes and even between flows on the same route. This implies that a detailed assessment considering the effect of the Franchise Award on individual flows or services is appropriate for flows which remain after the application of the filters. The internal documents submitted by Arriva have been taken into account in the detailed assessment in Annex 1.

Views of third parties

72. Some third parties raised concerns that the Franchise Award could reduce competition in some geographic areas where Arriva and the Northern Franchise compete. Third party concerns were strongest in relation to overlaps where the Parties' services were the only two providing services on that flow.⁵⁴ The CMA sought the views of relevant local authorities. Four of these local authorities⁵⁵ had no comments on the Franchise Award and another local authority⁵⁶ had no concerns in relation to any impacts on competition from the Franchise Award.
73. The CMA also received representations from third parties stating that the Franchise Award may adversely impact upon other bus companies due to commitments within the rail franchise. For example, on certain flows, the train frequency (or other competitive parameters) would be increased under the franchise agreement, such that it erodes the ability of third-party competitors to compete with the overlapping Arriva and Northern Franchise services. The CMA has considered these concerns in paragraphs 53- 55 above.

⁵⁴ For example, the X10 bus service to Newcastle and the X66 bus service to Darlington.

⁵⁵ Transport for Greater Manchester, West Yorkshire Combined Authority, Lincolnshire County Council and [REDACTED].

⁵⁶ [REDACTED]

Conclusion on horizontal unilateral effects

74. For the reasons set out in detail in Annex 1, the CMA found that the Franchise Award gives rise to a realistic prospect of an SLC in relation to the following routes⁵⁷:

- (a) Halewood – Liverpool (Service 79)
- (b) Hall Green – Leeds (Service 110)
- (c) Selby – York (Service 415/416)
- (d) Middlesbrough – Redcar (Service 63)
- (e) Middlesbrough – New Marske (Service 64)
- (f) Middlesbrough – North Skelton (Service X3)
- (g) Middlesbrough – Whitby (Service X4)
- (h) Newcastle Upon Tyne – Blyth (Service X10)
- (i) Newcastle Upon Tyne – Blyth (Service X11)
- (j) Berwick – Newcastle (Service X15)
- (k) Berwick – Newcastle (Service X18)
- (l) Darlington – Durham (Service 7)
- (m) Middlesbrough – Faverdale (Service X66)

75. Across these routes, a detailed flow-by-flow assessment confirmed the *prima facie* competition concerns identified, noting in particular:

- (a) the high revenues generated from the provision of both bus and rail services on these routes;
- (b) the fact that the bus services overlap with the Northern Franchise for a significant part of the bus route;
- (c) the minimal and/or weak competition from third party operators on these routes; and/or

⁵⁷ For the reasons set out in Annex 1, the CMA believes that the Franchise Award does not give rise to the realistic prospect of an SLC in relation to the bus-on-rail overlap on the Huyton – Liverpool route (Service 6) in Liverpool.

(d) the similarity between the overall offer on the overlapping services, such that passengers are likely to consider the two modes as substitutable and as such exert competitive constraint on each other.

76. With regard to bus-on-rail overlaps on the additional 31 routes described in paragraph 68(c), as listed in Annex 2 and for which the CMA was only provided data later in its Phase 1 investigation, the CMA was unable to undertake a detailed flow-by-flow assessment in the time available. In the light of the filtering methodology adopted in this case, the CMA cannot rule out that the Franchise Award gives rise to a realistic prospect of an SLC for these routes for the reasons set out below:

(a) the share of bus route revenues arising from overlap flows on these routes is significant and ranges from around 10% to around 43%. As such, the Parties may have the incentive and ability to increase fares and/or reduce other aspects of its offering following the Franchise Award. As part of its detailed flow-by-flow assessment for 14 routes, the CMA has found that the Franchise Award raised a realistic prospect of an SLC in relation to a bus route where overlap revenues account for around 14% of total route revenues and, as such, the CMA considers that competition issues cannot be ruled out in relation to the 31 routes where the share of bus route revenues is similar or higher;

(b) the total overlap revenues from the flows which remain, after applying the filtering methodology, still account for a significant proportion of the revenue on these routes (accounting for up to around 40% of route revenues). Given that the CMA has already applied the effective competitor filter (ie flows that are the subject of effective competition from third parties have already been excluded), the CMA considers that competition issues cannot be ruled out in relation to the 31 routes; and

(c) annual revenues on these routes are significant, with the average route revenue across these 31 routes at around £800,000. The CMA considers that, on this basis, the Parties may have the incentive to increase fares and/or reduce other aspects of their offering following the Franchise Award.

Barriers to entry and expansion

77. Entry, or expansion of existing firms, can mitigate the initial effect of a merger on competition, and in some cases may mean that there is no SLC. In assessing whether entry or expansion might prevent an SLC, the CMA

considers whether such entry or expansion would be timely, likely and sufficient.⁵⁸

78. Arriva has submitted that there are a number of third-party competitors who could enter or expand in the overlapping routes. This could be because a third-party provider has a network hub located near the overlapping flows or that it operates routes near such flows. It submitted that barriers to entry are low for providing a bus service on a specific flow once an operator has in place an operator's licence, vehicles and the logistics, such as a depot or more limited form of operating base, to serve the relevant area. It submitted that for all the flows analysed, there are mature rival operators operating routes nearby which could be expected to have few practical difficulties in modifying an existing route or establishing a new route in order to take advantage of an opportunity created by an uncompetitive offering by Arriva on a certain flow. Arriva also told the CMA that it did not monitor the offering of third-party operators in areas where it did not already have a presence.⁵⁹
79. The CMA has considered the submissions made by Arriva on entry or expansion in the detailed assessment sections. Setting aside the assessment of actual barriers to entry (eg sunk costs), the CMA notes that, in a market characterised by low barriers to entry and/or expansion, entrants may nevertheless be discouraged from entry by the small size of the market, or the credible threat of retaliation by incumbents (whether in the same market as the merged firm or another where that new entrant is already present). For example in *Arriva/Centrebus*,⁶⁰ the CMA concluded that barriers to entry could be significant, particularly for new entrants and these included expected responses from the incumbent operator. This was particularly important when set against evidence of aggressive scheduling by the incumbent operator.
80. In assessing the likelihood of post-merger entry or expansion, the CMA considers whether entry or expansion is likely to take place if the entrant expects post-entry prices to be at pre-merger levels. This is because, if prices were to rise post-merger, only an entrant (or an incumbent) who would find it profitable to operate (or add capacity) in the market at pre-merger prices is likely to enter (or expand) and return prices to pre-merger levels.
81. The CMA asked third parties to explain the factors (including a fare increase or frequency reduction) which would make a bus operator likely to enter a route. The CMA also asked third parties about plans for entry in relation to the

⁵⁸ [Merger Assessment Guidelines](#), from paragraph 5.8.1.

⁵⁹ Issues Meeting of 12 April 2016.

⁶⁰ ME/6226-13: Completed acquisition by Arriva Passenger Services Limited of the remainder of the entire share capital of Centrebus Holdings Limited, paragraph 105.

overlap routes between Arriva and the Northern Franchise and in relation to the 14 routes identified in paragraph 68(b). No third parties provided any evidence of planned entry on these 14 routes.

82. Third-parties generally confirmed that the expected response of the incumbent operator is an important consideration to entry decisions. For example, one bus operator told the CMA that [redacted].
83. Another bus operator noted that a fare increase would have no bearing on their decision to enter; however, a reduction in frequency would merit consideration of the opportunities this would create. In particular, it would consider whether this would affect them on other existing routes through the operator increasing its presence or reducing its fare structure. This suggests that entry is more likely for significant changes to the current service offering.
84. Another bus operator noted that in general, for routes that are closer to the bus operators' existing network, the increase in fares or the reduction in frequency required for them to actively consider entering a route will be lower. This reflects the fact that such routes would be, in principal at least, less costly to serve.
85. Taking into account the above, the CMA considers that evidence on the constraint from entry or expansion must be specific to the routes under consideration. Therefore the CMA currently believes that it has not received sufficient evidence to conclude that entry or expansion could prevent a realistic prospect of an SLC on the bus routes where there are competition concerns.

Rail-on-rail overlaps

86. As noted in paragraph 13 above, Arriva currently operates three rail franchises, two concession agreements and two open access rail services. The CMA and its predecessor bodies have noted that unilateral horizontal effects could arise from the common ownership of transport services giving rise to overlapping flows or services. These unilateral horizontal effects arise where this common ownership provides the ability and incentive to raise fares and/or reconfigure services post-Franchise Award (for example reducing frequencies). In relation to rail-on-rail overlaps, the CMA and its predecessor bodies have found that whilst limited, there is some scope for price competition between rail services, particularly in relation to unregulated fares.⁶¹

⁶¹ CC [Review of methodologies in transport inquiries](#), May 2007, paragraphs 52 – 54.

87. The CMA has considered whether the Franchise Award could lead to an increase in fares and/or a reduction in other aspects of its offering (including, for example, an impact on journey time and frequency of service) on the Northern Franchise or any of Arriva's other rail services as listed in paragraph 13 above. This could be because the overlapping Arriva and Northern Franchise services may be important competitive constraints on each other and the removal of this constraint may lead to increases in fares or reductions in other aspects of its offering. The competitive constraint could exist because a significant proportion of passengers of one of the services would have switched to the competing service in the event of a worsening of the offer (eg in terms of fares or service quality). For example, if inter-available fares⁶² and dedicated fares⁶³ come under the control of the same operator, there may be an incentive to either increase or withdraw the dedicated fares. In each case, the CMA has considered the extent to which the Parties may have the incentive and ability to increase fares or invest less in service quality.

Submissions by Arriva

88. Arriva submitted that it does not have the ability or incentive to raise fares or degrade services in relation to rail services.⁶⁴ Arriva told the CMA that its ability to alter the parameters of the offer to passengers of the Northern Franchise is limited due to contractual restrictions which cover, for example price, journey time, timetable and other aspects of service quality. While the price of some off-peak services can be altered, this is only for either dedicated fares or inter-available fares where Arriva is the lead operator on the route (normally the operator who has the greatest commercial interest on a certain route).⁶⁵ Arriva also submitted that the Northern Franchise agreement places significant constraints on Arriva's ability to alter the quality (for example, the frequency of services and number of carriages) or pricing of the services it offers.

⁶² Inter-available fares can be used between a certain origin and destination on any permitted route across multiple operator services. Inter-available fares are set by the lead operator (typically the operator who has the greatest commercial interest on a certain route) and must be observed by all train operating companies selling tickets for that journey or operating a service on (some or all of) the route.

⁶³ Dedicated fares refer to fares set by each train operating company independently which are only valid on that operator's service.

⁶⁴ Final Merger Notice, pages 30 and 31.

⁶⁵ A designated lead operator on each flow sets at least one inter-available fare which must be honoured by all operators serving all or part of that flow. See section 4.20 of the [Ticketing and Settlement Agreement](#).

89. Arriva suggested that service specifications in the franchise agreements as well as the ORCATS⁶⁶ allocation mechanism and profit sharing mechanisms would restrict fare rises on the rail-on-rail overlap flows.
90. The CMA accepts that the contractual obligations under the relevant franchise agreements (and in particular, the Franchise Agreement) may limit the ability or incentive of Arriva to alter non-price aspects of its offering on rail services. However, the CMA has not received sufficient evidence to allow it to conclude that the contractual obligations completely rule out the possibility of degradation in non-price aspects following the Franchise Award. For example, the Franchise Award may reduce the incentives for Arriva to exceed the levels specified in the Franchise Agreement, or to meet on individual routes, for which levels are specified as an average across the network.
91. Furthermore, the CMA notes that open access operators such as Grand Central have greater commercial freedom to set fares and non-price aspects of its offer to passengers. The award of the Northern Franchise may, therefore, significantly affect competitive constraints on these other overlapping services, irrespective of the constraints on Arriva's ability to alter prices or fares on the Northern Franchise. Therefore, the CMA considers that increased fares and/or reductions in non-price aspects are possible as a result of a significant reduction in competition on overlapping flows.
92. The CMA has also received insufficient evidence to suggest that risk/profit sharing with the government in respect of the Northern Franchise overall will reduce the incentive to increase profits on any of the rail-on-rail flows or in the aggregate (ie whether they apply at current profit levels). Arriva accepts that even with the contractual obligations there is still scope to increase prices.⁶⁷

Filtering approach

93. Arriva submitted that there are overlaps between the Northern Franchise rail services and some of the services of the XC, ATW, GC and DBTW. In total, 167⁶⁸ overlapping flows between the Northern Franchise and Arriva were identified.
94. Arriva also submitted that rail-on-rail overlaps with the Tyne & Wear Metro should be excluded from further analysis, since the DBTW concession

⁶⁶ ORCATS (Operational Research Computerised Allocation of Tickets to Services), is used for real time reservation and revenue sharing on inter-available tickets between TOCs. It is used to divide ticket revenue when a ticket or journey involves trains operated by multiple TOCs.

⁶⁷ Point 4.1.4 of the submission on rail-on rail overlaps to the CMA of 18 March 2016.

⁶⁸ This is after 14 duplicates had been removed that had been considered overlaps between both the Manchester British Rail code and Manchester Piccadilly station that is contained within that code.

agreement gives Arriva no flexibility to alter fares or non-price aspects and all fare revenues are for the account of Nexus (which owns and manages the DBTW concession agreement) only; as such, there is no incentive to increase passenger numbers (or degrade the overlapping Northern Franchise rail service). The CMA agrees with this assessment and it has therefore excluded overlaps between the Northern Franchise and the Tyne & Wear Metro from further analysis.

95. Arriva told the CMA that, when assessing the effects of the Franchise Award, the CMA should take into account the fact that a number of franchises Arriva currently operates are due to expire in the near future, specifically:
- (a) XC – Arriva’s operation of this service is due to expire in October 2016, although discussions are underway to extend the franchise to November 2019;
 - (b) DBTW – Arriva’s operation of this service is due to expire in March 2017, although this is extendable by Nexus to March 2019; and
 - (c) ATW – Arriva’s operation of this service is due to expire in October 2018.
96. In relation to XC and DBTW, the CMA notes that the existing Franchise agreements provide for extensions and Arriva is already in negotiations to extend these contracts. Given the likelihood of the extension and the significant period of extension, the CMA considers that it is likely that Arriva will operate these Franchises in the short to medium term. Moreover, for ATW, the CMA notes that its operation of these services will continue for a significant period until October 2018. The CMA has therefore not excluded from its analysis flows relating to Franchise Agreements that may expire in the future.
97. In relation to rail-on-rail overlaps, the filters which the CMA has applied are summarised below:
- (a) De minimis filter: The CMA has not considered in detail any overlapping flows where the Parties’ overlapping services have combined annual revenue below £5,000. These flows are considered to be of insufficient importance such that they would not give rise to the realistic prospect of an SLC. 52 overlapping flows generated less than £5,000 for the Parties’ services and have been filtered out on this basis.
 - (b) Effective competitor filter: the CMA and its predecessor bodies have previously used effective competition as a filter for identifying flows for

further analysis.⁶⁹ Overlapping flows where there is effective competition from a significant third-party competitor service were considered not to give rise to competition concerns. Therefore the CMA has filtered out overlapping flows where the Parties account for less than 40% of the flow revenue.⁷⁰ 20 overlapping flows are considered to have an effective competitor and have been filtered out from further analysis on this basis.

- (c) Flows between York and the Tyne and Wear area: The CMA has not considered in detail flows between York and the Tyne and Wear area because the CMA considers that using a Northern Franchise rail service would not be practicable on these flows. This is because the Northern Franchise rail service is unlikely to be a good alternative to the direct Cross-Country services as it would involve a significant diversion via the West Coast and Carlisle or involve interchanging to third party operators such as Virgin Trains East Coast. 7 overlapping flows have been filtered out from further analysis on this basis.
- (d) Revenue increment filter: If the Franchise Award leads to a relatively small revenue increment on a flow, the CMA considers that it would not lead to the realistic prospect of an SLC, since there would not be the realistic prospect that the Franchise Award would materially alter the incentives to maintain fares or non-price aspects on these flows. The CMA filtered overlapping flows where the Parties (together) account for less than 60% of the flow revenue and the increment as a result of the Franchise Award is less than 5%. The CMA also filtered out all flows where the increment as a result of the Franchise Award is less than 3% irrespective of their total combined share. In total, 35 overlapping flows have been filtered out on this basis.

98. Following application of these four filters, 54 flows⁷¹ remained for detailed analysis and for which the CMA could not dismiss competition concerns on the basis of filtering.

⁶⁹ See CC *Review of methodologies in transport inquiries*, May 2007, paragraph 26.

⁷⁰ Given that, as noted in paragraph 5, the CMA considers competition between transport options of the same transport mode to be more significant than inter-modal competition, the CMA considers it appropriate to adopt a more cautious threshold for rail-on-rail overlaps (ie. require third-parties to have a higher share of flow revenues) than in relation to bus-on-rail overlaps.

⁷¹ The Parties identified one additional flow (Warrington to Manchester) that would be filtered out on the basis of the Northern Franchise rail services in 2015 but would not be filtered out once planned timetable changes have been taken into account.

Further filters considered

99. Arriva also submitted that some rail-on-rail flows could be further filtered out on the following bases:⁷²
- (a) Regulated fares: A large proportion of ticket sales are price-regulated tickets (regulated fares⁷³) and, for the majority of customers on these services, the scope for increased prices as a result of the Franchise Award is limited.
 - (b) Inter-available fares: A high proportion of journeys on some of these services use inter-available fares, which suggests that the extent of price competition pre-Franchise Award between Arriva and Northern (and third party operators in some cases) is either non-existent or at worst, extremely limited. Therefore, Arriva said, the impact of the Franchise Award on ticket prices on these flows is expected to be very limited.
 - (c) Significant competition: There is significant competition on services and passengers on some of these services would switch to alternative modes of transport if prices increased or service quality decreased.
 - (d) No full overlap: There are flows identified as overlaps where there appears to be no complete service, either direct or indirect, on one of the Northern Franchise or Arriva (eg the Northern Franchise rail service runs a service on the entire flow and Arriva runs a service on only part of the flow).
 - (e) Non-rail competitors: There are a number of other alternative modes (non-rail competitors) which passengers could switch to on some of the flows (such as Hartlepool to Sunderland, and Manchester to Manchester Airport).
100. The CMA considers that these arguments are better suited for consideration on a flow-by-flow basis and these are discussed further below.

⁷² Assessment of rail-rail overlaps, Note prepared for the CMA, dated 6 April 2016.

⁷³ The government applies a regulated fares system to restrict the increases permitted on certain fares, the terms of which form part of the franchise agreement with each franchise operator.

Framework for detailed assessment

101. The CMA has considered whether the Franchise Award raises a realistic prospect of an SLC on overlapping rail-on-rail services. In its assessment of rail-on-rail overlaps, the CMA has considered the following factors:⁷⁴
- (a) Revenue share: The CMA has taken into account the share of revenue generated by each of the Parties on the relevant rail flows. If the combined share of revenue of the Parties on any of the rail services is low, this indicates that the incentive to increase fares is also likely to be low given that a large proportion of customers would most likely switch to competing services. Also, if the increment is low, there is a limited change to incentives.
 - (b) Comparability of the Parties' and competitors' services: The CMA has compared the features of the Parties' services with each other and those of competitors present on a flow to assess the extent to which these services may be viewed as close substitutes. To assess the similarity of services, the CMA has considered, where data is available:
 - (i) frequency;
 - (ii) average journey time;
 - (iii) proportion of revenue from tickets that are fare-regulated and the proportion from tickets that are inter-available⁷⁵; and
 - (iv) identity of the lead operator.
 - (c) Views of third parties.
102. Considering each of the arguments made in Paragraph 99 in turn:
- (a) Regulated fares: The CMA considers that having a large proportion of regulated tickets on a given flow does not necessarily rule out competition concerns about individual regulated fares under current regulation.⁷⁶ The

⁷⁴ Certain of these factors have previously been considered in, for example, CC [Review of methodologies in transport inquiries](#), May 2007, paragraph 27. See also ME/6506/14 Intercity Railways Limited/ICEC Franchise, CMA (2014), paragraph 67.

⁷⁵ Inter-available tickets are valid on all operators active on a particular flow or route, whereas dedicated tickets are only valid on the services of a particular operator.

⁷⁶ For example the fare basket approach currently applied to fare regulation in rail allows for changes to individual regulated fares within a basket and the level of permitted increase applies on the overall change in the basket. Therefore changes to individual fares on overlap flows are possible, particularly if these are offset by reductions in non-overlapping flows. Competition concerns could arise if regulated fares on overlapping flows rise faster than fares where there is no change in competitive conditions and are overall within the permitted basket increase. For

CMA is aware that⁷⁷, as part of the current Government's manifesto, franchise regulated fares are expected to be capped at Retail Prices Index (**RPI**) inflation for a period of 5 years from the general election and the ability to flex individual regulated fares has also been removed.⁷⁸ In light of the above, the CMA considers that there appears to be limited scope for competition concerns with respect to regulated fares. The CMA however notes that this restriction on regulated fares will not apply to Grand Central and will not prevent competition on other aspects of its offering and, as such, it would not be appropriate to apply it to overlaps between the Northern Franchise and Grand Central services. The CMA also notes that while regulated fares may impose some constraint on unregulated fares, no evidence has been presented that shows it would be a binding constraint for all unregulated fares, and therefore while regulated fares are a relevant factor, they must be considered with other aspects of the flow.

The CMA therefore considered it appropriate to remove 4 flows which do not give rise to competition concerns on the basis that regulated fares account for 90% or more of fares on these flows.⁷⁹

- (b) Inter-available fares: The CMA has in previous cases used the proportion of inter-available fares as a filter.⁸⁰ Although a large proportion of revenues deriving from inter-available fares may suggest that actual price competition pre-Franchise Award has been limited, it is not clear the extent to which, pre-Franchise Award, the presence of a little-used dedicated fare or risk of a competitive dedicated fare being introduced by a competitor has acted as a deterrent to the lead operator increasing the inter-available fares on a given flow.⁸¹ Therefore, this condition can only be applied confidently where a) one of the Parties is not the lead operator, and b) it appears unlikely that one of the Parties would become the lead operator over the course of the Northern Franchise. This is particularly true where the timetable is also changing and existing/current competition

inter-available tickets, flow revenues are split between the train operators on the flow based on the timetables and profile of demand, irrespective of which train the ticket holder travelled on.

⁷⁷ <http://www.bbc.co.uk/news/election-2015-32245068>

⁷⁸ The DfT confirmed that the planned changes to the Franchise Agreement to effect this policy are being implemented in accordance with the change process in the Franchise Agreement and are not open to negotiation with Arriva. The DfT stated that this policy is also being implemented with all TOCs in the same way (including Arriva Rail North, Cross Country and Arriva Trains Wales). [36]

⁷⁹ These four flows were not on the same route and had a limited impact on the incentive to reduce other aspects of the offering across any of the individual rail routes.

⁸⁰ CC *Review of methodologies in transport inquiries*, May 2007, paragraph 27.

⁸¹ Pre-Franchise Award, the Northern Franchise may have resisted increasing the inter-available fare because they considered that Arriva would introduce a cheaper dedicated fare if they did. The cheaper dedicated fare would reduce the purchases of the inter-available ticket and make the price rise unprofitable.

on a flow cannot be used as a guide to competition. The CMA has concerns that once competition is removed as a result of the Franchise Award, prices could rise to a level that would have previously been prevented by such price competition.

The CMA therefore considered it appropriate to remove 7 flows where inter-available tickets make up more than 95% of revenues⁸² and the Parties are not and are unlikely to become the lead operator (either because Arriva will not be the principal revenue earner on the flow or will have very little incentive⁸³ to try to become the lead operator), and, as such, these flows do not give rise to competition concerns. On a cautious basis, the CMA has not excluded flows:

- (i) where the Parties' internal documents point to them making an application to become lead operator (Leeds to Sheffield flow); and
 - (ii) where Arriva would clearly be the principal revenue earner and may find it profitable to request lead operator status (York – Wakefield and Brighouse – Doncaster).
- (c) Significant competition: The CMA notes that, in a rail case, a competitor may not be able to expand services without applying for additional timetable slots that may be difficult and time consuming to obtain. Moreover, where the ability of each of the operators to expand services is constrained, other factors may need to be considered in conjunction with competition (such as the departure times of the services and the amount of dedicated fares).
- (d) No full overlap: The CMA considers that indirect overlaps may still provide competitive constraints and the assessment of such arguments has to be case-specific (and as such unlikely to be suitable for a filtering approach). Flows where Arriva and Northern Franchise services are clearly complementary (eg. each covering distinct sections of an indirect journey) and are not therefore genuine overlaps, do not give rise to competition concerns.

⁸² In FirstGroup/ICEC (2005), the CC accepted that where more than 90% of revenue on a flow was derived from inter-available tickets, little competition existed for fares (on the basis of a sensitivity analysis on the effect of the 90% threshold in that case).

⁸³ These flows are all of modest size (less than £40,000 in annual revenue) and there is some doubt as to which operator is the principal revenue earner. Given that there are a number of criteria to be taken into account in determining lead operator status (such as consistency of fares with other flows in the area that would normally support the status quo where all flows in an area or of a particular type are allocated to the traditionally best placed TOC then it is not at all clear that Arriva would meet the overall criteria to be lead operator and would benefit relatively little by overturning this.

The CMA therefore considered it appropriate to remove 4 flows which do not give rise to competition concerns on the basis that the Parties did not have a genuine overlap even on an indirect basis, or where any overlap was already considered in other (longer) overlapping flows.⁸⁴ On a cautious basis, the CMA has however not excluded flows:

- (i) where there are low proportions of regulated fares, high flow revenues and the Parties were competing on at least part of the flow (Leeds – Nottingham); and
 - (ii) where there are low proportions of regulated fares and the direct and indirect routes provided by the merging franchises appear to be competing (Chester – Stockport).
- (e) Non-rail competitors: The CMA and its predecessor bodies have generally considered that services are more likely to compete closely with other services of the same mode of transport on a flow than with services of a different mode of transport. Arriva also noted that services in a given mode are likely to be closer competitors. Therefore, non-rail competitors are less likely to constrain the Parties than rail competitors (in relation to rail-on-rail overlaps). The CMA does not consider it has received evidence suggesting it should depart from the approach set out above. The nature and extent of such non-rail competition on these flows has not been demonstrated (in particular in terms of fares, or convenience of the origin and destination, or other evidence that rail travellers consider alternative modes of transport as viable options). Arriva has also suggested that there could be competition from cars without providing any evidence that rail passengers on the flow consider using their cars, have access to cars, or would find using a car convenient (due to factors such as drive time in peak travel periods or parking and fuel costs).

103. In addition, the CMA looked at those flows with the lowest increments to revenue shares (see Paragraph 101(a)), where the Franchise Award was likely to have a limited impact given the remaining level of competition. The CMA considered it appropriate to remove 1 flow where the increment was low compared to the remaining competition on the flow.⁸⁵

104. Taken together, the CMA considered that competition concerns could be ruled out for a further 16 flows, and that 38 flows remained for which the CMA could

⁸⁴ For most of these flows although both rail franchises earned revenue on the same flow this was via providing complementary services on two different sections of the route or was solely due to an overlap on a direct leg of the journey that was considered elsewhere.

⁸⁵ 7 flows with increments of less than 10% were considered; 4 of these had increments of less than 5% including the flow that was excluded which had: the lowest increment, the lowest combined revenue share of any of the 7 flows and limited competition (eg inter-available fares accounted for 100% of fares on the flow).

not dismiss competition concerns on the basis of its filtering methodology or the further considerations above.

105. For these remaining 38 rail-on-rail flows listed in Annex 3, the CMA found that one or more of the following factors are present: (i) high revenues generated from the provision of rail services on these flows (eg average revenue on these 38 flows being around £600,000); (ii) high shares of supply of rail services (ranging from 44% - 100%); (iii) related to the shares of supply, limited or no competition from third parties; and (iv) a significant proportion of revenues arising from fares which the Parties would have the ability to increase (ie some popular tickets are not subject to fare regulation).
106. The CMA notes that amongst the 38 rail-on-rail flows, there are flows where⁸⁶:
- (a) the Parties are the only two train operators (in 13 flows, the Franchise Award results in a combined share of supply by revenue of 100%);
 - (b) the Parties have a combined share of supply of:
 - (i) 90% or greater and an increment of at least 10% (applies to 19 flows);
 - (ii) 95% or greater and an increment of at least 20% (applies to 12 flows);
 - (c) the Parties set prices for a significant proportion of fares, given the low proportion of inter-available and regulated fares. The CMA therefore considers that there is price competition between the Parties on these flows which may be lost as a result of the Franchise Award, in particular where:⁸⁷
 - (i) inter-available fares account for less than 90% of fares (applies to 3 flows) and dedicated fares account for more than 2% of fares (applies to 5 flows); and
 - (ii) regulated fares account for less than 50% of fares (applies to 9 flows);
 - (d) unregulated fares account for more than £500,000 of total revenue (applies to 7 flows).

⁸⁶ Flows described under paragraph 118 do not add up to 38 as more than one factor may apply to a single flow. For example, the 12 flows in paragraph 118(b)(ii) are included in the 19 flows mentioned in paragraph 118(b)(i) and some of these flows also meet the criteria in paragraph 118(a).

⁸⁷ These measures of relative fare competition (in terms of regulated and inter-available fares) have been chosen in this case to illustrate some flows where potential competition concerns appear to be more pronounced and should not be considered as 'safe harbour' thresholds.

Internal documents

107. The CMA has considered the extent to which there is scope for competition on the flows and services which existing Arriva services operate and the competition faced by these, based on internal documents. The internal documents submitted by Arriva generally indicate that the ability and incentive to compete varies on a flow-by-flow basis and that Arriva responds to demand and competitive conditions. For example, ATW notes in a reporting document that it intends to maximise price increases on the [X] corridor⁸⁸ and [X].⁸⁹
108. Internal documents also show that competitor responses may constrain its ability to successfully introduce fare increases and notes the competition from other TOCs. One internal document notes that due to the nature of Grand Central's market position, Arriva must ensure that Grand Central's fares are competitively priced and cheaper than East Coast's equivalent products as an utmost priority.⁹⁰
109. Therefore, the CMA considers that there is scope for competition between rail franchise operators in the area of the Northern Franchise and that this competition may relate to fare levels or the decision to introduce products such as advance purchase tickets. The internal documents reviewed by the CMA suggest that the existing Arriva train companies consider a number of competitors in setting their offers and cannot exclude that Northern Franchise rail services may have provided a competitive constraint on overlapping flows.

Views of third parties

110. Third parties raised concerns regarding the rail-on-rail overlaps resulting from the Franchise Award. In each of Newcastle, Yorkshire, and Manchester regions, third parties commented that Arriva's existing services and the Northern Franchise rail services compete on several flows. These third parties raised concerns that there were few competing alternatives on the flows where they considered that the Parties competed.

Conclusion on horizontal unilateral effects

111. For the reasons set out above, the CMA believes that the Franchise Award gives rise to a realistic prospect of an SLC as a result of horizontal unilateral effects in relation to 38 rail-on-rail flows listed in Annex 3.

⁸⁸ ATW Report Period 12, 2013.

⁸⁹ ATW Report Period 12, 2013.

⁹⁰ GC Report Period 9, 2013.

Barriers to entry and expansion

112. The CMA has not received any evidence to conclude that entry or expansion could prevent a realistic prospect of an SLC on the rail-on-rail flows where there are competition concerns.

Third party views

113. The CMA contacted relevant third parties including the DfT, ORR, competitors and local government authorities/bodies and passenger groups.
114. Third party comments have been taken into account where appropriate in the competitive assessment above.

Conclusion on substantial lessening of competition

115. Based on the evidence set out above:
- (a) the CMA believes that it is or may be the case that the Franchise Award gives rise to a realistic prospect of an SLC as a result of horizontal unilateral effects on bus-on-rail overlaps on 13 routes. For bus-on-rail overlaps on another 31 routes, the CMA cannot exclude that the Franchise Award gives rise to the realistic prospect an SLC; and
 - (b) the CMA believes that it is or may be the case that the Franchise Award gives rise to a realistic prospect of an SLC as a result of horizontal unilateral effects in relation to 38 rail-on-rail flows.

Exceptions to the duty to refer

116. Where the CMA's duty to refer is engaged, the CMA may, pursuant to section 22(2)(a) of the Act, decide not to refer the merger under investigation for a Phase 2 investigation on the basis that the market(s) concerned is/are not of sufficient importance to justify the making of a reference (the ***de minimis* exception**). The CMA has considered below whether it is appropriate to apply the *de minimis* exception to the present case.

Markets of insufficient importance

117. In considering whether to apply the *de minimis* exception, the CMA will consider, in broad terms, whether the costs involved in a reference would be disproportionate to the size of the market(s) concerned, taking into account also the likelihood that harm will arise, the magnitude of competition

potentially lost and the duration of such effects.⁹¹ The CMA will not generally apply the *de minimis* exception where the size of the markets concerned exceeds £10 million.⁹²

118. The Parties submitted that the CMA should consider *de minimis* in this case.
119. The CMA considers that the aggregated annual value in the UK of the market(s) concerned (ie the markets for which the CMA concludes that there is a realistic prospect of an SLC) is in excess of £10 million, specifically:
- (a) total overlap flow revenues of around £8 million on 44 bus routes (total route revenues of around £40 million);⁹³ and
 - (b) total unregulated revenues of around £11.8 million on 38 rail-on-rail flows (total revenues of £22.6 million).
120. Consistent with the CMA's policy not to apply the *de minimis* exception in circumstances where the size of the markets concerned exceeds £10 million, the CMA finds that it would not be appropriate to consider this exception in this case.

Conclusion on the application of the de minimis exception

121. Taking all the above factors into consideration, the CMA believes that the market concerned in this case is of sufficient importance to justify the making of a reference. As such, the CMA believes that it is not appropriate for it to exercise its discretion to apply the *de minimis* exception.

Decision

122. Consequently, the CMA believes that it is or may be the case that the Franchise Award has resulted, or may be expected to result, in a substantial lessening of competition within a market or markets in the United Kingdom.
123. The CMA therefore believes that it is under a duty to refer under section 22(1) of the Act. However, the duty to refer is not exercised⁹⁴ whilst the CMA is considering whether to accept undertakings⁹⁵ instead of making such a

⁹¹ *Mergers: Exceptions to the duty to refer and undertakings in lieu of reference guidance* (OFT1122), December 2010, chapter 2. The *Mergers: Exceptions to the duty to refer and undertakings in lieu of reference guidance* were adopted by the CMA (see *Mergers: Guidance on the CMA's jurisdiction and procedure*, Annex D).

⁹² *Mergers: Exceptions to the duty to refer and undertakings in lieu of reference guidance*, paragraph 2.2.

⁹³ The total revenue figures do not include one route for which information was not provided.

⁹⁴ Section 22(3)(b) of the Act.

⁹⁵ Section 73 of the Act.

reference. Arriva has until 19 May⁹⁶ to offer an undertaking to the CMA.⁹⁷ The CMA will refer the Franchise Award for a phase 2 investigation⁹⁸ if Arriva does not offer an undertaking by this date; if Arriva indicates before this date that it does not wish to offer an undertaking; or if the CMA decides⁹⁹ by 26 May that there are no reasonable grounds for believing that it might accept the undertaking offered by Arriva, or a modified version of it.

Andrea Coscelli
Executive Director, Markets and Mergers
Competition and Markets Authority
12 May 2016

⁹⁶ Section 73A(1) of the Act.

⁹⁷ Section 73(2) of the Act.

⁹⁸ Sections 22(1) and 34ZA(2) of the Act.

⁹⁹ Section 73A(2) of the Act.

Annex 1: Detailed Assessment of 14 routes with bus-on-rail overlaps

Flow-by-flow assessment

124. In relation to the 14 routes discussed below, the CMA considers there to be evidence suggesting that the Parties compete to some extent and has therefore set out below its assessment as to whether the Franchise Award could result in a substantial lessening of competition (**SLC**) on any of these flows.

Yorkshire

Service 110: Hall Green – Leeds

125. The Northern Franchise service overlaps with Arriva's 110 bus service. Arriva's 110 bus service is part of Arriva's Sapphire range of bus services, which offers premium travel (including high-frequency, direct and fast routes) between Leeds and Wakefield and the surrounding conurbations of Wakefield. The overlapping rail stations served by the Northern Franchise rail service are Leeds, Outwood, Wakefield Westgate, Wakefield Kirkgate and Sandal & Agbrigg.
126. Revenue generated by the Arriva 110 bus service amounted to [X] in the last financial year, of which the overlapping flows accounted for around [X]. However, on the basis of total passenger numbers, the overlapping flows account for a larger share of passengers, at over 40%. This indicates that the Arriva 110 bus service and the Northern Franchise rail services overlap geographically and in their passenger base and, as such, are likely to impose a competitive constraint on each other.
127. Journey frequencies are similar between the Parties' services¹⁰⁰ and fares are also similar (eg £3.20 on the bus and £3.50 on the train for adult singles). Journey times are around 50% shorter on the train.
128. There is some third party competition between Leeds to Wakefield from Virgin Trains, which operates an hourly service. According to data submitted by Arriva, Virgin Trains accounts for up to around 50% of revenues on the Leeds to Wakefield flow and as such would likely capture a large share of diverted bus passengers on this flow if Arrive were to degrade its bus service or raise

¹⁰⁰ The Arriva 110 provides up to 6 services per hour, the Northern Franchise provides up to 4 services per hour (Leeds – Wakefield) and XC provides up to 1 hourly service. Post-Franchise Award, Arriva will offer 5 hourly train services on the Leeds – Wakefield flow (2 on the smaller stations) and a further 6 hourly bus services.

bus fares. However, the Northern Franchise and Arriva 110 services overlap on the intermediate flows, which Virgin Trains does not serve. The Northern Franchise rail service and Arriva 110 services are therefore likely to be closer alternatives and compete more closely than the competition between the Arriva 110 and the Virgin East Coast services.

129. Arriva has submitted that it faces potential competition from Stagecoach which operates four Sunday services on the 444 bus service between Leeds to Wakefield (via a different route). It submits that Stagecoach could expand its services on the 444 bus service, which would be in competition with the Arriva 110 bus service, in the event that Arriva degraded its own bus service offering. However, the 444 bus service is predominantly operated by Arriva and, as such, Stagecoach is likely to consider the potential response from Arriva as the main operator on this route when making decisions on expansion. The CMA has not been presented with evidence to suggest that expansion is a significant competitive constraint on this route such that it would mitigate the potential for service degradation.
130. On the shorter flows (eg Wakefield –Sandal & Agbrigg), Arriva submits that it faces competition from other operators (Frank Poppleton, Globe Holidays and Stagecoach). However, these overlap flows account for a small share of route revenues and, as such, are unlikely to impose a significant constraint on Arriva 110 bus service.
131. One third party operator submitted that the Arriva's high frequency bus and the Northern Franchise rail service compete particularly on the basis of the comparable fares.
132. The CMA considers that Arriva 110 bus service and the overlapping Northern Franchise services are likely to be significant competing services since (i) the overlap accounts for a significant proportion of the Arriva 110 bus service; (ii) the bus and rail services offer similar frequencies and fares; (iii) third-party competition appears limited; and (iv) passengers may trade-off the convenience of the stopping services offering greater accessibility and the faster rail services.
133. Given the above, the CMA believes that there is a realistic prospect that the Franchise Award will result in an SLC on this overlap.

Service 415/416: Selby – York

134. The Northern Franchise overlaps with Arriva's 415/416 bus service. Arriva's bus service 415/416 is part of the Arriva MAX range (which offers fast connections between conurbations) serving York – Riccall – Selby. The

relevant Northern Franchise service is the York – Selby – Hull train, which offers hourly services which typically only stop at York and Selby, before travelling onto Hull. The Parties therefore overlap on the York to Selby flow which are the origin/destination points for the 415/416 buses which serve a more direct route (geographically). There is also an indirect Northern Franchise rail service (hourly via Micklefield).

135. Revenue generated by the Arriva 415/416 bus service amounted to [X] in the last financial year, of which the overlapping flows accounted for around [X]. However around 60% of passengers are boarding services at York and Selby, suggesting that the flow accounts for a large share of the route and that the Parties' calculations may underestimate the extent of the overlap.¹⁰¹
136. The Arriva 415/416 bus service offers more frequent services than the Northern Franchise rail service (4 against one service per hour on Northern) and fares are 50% cheaper on the Arriva bus services. However, journey times are significantly shorter on the rail service (by more than twice the time). Therefore passengers may trade off the longer journey times on the bus, against the lower fares and higher frequencies on the bus, such that the overlapping services are good alternatives to each other.
137. Third-party competition on the overlap flows is limited. Trans-Pennine Express (TPE) provides an hourly indirect service between York and Selby via Leeds. The CMA notes that the Northern Franchise rail service has a 98% share of total rail revenues on the route, suggesting that the indirect TPE services are not a significant constraint on the Arriva and Northern Franchise services and would be unlikely to capture a significant share of diversion in the event of Arriva degrading its offer on the 415/416. Utopia Coaches service 42-0 provides services every 2 hours between York and Selby and is unlikely to be a good alternative to the Arriva or Northern Franchise services.
138. Arriva submitted that there are a number of significant competitors operating in the area, not least First Bus, which it indicated is the most significant operator in York. For example, First runs bus service 7 between Designer Outlet and York City Centre.¹⁰² These competitors provide routes in the areas adjacent to the overlaps and could serve the York to Selby route if the Arriva service were to be degraded. The CMA notes that these existing routes are

¹⁰¹ The CMA has previously discussed the calculation of the proportion of all passengers on flows by estimating the proportion of passengers disembarking at a bus stop, by the share of passengers boarding in the opposite direction of the same service. This approach circumvents the issue of lacking information of point of disembarkation for certain passengers. This approach would provide greater weight to stops where a significant share of passengers board the bus. In the case of the 415/416, this would be the overlap flow stops.

¹⁰² First service 7 is part of its 'Park and Ride' range of services which provide travel between the centre of York and attractions around York. See here: <https://www.firstgroup.com/york/routes-and-maps/park-ride/routes>

unlikely to be significant alternatives to the Arriva and Northern Franchise services on the overlap flows.

139. The CMA considers that Arriva service 415/416 and the overlapping Northern Franchise services are likely to be significant competing services since (i) the 415/416 does not overlap with third-party competing services on the rest of its route; (ii) the indirect TPE and less frequent/differentiated Utopia services appear to be weak alternatives; and (iii) the overlapping Northern Franchise service is likely to be a significant constraint on the Arriva service. Furthermore, the CMA has assessed barriers to entry or expansion and concludes that entry or expansion in itself could not prevent a realistic prospect of an SLC on the bus routes where there are competition concerns (see paragraphs 77-85).
140. Given the above, the CMA believes that there is a realistic prospect that the Franchise Award will result in an SLC on this overlap.

Middlesbrough – Redcar – Cleveland

Services 63/64: Middlesbrough – Redcar – New Marske

141. The Northern Franchise overlaps with Arriva's 63 and 64 bus services. The 63 and 64 bus services both serve the Middlesbrough Bus Station – Redcar Central flows. The overlaps between the Arriva 63 bus service and the Northern Franchise services occur on the Middlesbrough – James Cook University Hospital – Marton - Redcar flows, whilst the 64 bus service serves all the stations between Middlesbrough – New Marske on one branch of the Northern Franchise route (services to Saltburn). The most significant overlap (in terms of share of revenues arising on the flow) is between the Arriva 64 bus services and the Middlesbrough to Saltburn line on the Northern Franchise rail route.
142. Revenue generated by the Arriva 63 and 64 bus services amounted to [£] and [£] respectively in the last financial year, of which the overlapping flows accounted for around [£] and [£] respectively.
143. According to data provided by Arriva, the fares on the Arriva 63 and 64 bus services and the overlapping Northern Franchise rail services are broadly similar. The Arriva bus services are more frequent (bus service 63 offers up to 6 services per hour), whereas the Northern Franchise services are hourly. However, the Arriva bus services are slow/stopping services and as such journey duration on the bus services is longer, particularly on the longer overlap flows. Therefore passengers on overlapping flows may trade-off the accessibility and frequency of the stopping bus services against the longer

journey times on the Northern Franchise services and as such consider the overlapping services as good alternatives.

144. Arriva submitted that routes serving the Middlesbrough – Redcar flows (and beyond) are part of the Tees Valley Bus Network Partnership with the relevant local authorities. The Partnership places obligations on the operators, including Arriva, to ensure that there is sufficient capacity on their bus services. The CMA notes that, as a general principle, local bus services are not subject to the same degree of regulation as rail services and therefore there is a greater degree of flexibility for the operator in relation to bus services. The CMA has not received evidence allowing it to assess the impact of the Tees Valley Bus Network Partnership on Arriva’s ability to flex aspects of the offer that matter to passengers and their choices.
145. Arriva also submitted that other operators in the area had substantial networks and that these operators would be ready to expand services in the event that a commercial opportunity arose (eg reduced frequencies on Arriva services). The CMA has assessed barriers to entry or expansion and concludes that entry or expansion in itself could not prevent a realistic prospect of an SLC on the bus routes where there are competition concerns (see paragraphs 77-85).
146. One internal Arriva document indicates that bus services in the Middlesbrough – Redcar areas compete with the Northern Franchise services.¹⁰³ Another internal document notes that Stagecoach varied its route onto an area served by bus service 63, Middlesbrough – Marton, suggesting that there is some competition from Stagecoach on the shorter flows.¹⁰⁴
147. The CMA considers that Arriva bus services 63 and 64 and the overlapping Northern Franchise services are likely to be significant competing services since (i) the competitive constraint from third-party competing services appears limited; (ii) fares are broadly similar on the overlapping services; (iii) passengers may trade-off the longer journey times on the Arriva bus services against the higher frequency, such that the overlapping services are good alternatives to one another; and internal documents suggest that there is competition between the overlapping services.¹⁰⁵
148. Given the above, the CMA believes that there is a realistic prospect that the Franchise Award will result in an SLC on this overlap.

¹⁰³ Arriva North-East Bus Report P5 2014.

¹⁰⁴ Arriva North-East Bus Report P10 2014.

¹⁰⁵ See also paragraph 154 on the impact of Arriva’s existing network in the Tees Valley on incentives to maintain its passenger offer on overlapping flows.

Services X3/X4: Middlesbrough – North Skelton – Whitby

149. The Northern Franchise overlaps with Arriva's X3 and X4 bus services. Arriva's X3 and X4 bus services are part of the Arriva Sapphire range of premium services. The main overlap is with the Northern Franchise rail service running between Middlesbrough and Saltburn (part of the Bishop Auckland/Darlington route), but there is also a limited overlap with the Middlesbrough to Whitby service.¹⁰⁶
150. Revenue generated by the Arriva X3 and X4 bus services amounted to [£] and [£] respectively in the last financial year, of which the overlapping flows accounted for around [£] and [£] respectively. The CMA notes that Arriva has not identified the Middlesbrough to Whitby overlap with the infrequent Whitby Northern Franchise line. This would add to the size of the overlap on the X4, since both services cover this flow, albeit at significantly different frequencies.
151. Fares on the Northern Franchise rail service and Arriva bus services are similar and journey times are more comparable than the 63/64 bus services (discussed above) given that the X3/X4 are part of the Sapphire services offering faster travel between conurbations. Frequencies are the same on the Middlesbrough to Saltburn line and significantly higher on the Arriva bus services with respect to the Whitby Northern Franchise line. Therefore, the overlapping X3/X4 and Northern Franchise services appear to be close alternatives in their offer to passengers, as indicated by the extent of the overlap and the similarity in service offer.
152. Arriva has not identified any overlapping third-party services. Arriva submitted that competitors in the area had significant networks and would respond to attempts to degrade the offer on the Arriva services by introducing or expanding nearby services and that the Tees Valley Bus Network Partnership acts as a constraint on Arriva's ability to degrade services.¹⁰⁷ The CMA has not seen evidence suggesting that these constraints would prevent a realistic prospect of an SLC on the bus routes where there are competition concerns.
153. An internal document identifies the Northern Franchise services as competing with the Arriva X3 and X4 bus services and indicating that Arriva had decided to offer its Routesaver¹⁰⁸ tickets on these services in response to competition

¹⁰⁶ The X4 provides half-hourly journeys between Middlesbrough Bus Station and Whitby Bus Station, via Redcar. The X3 serves most of the X4 route (to Saltburn), at which point the X3 turns towards Skelton and Lingdale (South), whilst the X4 travels to Whitby Bus Station

¹⁰⁷ See paragraph 144 above.

¹⁰⁸ Routesaver tickets allow unlimited travel at any time of day on specific services or parts of services. Routesaver tickets are available as one-day, weekly, 4-week and annual tickets. X3/X4 Routesaver offers

with the Northern Franchise rail service.¹⁰⁹ One Arriva internal document mentions a third-party competitor in Whitby, which is offering lower fares in competition with the Arriva services.¹¹⁰

154. Arriva operates an extensive network of bus services in the Tees Valley. This is important for two reasons: firstly, passengers trade-off service factors (such as fares, frequencies and journey times) when making choices between overlapping services. On flows/corridors where Arriva bus services provide high combined frequency, passengers may be more willing to trade off longer journey times on the bus against the shorter journey times (but lower frequency) on the Northern Franchise services. On such flows (eg Middlesbrough – Redcar), Arriva bus services are a particularly good alternative to the Northern Franchise services. Therefore the extent of competition between the rail and bus services may go beyond that indicated by route level analysis. Secondly, the CMA and its predecessor bodies have in previous cases indicated that the greatest barriers to entry or expansion for bus operators are the threat of retaliation by the incumbent network operator and the significant cost associated with entry on a network basis.¹¹¹ Given the above, the CMA considers that entry or expansion is unlikely to act as a significant competitive constraint on the Parties services.
155. The CMA considers that (i) Arriva X3 and X4 overlap with the Northern Franchise for a significant part of the route; (ii) the overall offer on the overlapping services is similar, such that a significant proportion of passengers are likely to consider the two modes as substitutable and as such exert a competitive constraint on each other; (iii) there are minimal third-party services overlaps, which are unlikely to constrain the combined Arriva and Northern Franchise services; and (iv) internal documents suggest that the overlapping services are close competitors.
156. Given the above, the CMA believes that there is a realistic prospect that the Franchise Award will result in an SLC on this overlap.

Darlington

Service 7: Darlington – Durham

157. The Northern Franchise overlaps with Arriva's 7 bus service. The 7 bus service is part of the Arriva Sapphire range of premium services. The relevant

unlimited travel on services X3, X3A and X4 between Saltburn, Redcar and Middlesbrough. Source: <https://www.arrivabus.co.uk/north-east/bus-tickets/routesaver-tickets/>

¹⁰⁹ Arriva North-East Bus Report P5 2014.

¹¹⁰ Arriva North-East Bus Report P10 2014

¹¹¹ See CC [Review of methodologies in transport inquiries](#), May 2007, paragraph 72.

Northern Franchise rail services are the Bishop Auckland to Middlesbrough line via Newton Aycliffe and the Darlington to Newcastle line via Durham.

158. The Arriva 7 bus service and the Northern Franchise service overlap on the Bishop Auckland to Middlesbrough line and the overlaps account for around 14% of route revenues on the bus service. Given the Arriva service appears to be a connecting services to/from Darlington and Durham, the overlaps with the Northern Franchise could be significant. Therefore 14% is very likely to be a significant underestimate of the true scale of the overlap.
159. Journey times and fares between the Northern Franchise and Arriva bus service are comparable on the Darlington to Newton Aycliffe flow. In terms of journey frequency, Arriva's 7 bus service offers up to 4 services per hour, against the 1 service per hour on the Northern Franchise rail service. Journey times are however significantly faster on the rail services than on the Arriva service. Therefore passengers may trade-off longer journey times on the Arriva bus services and the higher frequency, such that the overlapping services are good alternatives for passengers.
160. On the Darlington to Newcastle via Durham line, VTEC and TPE provide rail services. TPE provides two services per hour and VTEC services are every two hours.
161. The CMA considers that (i) the overlap accounts for a significant proportion of the Arriva service 7 (which is likely to be underestimated by the share of revenues data provided); (ii) the overall offer on the overlapping services is similar or where there are differences in journey times, the frequency trade-off may compensate passengers, such that the overlapping services are close alternatives; and (iii) there are minimal third-party services overlaps, which are unlikely to constrain the combined Arriva and Northern Franchise services.
162. Given the above, the CMA believes that there is a realistic prospect that the Franchise Award will result in an SLC on this overlap.

Service X66: Middlesbrough – Faverdale Arriva Depot

163. The Northern Franchise overlaps with Arriva's X66 bus service. Arriva's X66 bus service is part of the Arriva MAX routes, which offer fast inter-urban services and is closely related to the X67. The X66 bus service operates between Darlington Tubwell Row and Middlesbrough Bus station, with some early morning services extending the route to Faverdale Arriva Depot. The relevant rail services are on the Bishop Auckland – Darlington – Middlesbrough – Saltburn line of the Northern Franchise route. The most

significant flows (in terms of share of route revenues) are between Stockton/Thornaby and Middlesbrough.

164. Revenue generated by the Arriva X66 bus services amounted to [X] in the last financial year, of which the overlapping flows accounted for around [X].
165. The Arriva X66 operates every half-hour and when combined with the X67 it provides services every 15 minutes.¹¹² The Northern Franchise provides up to 1 service per hour on the services stopping at North Road and 2 services per hour on the faster route. Fares are broadly similar on the Northern Franchise rail service and the X66 bus service.
166. TPE provides limited services on this flow, with services running every two hours during the peak periods. Arriva submits that Stagecoach bus services 36/37/38 and Go North East bus services X7/X9/X10 compete with Arriva services between Thornaby/Stockton and Middlesbrough. These third-party services together provide up to 11 services per hour on these flows. Arriva argued that the presence of these services and the Stagecoach depot meant that competitors could enter or expand onto the overlapping flows in the event of a degradation of the Arriva services. The CMA notes that although third-party competing services provide an alternative for passengers on the shorter flows, the effect of the Franchise Award is to remove an important competitive constraint on Arriva's X66 bus service.
167. One internal document notes that the X66/X67 competes with the Northern Franchise services and planned frequency enhancements are likely to make it a stronger alternative to the Northern Franchise services.¹¹³
168. The CMA considers that (i) the overlap accounts for a significant proportion of the Arriva service X66; (ii) the overall offer on the overlapping services is similar, such that a significant proportion of passengers are likely to consider the two modes as substitutable and as such exert a competitive constraint on each other; (iii) there are minimal overlaps with third-party services; and (iv) an internal document suggests that the X66 bus service competes with the Northern Franchise service.
169. Given the above, the CMA believes that there is a realistic prospect that the Franchise Award will result in an SLC on this overlap.

¹¹² The X66 and X67 cover the majority of the same route, but diverge in their route around Stockton. However the timetabling for the services is aligned, such that the two services alternate on the basis of combined 15 minute frequencies.

¹¹³ Arriva North-East Bus Report P8 2015.

Services X10/X11: Newcastle Upon Tyne – Cramlington – Blyth

170. The Northern Franchise overlaps with Arriva's X10/X11 bus service. Arriva's X10 and X11 bus services are part of the Arriva Max bus services providing fast inter-city bus travel. The bus services overlap with the Northern Franchise on the Chathill to Newcastle route, between Cramlington, Manors and Newcastle train stations.¹¹⁴ The X10/X11 bus service serves several of the same flows as Arriva bus services X8/X9, which provide slightly differentiated routes (to the X10/X11) between Newcastle and Blyth via Cramlington. One third party suggested that the Arriva X22 bus service is also a related bus service which operates between Newcastle and Cramlington, on route to Ashington.
171. Revenue generated by the Arriva X10/X11 bus services amounted to [X] in the last financial year, of which the overlapping flows accounted for around [X] of revenues for each service.
172. Arriva operates an extensive network of buses in Northumberland and several other routes serve the Cramlington – Manors – Newcastle flows. Arriva submitted that its combined frequency on services 43, X10, X11 and X13 of eight services per hour, is significantly higher than the Northern Franchise rail services, which offer up to 1 service per hour. This means that the Northern Franchise rail services do not exert a significant competitive constraint on the overlapping bus services.
173. The CMA notes that passengers consider the overall offer of competing transport options and may trade-off service factors (eg passengers may be willing to travel on services with longer journey times if fares are lower than the faster alternative). Passengers may therefore consider the Arriva and Northern Franchise services as good alternatives (despite the differences in frequencies), such that they exert a significant competitive constraint on each other. For example, travelling on the more frequent Arriva X10/X11 bus service between Cramlington and Newcastle takes 24 minutes (compared to 16 minutes by rail, but the rail service is less frequent, operating hourly) and the bus services offer cheaper tickets (£3.20 on the bus against £4.40 on rail).¹¹⁵
174. Furthermore, the CMA notes that even small rises in fares or reductions in frequencies may make the bus services less attractive to passengers and

¹¹⁴ The X11 service does not stop at Newsham Farm Shops while the X10 does not stop at Northburn Hauxley Drive.

¹¹⁵ The greater bus frequency may be one factor that gives Arriva a higher share of revenues on these flows than the Northern Franchise rail services. For example only 2% of revenues between Cramlington and Manors are derived on the Northern Franchise services.

encourage diversion to the overlapping rail services. Through the Franchise Award, this diversion is re-captured by Arriva, making the fare increases or frequency reductions profitable and as such more likely.

175. There are no third-party competitors on the overlap flows between Cramlington – Manors and Newcastle. Arriva submitted that the Go North East (**GONE**) services 17/17A (hourly) Centurion and 19 (half-hourly) Cobalt, connect Cramlington and other central parts of Newcastle. Furthermore, GONE 309/310 Cobalt Clipper services connect Newcastle and Blyth (the start and end points of the X10/X11) via a different route, travelling along the coast. Arriva told the CMA that the 309/310 route could be varied to match the X10/X11 in the event of a downgrade of the Arriva services. However it has also said that such variation would require PTE approval, given that the service is supported (albeit it was uncertain about the information provided by Northumberland County Council).
176. Arriva operates bus service 308, which also runs between Blyth – Whitley Bay – Newcastle (mirroring the GONE routes). As noted in paragraph 154, the CMA considers that any decision to modify existing routes or enter into new routes by a third party (eg GONE) will consider the expected response of incumbent operators such as Arriva, one of which may be to alter scheduling on the overlap routes or other parts of the network. Therefore, the CMA considers that the incentives to enter the market in the event of a degradation on the Arriva services are unlikely to be significant.
177. The CMA notes that the GONE bus service 19 is an hourly service between Cramlington and the stations in Newcastle (not half-hourly). Furthermore, the 17/17A, 19 and 309/310 GONE bus services do not serve the central Newcastle destinations that the Arriva bus and Northern Franchise services cover. Passenger demand is for transport between two specific points and as such options which do not serve the same points (or within a narrow distance band as discussed in the paragraphs 37-42) are unlikely to be good alternatives to the Northern Franchise or Arriva services. The CMA also notes that third parties have generally submitted that bus services involving indirect options are likely to be weak alternatives, because bus services are generally not scheduled to provide connecting services and as such may involve significant waiting time at connection points.
178. Arriva also submitted that the route is covered by the Explorer multi-operator ticketing (**MOT**) scheme. The ticket offers unlimited travel for a day on bus, train and other services across the North-East. The scheme accounts for around 19% of revenues in the North-East. Arriva has not provided supporting evidence of the extent to which the Explorer ticketing scheme limits its

incentives to lower frequency, increase fares or otherwise worsen the offer on the overlapping services.¹¹⁶

179. The CMA considers that (i) the overlap accounts for a significant proportion of the Arriva services X10/X11; (ii) the Arriva bus services are likely to be good alternatives to the Northern Franchise services (particularly when considering the other Arriva services in the area), such that a significant proportion of passengers are likely to consider the two modes as substitutable and as such exert a competitive constraint on each other; and (iii) the third-party services are unlikely to be good alternatives to either of the Parties services.
180. Given the above, the CMA believes that there is a realistic prospect that the Franchise Award will result in an SLC on this overlap.

Services X15 and X18: Newcastle – Berwick

181. The Northern Franchise overlaps with Arriva's X15 and X18 bus services. Arriva bus services X15 and X18 are part of Arriva's MAX services which offer express inter-urban services. The X15 operates hourly between Alnwick Bus Station and Newcastle Haymarket Bus Station (occasionally extending travel to Berwick rail station). The X18 operates between Alnwick and Newcastle and around half that frequency on the Berwick to Alnwick flows. The X14¹¹⁷, X15 and X18 all overlap on a number of corridors between Morpeth and Newcastle / Manor stations. In addition, the X18 overlaps with the Northern Franchise services for flows from Alnmouth Station. The relevant Northern rail services are the Chathill – Alnmouth – Morpeth – Newcastle services.
182. Revenue generated by the Arriva X15 and X18 bus services amounted to [£] and [£] respectively in the last financial year, of which the overlapping flows accounted for around [£] and [£] respectively. Arriva did not identify the overlap between its bus services serving Alnwick (but which do stop within 1,600 metres of Alnmouth rail station) and the Northern Franchise rail service. The CMA notes that although Alnmouth for Alnwick station is based in Alnmouth village, it appears to be serving the larger settlement in Alnwick. Therefore residents of Alnwick may consider the Northern rail services and the Arriva bus services as good alternatives and that the size of the overlap is more significant than suggested by the data submitted by Arriva.

¹¹⁶ The Explorer ticket costs £9.80 for adults and as such is unlikely to be a good alternative for passengers travelling between the overlap flows, where a day ticket for Arriva services costs £4.80 and a peak return on Northern costs £6.

¹¹⁷ This is not one of the bus services identified for a detailed competitive assessment. Revenues on the X14 are around £640k and the overlap flows account for around 14% of total route revenues.

183. Journey times on the Northern Franchise services are much shorter, particularly on the longer flows. For example, travel on the X18 bus between Alnmouth and Newcastle takes 1 hour 43 minutes and around 28 minutes (or about a third of the time) on the rail. However fares are considerably lower on the bus services. For example, an adult single is £6 or a day ticket £7.30 on the Arriva bus, whereas the cheapest adult peak single on the Northern Franchise services is £10.30. Combined with the higher frequency on the bus services, this means that the Parties' services may be good alternatives to each other for passengers, who may trade-off longer journey times against higher frequency and lower fares on the Arriva bus services.
184. One third party told the CMA that there was some competition between the Arriva bus services and the Northern Franchise services for flows between Morpeth and Newcastle.
185. Cross-Country (Arriva) and Virgin Trains East Coast provide rail services between Morpeth and Newcastle each with a frequency between 1 service every hour or every 2 hours. The Virgin Trains East Coast service may provide some competitive constraint on the Arriva service on this flow, which accounts for around 16% of route revenues on the X18.
186. Arriva submitted that a proportion of the overlapping routes and a number of third-party competitors operated tendered services on behalf of Northumberland County Council, covering flows to the North of Alnwick. Furthermore, Travelsure operates the 418 which is co-ordinated with its own services for travel North of Alnwick (to Belford). Arriva submitted that competition between Arriva and third-party tendered services, ensured that timetabling on the non-tendered parts (ie South of Alnwick) was also protected, since the bus services had to travel through the intermediate conurbations where the overlaps arise (eg Morpeth) to serve Newcastle. Arriva also submitted that several of the conurbations where overlaps arose were small (eg Alnmouth village had 445 residents in 2011). Given the number of tendered services on a significant part of the route and the small conurbations involved, Arriva told the CMA that Northumberland County Council would expand control in these areas if Arriva increased its fares.
187. Arriva submitted that a number of third-party competitors operated bus routes tendered by Northumberland County Council, covering flows to the north of Alnwick. Furthermore, Travelsure operates the 418 which is co-ordinated with its own services for travel North of Alnwick (to Belford). The CMA does not consider that this is likely to be a significant constraint on Arriva's ability or incentive to reduce its offer on the overlapping services. The significance of overlaps is already captured in the filtering methodology (eg the de-minimis and effective competitor filters). The CMA further notes that the majority of the

overlap between the Arriva and Northern Franchise services are for flows to the South of Alnwick. The CMA has not received evidence to support Arriva's submissions on the role of Northumberland County Council in protecting frequencies, fares or other aspects of the offer to passengers.

188. Arriva also submitted that the route is covered by the Explorer MOT scheme. The ticket offers unlimited travel for a day on bus, train and other services across the North-East. The scheme accounts for around 19% of revenues in the North-East. Arriva has not provided supporting evidence of the extent to which the existence of the Explorer ticketing scheme limits its incentives to lower frequency, increase fares or otherwise worsen the offer on the Parties' services.
189. The CMA considers that (i) the overlap accounts for a significant proportion of revenues on the X15 and X18 services; (ii) the Arriva services are likely to be good alternatives to the Northern Franchise services (particularly when considering the other Arriva services in the area), such that a significant proportion of passengers are likely to consider the two modes as substitutable and as such exert a competitive constraint on each other; and (iii) the competition constraints from third-party services appear to be very limited.
190. Given the above, the CMA believes that there is a realistic prospect that the Franchise Award will result in an SLC on this overlap.

Liverpool

Service 79/79D: Liverpool – Halewood

191. The Northern Franchise overlaps with Arriva's 79/79D bus services. Arriva's 79 bus service is a high frequency service operating between Liverpool One Bus Station and Halewood Shopping Centre. The relevant rail service is the Liverpool to Manchester Piccadilly via Warrington Central section of the Northern Franchise. The longest overlap between the Parties' services is between the Liverpool Lime Street/Liverpool One Bus Station and Halewood. There is also a short overlap between Liverpool Lime Street and Wavertree Technology Park on the Northern Franchise rail network.
192. Revenue generated by the Arriva 79/79D bus service amounted to [X] in the last financial year, of which the overlapping flows accounted for around [X].
193. Journey times are longer on the Arriva bus services (eg 38 minutes for Halewood to Liverpool by bus against 21 minutes on the Northern Franchise rail service) and fares are lower (£2.20 flat fare by bus against £3.80 for an adult peak single on rail). Therefore the Parties' services may be considered

to be good alternatives by passengers who are willing to trade off the longer journey times against the lower fares on the bus when compared to the rail journey times and fares.

194. The overlapping services are part of Merseytravel Solo / Trio / Saveaway MOT. A weekly solo ticket in zone C (includes Liverpool and Halewood MOT bus travel) is £18.20 while a weekly Arriva bus only ticket is £16.00. Allowing for the added value of multi-operator travel, these tickets are likely to compete on these flows for season ticket passengers.
195. Arriva submits that there are a number of competing providers to its 79/79D service, some which involve indirect connecting services. Cumfybus operates a service between Liverpool Lime Street Station and Prescot, which overlaps with the shorter Wavertree flow. Arriva also submits that there are indirect services between Liverpool Lime Street and Halewood (eg Huyton Travel 163/166 Halewood - Belle Vale and Huyton Travel 173 Belle Vale – Liverpool Lime Street). However the CMA considers that these limited overlaps are unlikely to impose a significant constraint, particularly in relation to the Liverpool Lime Street – Halewood flow bearing in mind that travel options involving changes on bus services are weak alternatives to direct bus services because of the lack of timetable alignment, particularly across operators.
196. The CMA considers that (i) the Arriva 79/79D and Northern Franchise services appear to be close alternatives on the Liverpool Lime Street – Halewood flow; and (ii) the competition constraints from third-party services appear to be limited.
197. Given the above, the CMA believes that there is a realistic prospect that the Franchise Award will result in an SLC on this overlap.

Service 6: Liverpool – Huyton

198. The Northern Franchise overlaps with Arriva bus service 6. Arriva bus service 6 operates between Liverpool Queen Square Bus Station and Huyton Bus Station. The relevant Northern Franchise rail services are the Liverpool – Blackpool (branch one) and the Liverpool – Manchester Victoria/Manchester Airport and Ellesmere Port (branch two).
199. Revenue generated by Arriva on these 22 flows amounted to [X] in the last financial year, which represents about [X] of total revenue on the relevant routes. 21 flows are excluded from further analysis on the basis of the de minimis and effective competitor filters and only one flow is left which has revenues of around £1,000 and accounts for a small proportion of route revenues (around 2%).

200. The CMA notes that the remaining flow appears to be served by bus service 61 (Halton Transport). Halton Transport 61/61A and Cumfybus 139 each provide half- hourly (peak) frequency services from Monday to Saturday between Liverpool and Huyton (Halton also provides limited Sunday services). Therefore, third-party competitors provide a competitive constraint on the majority of the overlap flows.
201. The CMA therefore considers that the Franchise Award does not raise a realistic prospect of an SLC on the overlaps between Arriva bus service 6 and the Northern Franchise services.

Annex 2: 31 routes with bus-on-rail overlaps raising competition concerns

No.	Arriva Division	Route number(s)	Origin – Destination
1	North East	8	Darlington - Spennymoor
2	North West	20	St Helens - Earlestown
3	North East	21	Darlington - Peterlee
4	North East	22	Middlesbrough - Ings Farm, Durham - Sunderland
5	North East	35	Morpeth - Newbiggin
6	North East	43	Newcastle - Morpeth, Durham - Esh Winning
7	North West	75	Halewood - Liverpool
8	North West	76	Halewood - Liverpool
9	Yorkshire	148	Wakefield - Knottingley
10	Yorkshire	184	Castleford - Pontefract
11	Yorkshire	185	Wakefield - Pontefract
12	Yorkshire	187	Wakefield - Pontefract
13	Yorkshire	189	Wakefield - Leeds
14	Yorkshire	203	Huddersfield - Leeds
15	Yorkshire	281	Thornhill - Fieldhead
16	North West	352	St Helens - Wigan
17	Yorkshire	400	Selby - Goole
18	Yorkshire	401	Selby - Goole
19	Yorkshire	410	Chequerfield - Leeds
20	North East	1/1B/X1	Blyth - Widdrington, Darlington - Tow Law
21	North West	10/10A	Salford - Manchester, Macclesfield - Bollington, St Helens - Liverpool
22	North West	10B	Huyton - Liverpool
23	North East	28/28B	Middlesbrough - Lingdale, Middlesbrough - Stokesley
24	North East	29/29A	Middlesbrough - Nunthorpe
25	North East	5/5A	Middlesbrough - Loftus, Middlesbrough - Brotton, Darlington - Bishop Auckland
26	North East	85/X85/685	Newcastle - Haydon Bridge, Haydon Bridge - Carlisle, Newcastle - Hexham
27	North East	X12	Middlesbrough - Newcastle
28	North East	X13	Blyth - Newcastle
29	North East	X14	Newcastle - Thropton
30	North East	X5	Blyth - Newcastle
31	North East	X93	Middlesbrough - Scarborough

Annex 3: 38 rail-on-rail overlapping flows raising competition concerns

No.	Origin	Destination
1	Sunderland	Hartlepool
2	Sunderland	Eaglescliffe
3	Hartlepool	Eaglescliffe
4	Leeds	Wakefield
5	Leeds	Sheffield
6	Leeds	Chesterfield
7	Leeds	Nottingham
8	Wakefield	Sheffield
9	Wakefield	Chesterfield
10	Wakefield	Nottingham
11	Doncaster	Sheffield
12	Bradford	Halifax
13	Bradford	Brighouse
14	Bradford	Mirfield
15	Bradford	Wakefield
16	Bradford	Pontefract
17	Halifax	Brighouse
18	Halifax	Wakefield
19	Brighouse	Wakefield
20	Brighouse	Doncaster
21	Mirfield	Wakefield
22	Wakefield	Pontefract
23	Pontefract	Doncaster
24	Chester	Manchester
25	Chester	Stockport
26	Warrington	Earlestown
27	Earlestown	Manchester
28	Newton-le-Willows	Manchester
29	Newton-le-Willows	Manchester Airport
30	Manchester	Wilmslow
31	Manchester	Crewe
32	Manchester	Macclesfield
33	Manchester	Congleton
34	Stockport	Macclesfield
35	Stockport	Congleton
36	Wilmslow	Stockport
37	Newton-le-Willows	Macclesfield
38	Warrington	Manchester