

Department for
Transport

**A guide to the railway franchise
procurement process**

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Introduction

1. This short guide explains the processes which the Department for Transport follows when procuring railway franchises, in line with the duties and powers set out in the 1993 Railways Act (as amended)], taking account of other relevant UK and EU legislation and with Office of Government Commerce OGC and HM Treasury procurement regulations and practices.
2. This guide is intended to give a general overview to the public and to prospective bidders. The Department is committed to a process of continuous review and improvement of the franchising process and intends to make the procurement process as simple and transparent as possible. The Department believes that this approach will most likely secure best value for money (VfM) bids on behalf of rail passengers and taxpayers.

Pre-Qualification

3. The first step in the procurement process is the release of a Prior Information Notice (PIN) which sets out the anticipated programme for procuring a specific franchise or franchises and includes a brief specification of what the relevant franchise or franchises will comprise and likely procurement programme dates.
4. Secondly, advertisements will be placed in domestic, European and international journals, trade press and other publications, and/or an OJEU will be issued, to inform potential applicants of the opportunity in more detail and asking for expressions of interest. Those who are interested will be able to download a pre-qualification document pack from the Department's website.
5. The purpose of pre-qualification is to select those to whom the Department would be happy to award the franchise, subject to them submitting the best value bid. The

objective is therefore is to secure a manageable field of high quality bidders. In this context, procurement best practice regards three to five bidders as the optimum number to provide adequate competition. Although possible, the Department would regard a field of more than five bidders as unlikely because that would add to both suppliers' and the Department's costs, without a commensurate benefit in terms of stronger competition. Bidders are also likely to consider that the probability of winning, in a field of more than five, is insufficient to justify the cost of bidding. However, the number of bidders is less important than their quality.

6. The Department wants to pre-qualify those who can be expected to submit attractive, competitive and realistic bids, and who will then be capable of delivering a high-quality service at the price which they have offered. To achieve this, the pre-qualification questionnaire invites applicants to provide evidence of their competence and experience, which the Department will assess. For assessing the responses the Department uses pre-determined scoring systems, as follows:
 - Generally 50% of the total score available is awarded for demonstrating a proven track record of service delivery and financial management in relevant areas of activity (which may not necessarily be within the UK including evidence of a commitment to continuous improvement and business excellence)
 - 50% of the score is awarded for demonstrating appropriate outline plans and experience for the development and management of the Franchise.
7. Those who pre-qualify will be those with the highest aggregate scores and rankings. The pre-qualification scoring process is empirically based and necessarily involves judgements, but these are based solely on the evidence submitted by applicants in their documented responses. Where applicants are current UK rail franchise operators, the moderation of the scores allocated for track record will take into account other available evidence. This evidence will include industry performance data, National Passenger Survey results and recorded breaches of agreements with the Department of companies in the same owning group as that of the applicant or members of the applicant's consortium.
8. Public or other representations are not taken into account, nor are the number of franchises which a potential bidder already operates or the proximity of those franchises to the one being let.
9. The required evidence of past track record can vary between franchises and full details will be provided in the advertising notices which launch the franchise procurement processes. The track record need not be established in the passenger rail market in the UK; it can also be established outside the UK, in a different field of public transport for example, bus or air. or in some other sector. However, the Department does expect at least one of the companies participating in a bidding team to have established its good track record in the field of rail passenger services.

10. In assessing and scoring the track record of passenger service operators, the Department will score and rank only those variables which were within the bidders' direct control. For example, bidders will not get credit, or be penalised, for a change in reliability which is primarily attributable to the infrastructure operator or others.
11. The Department will assess any past failure to deliver on contractual commitments, including those of price and quality, whether arising from over-optimistic bidding or from poor management. In the case of rail franchise contracts this will apply to those let since January 2001.

Consultation

12. In parallel with the pre-qualification for potential bidders, the Department will consult affected transport authorities and devolved administrations about the services which should be specified in the franchise contract before the ITT is issued. The Department will consider with these partners the specification of services which meet the franchise objectives, deliver value for money and are affordable. The Department will also take into account wider franchising, transport and economic objectives, including how specification, evaluation and the franchise contract work together to deliver the appropriate mix of commercial flexibility and public service outputs.
13. This consultation also provides an opportunity for funding authorities, the Scottish Ministers, the Welsh Assembly Government, Transport for London and the Passenger Transport Authorities to decide whether to exercise their rights to request the Department to purchase additional services on their behalf or to reduce service provision.
14. The Department will seek the views of Passenger Focus in the development of the franchise proposition, and, where available, will use research into the views and preferences of passengers. At the same time as the ITT is issued, the Department will issue a Stakeholder Briefing Document aimed at all interested parties, including passengers. This aims to fully explain the proposition which the Department is seeking bids on.

The invitation to tender

15. The applicants who are accredited will receive an invitation to tender (ITT) to operate the franchise.
16. The ITT will include a base service specification. The specification for the train service requirements may include a range of service features and outputs, which may include mandated minimum quantum of station stops for specific passenger flows or service groups as a Train Service Requirement (TSR) which the Secretary of State requires to be provided to destinations along the routes and any other essential requirements that he/she may have. Other essential requirements may include, for instance, a requirement to operate or manage certain stations or manage the introduction of new

rolling stock. The base service specification is the basis on which the Secretary of State will have approved the letting of the franchise, having considered affordability, value for money and wider objectives, and having reached a judgement on how best to reconcile the conflicting interests of different types of rail-user and different communities. A bid which does not comply with the base service specification will be regarded as non-compliant.

17. The Secretary of State is keen to maximise input and innovation that bidders make to the detailed design of the timetable. The Secretary of State therefore intends to avoid over-specifying the base service specification, whilst providing sufficient clarity about the requirements to ensure that there is a level playing field when bids are appraised.
18. In addition to the Secretary of State's base service specification, the Department may also invite or require bidders to submit priced options. These will cover increases or decreases in service level, which the Department or other contract funder, on whose behalf we are acting, would be willing to implement if the resulting cost or saving was sufficiently attractive. The advantages of knowing the actual cost or saving resulting from a substantial change to the franchise are obvious. From the funder's perspective, the priced option is a very powerful tool, but we recognise that it adds time and cost to bid-preparation. The Department will ensure that it only includes priced options which it is genuinely interested in pursuing and believes it can afford, and will endeavour to ensure that other funders do likewise.
19. Bidders are generally free to include in addition bidder generated options. These can take a variety of forms. They might be investments, which the bidder believes are commercially attractive, but would not recover their costs within the lifetime of the franchise. They might be changes to service patterns that would improve reliability or the financial performance of the franchise, but are beyond the bounds set in base service specification. There is, of course, no presumption that the Department will take up any such options as the Department has to manage within a fixed rail expenditure budget. Accordingly, the bidder-generated options which will be of most value are ones which do not make additional demands on Government funding, e.g. station improvements which pay for themselves by generating increased passenger numbers.
20. The Department wishes to keep the costs and timescales of franchise bid preparation and appraisal as low as reasonably possible. We will encourage bidders to focus on the essentials - how they would operate a robust service, improve reliability and revenue, and reduce cost. As part of the Department's process of continuous improvement efforts will be made to reduce both the volume and cost of bids.

Franchise award

21. The franchise contract will be awarded to the bidder who offers the Department the best, robust proposition, in terms of price and reliability, for operating the base service specification in the ITT. This proposition will need to be affordable, and represent an acceptable level of value for money.

22. For this purpose, the Department will assess the deliverability and quality of the bidders' propositions. This assessment will be used to give the Department confidence that the successful bid can deliver its commitments, and will be taken into account where two or more bids are close in the assessment of price.
23. The Department will assess the cost and revenues set out in bids for deliverability. If this assessment indicates a significant risk that costs or revenues will not be delivered, or identifies other reasons why the franchisee is likely to be financially unstable, the Department may exclude bids from the competition on the grounds that they are financially high risk. Alternatively the Department may seek additional guarantees to be written into the contract to reduce the risk to public finances to an acceptable level.
24. For the purposes of award, the price offered by bidders will be restated as a net present value (NPV), using the same discount factor as the Department applies in appraising investments. The NPV will be calculated over the period of the franchise and may take into account potential extension periods.
25. Before award the Department will consider the affordability of the franchise proposition put forward by all bidders. If the premium/subsidy of any bid is unaffordable it is open to the Department to reject that bid. If all bids are unaffordable it is open to the Department to cancel the competition. Affordability of the national rail and transport budgets will be a key consideration in this judgment.
26. The Department will consider the value for money of the franchise proposition put forward by the leading bidder. If the value for money of the bid is unacceptable it is open to the Department to award to the next ranked bidder that has acceptable value for money. If all bids are unacceptable it is open to the Department to cancel the competition.
27. A separate paper "franchise evaluation flow charts" is prepared for each franchise competition and provides more detail on evaluation process which is used in the evaluation of franchise bids.

During the franchise

28. Once a contract is awarded we expect the franchisee to deliver the service and the price they have committed to in their bids.
29. The Department wants to keep franchise-monitoring effective and efficient by focussing on essentials. A failure to deliver the contractual commitments which a franchisee has voluntarily entered into will be regarded as serious. The new franchises build in graduated penalties, culminating in termination, for failure to deliver an improvement in the franchise services to which a franchisee has contractually committed. Financial failure will be regarded as equally serious.
30. OPRAF and the SRA have in the past rescued failing franchises, rather than putting in an operator of last resort (OOLR) and then reletting the franchise. The Department

has not, and will not, follow that precedent. Such rescues may have been justified in a relatively immature market where there was only limited experience of commercial passenger-service operation for bidders to draw on, and only limited evidence on which they could base revenue and cost forecasts. Given a more mature market, franchisees must build resilience into both their operational and financial plans to deal with the changes in the economic environment to which a passenger rail operation may be subject. Revenue risk sharing mechanisms will be required where appropriate and will be designed on a franchise specific basis. The new InterCity West Coast franchise will contain an adjustment mechanism linked to fluctuations in GDP growth which cushion the franchisee against a major downturn in revenue due to exogenous economic factors (in return for a share for the Department of the potential upside)

31. Franchises let between 2004 and 2009 (template Franchise Agreement) contain Revenue risk sharing mechanisms which offer protection post year 4 if revenue fails to reach target level for any reason.
32. The Department will consider (with no presumption that it will accept and subject to state aid rules) requests for additional support from franchisees who are on franchises let pre 2004, but would have received protection from the revenue-risk sharing mechanisms, or been able to make a force majeure claim if they had been on a post 2004 (tFA) a contract. This recognises that there may be exceptional circumstances, for example a large and widespread downturn in demand, where it might be wrong to penalise the franchisee and where wholesale use of the OOLR mechanism would be impracticable and damaging to the market. However, these exceptional circumstances aside, the Department will insist that a franchisee which is unable to operate to the price it bid should surrender the franchise. The Department will therefore hold franchisees to the terms of their contracts. Where an event of default occurs which leads to termination, the Department also reserves the right to trigger the cross-default mechanism in franchise contracts, under which termination of a franchisee may bring about a termination of other franchise agreements to which the franchisee or an affiliate company is a franchisee.

The roles of Ministers and officials

33. The Secretary of State wishes to maintain a clear distinction between the decisions which Ministers will take and those which are delegated to officials within the Department.
34. Ministers need to balance the sometimes conflicting claims of affordability, VfM, wider objectives and the requirements of different users of the railway. The Secretary of State will decide what passenger services to secure from each franchise and will approve the base service specification (see paragraph 12). They may also decide which priced options and bidder-generated options to accept.
35. Ministers also need to be satisfied that the overall franchise-letting and management processes are fit for purpose, and that these should produce the required contracted outcomes on behalf of the passenger and tax-payer.

36. However, Ministers do not wish or need to be involved in the procurement commercial decisions, including the pre-qualification of bidders, the award of contracts, or the day to day management of contracts. These will be handled on their behalf by officials.
37. Within the Department a designated committee of senior officials, the Contract Award Committee (CAC), take the decisions on selecting those suppliers who are invited to tender, and subsequently, the winning bid. During this process the names of bidders are anonymised, i.e. the members of the CAC do not know the identities of the bidders whose scores and risk-assessments are presented. The CAC gives confirmation to the Board Investment and Commercial Sub-Committee, chaired by a Director General, that they are content that the selection process has been compliant. The CAC also seek confirmation from the Sub-Committee, the Secretary of State and HM Treasury that the 'base service specification' remains affordable and VfM, and seek Ministers decisions on whether to take up the winning bidder's priced options and bidder-generated options.
38. Contractual agreement with the bidder occurs the day before the intention to award is announced to the financial markets and to Parliament. It is only at this stage that the identity of the winning bidder is disclosed to Ministers and senior officials. Formal signing of the contract will normally take place following successful conclusion of a voluntary 10 day standstill period.

Procurement transparency and commercial confidentiality

39. The Department intends to make the franchise letting process as transparent as possible, hence the decision to publish this guide. The Department will also publish the ITT, information on the price offered by the winning bidder and the reliability and other improvements to which that bidder is contractually committed. Both passengers and taxpayers are entitled to know what has been purchased on their behalf. The Franchise Agreements will be made available on the Public Register.
40. However, the Department also regards commercial confidentiality as essential. It cannot secure the best deal for passengers and taxpayers unless it can operate a commercially confidential procurement process. The Department therefore insists that bidders do not discuss with anyone the details of their bid or their discussions with the Department or their views on the progression of the procurement. Within the constraints of the Freedom of Information Act and the exclusions provided within the Act the Department will not release information on the bids, other than that required by third parties supporting the Department in undertaking the procurement.

Franchise-letting timetable

41. The Department will set a timetable for letting franchise contracts, which builds in sufficient time (not less than three months) for the incoming franchisee to manage an

orderly mobilisation before the contracted operations begin.

Legal Disclaimer. The information and advice in this Guide are not intended to be a comprehensive summary, nor to provide legal advice, and should not be relied upon or treated as a substitute for specific franchise replacement instructions contained in the PIN, Pre-Qualification document pack or ITT issued to bidders, or any other franchise specific information released by the Department from time to time as part of the franchise procurement process. For the avoidance of doubt, this Guide is not a statement of policy about how the Secretary of State proposes to select the person who is to be the franchisee in relation to a franchise agreement, as described in Section 26(4A) of the Railways Act 1993, as amended.