

Decision to launch a review of FirstGroup plc undertakings in relation to 1989 merger of Badgerline Holdings Ltd and Midland Red West Holdings Ltd

31 January 2017

Introduction

1. In its [2016/17 Annual Plan](#), the Competition and Markets Authority (CMA) committed to build on its programme of work to review¹ its existing remedies systematically and to remove measures that are no longer necessary by launching further reviews of old merger or market remedies.²
2. The CMA has now decided to launch a review under the Enterprise Act 2002 of undertakings arising from the 1989 merger of Badgerline Holdings Ltd (now FirstGroup Holdings Limited) and Midland Red West Holdings Ltd (now FirstBus Group Limited).

Details of remedy

3. The CMA has identified the undertakings in relation to the 1989 merger of Badgerline Holdings Ltd (Badgerline) and Midland Red West Holdings Ltd (trading as City Line) as being appropriate for review.³
4. The Monopolies and Mergers Commission (MMC) did not find any concerns with respect to commercial services but identified serious detriments to competition for Avon's contract services as a result of the merger. It concluded therefore that the merger may be expected to operate against the

¹ The CMA has a statutory duty to keep under review undertakings made under the Fair Trading Act 1973 as well as those under the Enterprise Act 2002. For Fair Trading Act 1973 undertakings, the CMA will advise the Secretary of State for Business, Innovation and Skills regarding retaining, varying or releasing undertakings, while for Enterprise Act 2002 undertakings, the CMA can reach the decisions itself.

² In its [2015/16 Annual Plan](#), the Competition and Markets Authority (CMA) committed to commence this programme of work. As part of this, in April 2015, the CMA launched reviews of 71 structural merger remedies that had been put in place before 2005. These reviews resulted in 51 obsolete remedies being removed from the CMA's register. In 2016 the CMA [sought views from stakeholders from 22 April to 20 May 2016](#) on which further remedies it should review as part of this exercise. On 14 June 2016 and 31 August 2016 the CMA launched [reviews of a number of remedies](#). See [CMA webpage: Review of merger undertakings given before 1 January 2006](#) for details.

³ The undertakings were originally given by Badgerline Holdings Ltd in 1989 and subsequently given again by Firstbus plc after an amendment in February 1996.

public interest. It was concerned that effective competition for Avon council contracts would disappear as a result of the merger. In particular:

- (a) that there would be an increase in the anti-competitive practice whereby Badgerline, having deregistered certain commercial services, had reregistered them partially or wholly after failing to win the tendered contracts for the subsidized services replacing them; and
- (b) that the loss of City Line as an independent major competitor for Avon's contract services would weaken competitive tendering and thus increase the cost to Avon of supporting socially necessary bus services or, in certain circumstances, make it impossible for Avon to support these services to the full extent that it would wish to support them.

5. Undertakings were given by Badgerline (the Badgerline undertakings) in October 1989⁴ and contain four main components:

- A prohibition on Badgerline/City Line (both now part of FirstGroup plc) engaging in the practice of de-registering a commercial bus service, tendering for any replacement subsidised service but re-registering a commercial service which 'substantially duplicates' the subsidised service in the event that the Avon contract is awarded to a competitor.
- A cap on the price quoted for the subsidised service, based on the expected direct costs less revenue.
- A requirement to refund 50% of the excess revenue if Badgerline/City Line wins the contract and actual revenue exceeds estimated revenue in any year.
- A requirement to provide, on request by Avon County Council⁵, an independent auditor with information for the purposes of monitoring compliance.

6. An amended version of the undertakings was given in February 1996 by Firstbus plc, which was created by the 1995 merger of Badgerline and GRT Group.⁶ The amended undertakings broadly substantively reproduce the

⁴ See [undertakings given by Badgerline Holdings Ltd on 3 October 1989](#).

⁵ We note that Avon County Council was disbanded in March 1996 and its functions taken over by four local authorities, plus a Local Enterprise Partnership of those local authorities which has over-arching responsibility for public transport in the area.

⁶ See [amended undertakings given by Firstbus plc on 2 February 1996](#).

original although some clauses were re-drafted more concisely and some excisions were made.⁷

Prioritisation principles

7. In order to make the best use of its resources, the CMA needs to ensure that it makes appropriate decisions about which projects and programmes to undertake across its areas of responsibility. The CMA has selected the Badgerline undertakings for review at this time in the light of its published [prioritisation principles](#) as described below. These principles are impact, strategic significance, risk and resources. We consider each of these in turn.
- (a) **Impact:** Overall, the removal of remedies that are no longer appropriate allows the CMA to focus its resources on monitoring remedies that continue to generate benefit for consumers and the UK economy. The CMA expects the impact of reviewing older undertakings to deliver reductions in regulatory burdens, generating indirect benefits for consumers. Given the age and behaviour restraints imposed by the Badgerline undertakings a review at this stage is appropriate.
 - (b) **Strategic significance:** This review reflects the CMA's statutory duty to keep under review orders and undertakings and also the CMA's published priorities in the current financial year.
 - (c) **Risk:** The Badgerline undertakings are over 25 years old. Given the age of these undertakings, it is possible that they may no longer be appropriate given market and other developments likely to have taken place. Consequently, the CMA considers there to be a realistic prospect of finding a relevant change of circumstances in this review. However, the passage of 25 years may also present a risk that stakeholders are not in a position to provide sufficient quality of evidence about changes relevant to the undertakings and consequently review is not able to proceed at a satisfactory pace. We propose to engage actively with FirstGroup and other local stakeholders to manage this.
 - (d) **Resources:** The CMA considers that the resources involved in conducting a review is likely be modest.

⁷ Substantive elements of the 1989 undertakings excised from the 1996 version are: clause 2(a); the definition of 'revenue' as on-bus revenue plus 10%; reference to the independent auditor using a 20% sample of all tenders; a provision that the auditor would specify what adjustment would give effect to the undertaking retrospectively; clauses 2(e), 2(f) and 3; and the appendices.

Decision to launch a review

8. The CMA has decided to launch a review of the undertakings given in the merger of Badgerline Holdings Ltd and Midland Red West Ltd. In reaching this decision, the CMA has obtained sufficient evidence, through its own research and information provided by FirstGroup Holdings Limited (FirstGroup), to have established a realistic prospect of finding a change of circumstances. In particular, in the intervening 26 years it is likely that there will have been changes on both demand and supply side of the market.
9. In its review the CMA will consider whether the magnitude of these changes, in relation to the concerns which the MMC sought to remedy, is sufficient to amount to a change of circumstances such that the undertakings are no longer required or need to be varied

(1) Demand side factors such as administrative structure and tendering practices

10. We have identified the following changes on the demand side:
 - **Avon County Council has ceased to exist:** Avon County Council was disbanded in March 1996, shortly after the merger of Badgerline and GRT Group to form FirstBus plc, and replaced with four local authorities.⁸ The area originally covered by Avon County Council remains informally known as Greater Bristol and the four authorities now also operate in a Local Enterprise Partnership called the West of England Partnership (WEP) which has over-arching responsibility for public transport. FirstGroup has argued that the abolition of Avon County Council represents a relevant change of circumstance for the purposes of section 92 of the Enterprise Act. We will examine the undertakings in light of this change and also in the context of the MMC's original concerns and other relevant economic developments.
 - **Changes in tendering practices:** FirstGroup has submitted that the four local authorities who succeeded Avon County Council in 1996 have increased buyer power due to changes in procurement practices and their focus on increasing choice and encouraging more bidders. For example: initiatives such as 'kick start' tenders which new entrants can use to gain a commercial foothold; the use of online tenders have reportedly attracted greater interest from bidders; and designing contracts which are less

⁸ Bristol City Council, South Gloucestershire Council, North Somerset Council, Bath and North East Somerset Council.

prescriptive and more open to input from operators. We also note that Bristol City Council adopted a mass tendering approach to contracting its bus services in 2006, which led to the entry of Rotala.⁹

- **Increase in the scope of routes being offered for tender:** FirstGroup has submitted that further additional procurers have emerged in the market since the undertakings were given, such as WEP, Bristol Airport and the University of the West of England.
- **Changes to tendering policy:** Since the undertakings were given there have been many changes to transport policy and funding of tendered services. We will consider the extent to which such changes and other initiatives¹⁰ represent a relevant change of circumstance in the 'Greater Bristol' area.

Further the Competition Commission (CC) Market Investigation report¹¹ into local bus services in 2011 along with remedies, led to the Local Bus Services Market Investigation (Access to Bus Stations) Order 2012.¹² We will consider the extent to which these developments constitute a relevant change of circumstances in the context of the MMC's concerns.

(2) Supply side constraints on FirstGroup

11. There have been changes to the competitive structure of the market:

- **The emergence of new significant operators:** FirstGroup has submitted that it now faces greater competition from other bus operators than it did in the late 1980s. We have observed at least two new entrants in the Bristol area¹³, the larger of which has been able to expand through winning significant contracts. These competitors may pose a greater competitive restraint on FirstGroup than those operating on Badgerline/City Line at the time of the merger.

FirstGroup also highlights greater competition from Bath Bus Services (owned by RATF), Stagecoach and Crosville Motor Services. Although these have operations geographically focused outside the relevant area,

⁹ Competition Commission: [Local bus services market investigation report](#), 20 December 2011, paragraphs 13.73 and 13.105.

¹⁰ These include: a three phase Joint Local Transport Plan covering the total period 2001-2026; bundled/mass tendering of contracted routes by Bristol City Council in 2006 and 2011; development of the Greater Bristol Bus Network; bids for Bus Service Operators' Grants and Better Bus Area grants for funding for infrastructure and route improvement projects.

¹¹ Competition Commission: [Local bus services market investigation report](#), 20 December 2011.

¹² [Local Bus Services Market Investigation \(Access to Bus Stations\) Order 2012](#), 26 July 2012.

¹³ Abus in 1991 and Rotala (under the brand Wessex Bus) in 2007.

they have the capacity to bid for tenders within the relevant area. We note that large national operators have acquired some of the other bus operators referred to in the MMC's original report¹⁴ resulting in changes in their corporate structure, branding and apparent geographic area served.¹⁵ Further investigation is required to establish the extent to which this applies to the tendered services which were of concern to the MMC.

- **Changes to route network and service levels:** Bus operators serving the relevant area make changes to their routes and service relatively frequently which may be relevant to the concerns articulated by the MMC. The extent to which these changes reflect broader local authority procurement strategy and involvement in local public transport improvement initiatives developed centrally by the DfT will be considered.¹⁶ Further investigation is also required to establish whether these changes apply to the tendered services which were of concern to the MMC.

Stakeholder views

12. The CMA is seeking views from interested parties as to whether or not there is a case for removing or varying these undertakings. In particular, we would welcome comments from local authorities, other bus service procurers, bus operators and bodies representing bus passengers on the following issues:
 - How the ability of contracting bodies to attract a satisfactory range of viable and competitive bids has changed in the intervening years.
 - Developments in the role and objectives of local authorities and other bus service procurers in relation to tendering processes in comparison with those of Avon County Council.
 - The emergence or growth of competing bus operators, or potential competitors, which are able to provide a competitive restraint for tendered bus services.

¹⁴ MMC Report: [Badgerline Holdings Ltd and Midland Red West Holdings Ltd: a report on the acquisition by Badgerline Holdings Limited of Midland Red West Holdings Limited; Cm 595, 8 March 1989](#) (the 'MMC Report')

¹⁵ For example: Wilts & Dorset is now owned by the Go-ahead Group plc and since 2012 operates under two brands in Amesbury and Bournemouth and Poole; Southern National and Western National are both owned by First Group plc (Western National was included in 1995 merger of Badgerline with GRT Group and its Gloucestershire operations were sold to Go-ahead Group and Stagecoach West); Cheltenham & Gloucester Omnibus was bought by Stagecoach Group plc renamed Stagecoach West.

¹⁶ For example, development of bus corridors has been a significant element in the Joint Local Transport Plans developed by the West of England Partnership.

- The practical impact of these undertakings on competition for tendered services and the ability of councils to continue to offer the tendered services.
13. Those responding should provide their views, supported with relevant evidence where possible, in writing to the CMA either by email or by post as set out below:

Nancy Race
Competition and Markets Authority
6th Floor North
Victoria House
37 Southampton Row
London WC1B 4AD

Email: remedies.reviews@cma.gsi.gov.uk

14. Responses should be received by the CMA by 5pm on **3 March 2017**.