

FirstGroup's bus undertakings

Introduction

1. This appendix outlines the behavioural undertakings FirstGroup gave to the Secretary of State about many of its bus services in Scotland following its acquisition of SB Holdings Limited (SBH). These undertakings affect its bus operations in Glasgow and central and southeast Scotland, excluding the City of Edinburgh; they were accepted by the then Competition Minister on 17 January 2002.

Background

2. FirstGroup acquired SBH in June 1996. The acquisition was referred to the MMC which recommended that FirstGroup should divest certain activities to a single buyer. These were its Falkirk-based Midland Bluebird subsidiary and one of SBH's four Glasgow depots, together with routes spread reasonably over Glasgow representing at least 20 per cent of SBH's turnover and a bus fleet appropriate to serve these routes. This recommendation was accepted by the OFT and the Secretary of State subject to a slight change regarding Glasgow where FirstGroup was required to divest any one of its four depots together with the routes operated from that depot.
3. Following the May 1997 general election, FirstGroup requested a review of these remedies on the grounds that Stagecoach had entered the Glasgow market in direct contradiction, it considered, to the evidence that it had given to the MMC. After a review, the OFT recommended that FirstGroup should still be required to divest the Midland Bluebird business but that there was no longer a need to dispose of the Glasgow depot and routes. The Secretary of State announced in July 1998 that she accepted there had been changes in the Glasgow bus market since the MMC report. She said that Stagecoach's entry had demonstrated that competition was possible in the relevant market and divestment was no longer necessary. Nonetheless concerns remained that the scale and dominance of FirstGroup, following the merger, might deter entry. The Secretary of State therefore decided to seek a package of behavioural undertakings that would (a) prevent FirstGroup from exploiting its market power by raising prices and reducing its level of services; and (b) protect new entrants by restricting changes in fares, frequencies, journey intervals and tendered services. The OFT subsequently negotiated undertakings with FirstGroup.

The undertakings

4. The two main elements of the undertakings are (a) a fare cap and (b) restrictions on FirstGroup's ability to reduce levels of service or respond to entry by competitors on its routes.
5. The undertakings apply to two distinct geographical areas defined as (a) the FirstGroup Glasgow operating area¹ and (b) the Midland Bluebird and Lowland operating area (broadly central and south-east Scotland, excluding the City of Edinburgh).² The fare cap applies to all FirstGroup's operations within both operating

¹The unitary authority areas of the City of Glasgow, North Lanarkshire, South Lanarkshire, East Dunbartonshire, West Dunbartonshire and East Renfrewshire.

²The unitary authority areas of Stirling, Falkirk, Clackmannanshire, West Lothian, Midlothian, East Lothian and the Scottish Borders.

areas. The other restrictions only apply to all FirstGroup's operations within the Midland Bluebird and Lowland operating area. (As the OFT was not certain that Stagecoach would remain in the Glasgow market or that future competition there would be effective, the fare controls covered both areas. The OFT did not, however, require anti-predation undertakings covering Glasgow, given the Secretary of State's view that it was a contestable market.)

The fare cap

6. The fare cap limits FirstGroup's ability to raise fares in both areas by applying restrictions to a basket of fares. It has two parts: a fare freeze for two years (which has now expired) followed by a requirement that the annual percentage increase across the basket of fares will not exceed the change in the RPI in the preceding year.
7. As fares and fare structures differ between FirstGroup's operations in east and west Scotland, separate fare baskets are defined for the two areas. Within the FirstGroup Glasgow operating area, the fares included are all those that FirstGroup charged on 1 September 1997. Within the Midland Bluebird and Lowland operating area the base date is 1 February 1998. The fare baskets do not include tendered, concessionary, multi-operator or discounted fares or ticket types, such as Firstday and Firstweek that were introduced after the undertakings were entered into.
8. For both fare baskets, each fare type included is weighted according to the number of passengers purchasing it over a specified sample period and the total weighted revenue is calculated. FirstGroup may increase or decrease each of the fare values in any given year, provided that the total weighted revenue that would be generated by the same weighted sample does not increase by more than the percentage change in the RPI in the preceding year. FirstGroup's ability to withdraw any fare type (for example, the 'three stages adult single') is restricted. It is required to apply the relevant regulated fares on any new service introduced within either operating area.
9. Thus there is no direct limit (other than the maximum fare cap itself) on the price that FirstGroup may charge for any particular fare. Any significant increase in a particular type of fare is, however, likely to affect the other fares within the basket by limiting any increase in them or requiring reductions.
10. The fare cap is supported by undertakings not to change (without the OFT's consent) a range of related matters including fare stages and zones, peak fare periods and their terms and conditions. FirstGroup also has to provide the OFT with fare tables for a sample of routes specified by the OFT and spreadsheets demonstrating compliance with the fare cap each year.

Anti-predation undertakings

11. All the anti-predation undertakings outlined in paragraphs 12 to 16 apply only within the Midland Bluebird and Lowland operating area.

Fares and frequencies

12. Where FirstGroup either sets fares lower, or operates services at higher frequencies, than a competing operator's service and, as a result, the competing service ceases to operate before January 2005, then (for a period of three years from the date on which the competitor gives notice that the competing service will be deregistered) FirstGroup must not without the OFT's consent:

- (a) charge any fare on the services that competed with the competitor's service which exceeds the lowest fare charged by it after the competitor registered its service; or
- (b) reduce the frequency of the services that competed with the competitor's service below the highest frequency operated by FirstGroup after the competitor registered its service.

Even spacing of services

- 13. FirstGroup must ensure that any new commercial bus services operated by it are evenly spaced between those of any competitor.

Tendered services

- 14. FirstGroup is prevented from operating any new commercial service, or increasing the frequency of any existing commercial services, in competition with a tendered service for which it has bid unsuccessfully.

Maintaining mileage operated

- 15. Finally, FirstGroup must not reduce the registered commercial mileage it operates in the area to less than 95 per cent of that at January 2002.
- 16. FirstGroup is still able to reduce the mileage operated on some services or even close them, provided that the overall total satisfies the required limit. A significant redeployment of buses between routes would therefore be possible. The size of buses operated could also be changed.

Duration of undertakings

- 17. FirstGroup told us that it had applied the principles underlying the undertakings since 1 September 1997 within the First Glasgow operating area and since 1 February 1998 within the Midland Bluebird and Lowland area. With the exception of the anti-predation undertaking referred to in paragraph 12, the undertakings are unlimited in duration.
- 18. On 3 September 2003, FirstGroup asked the OFT to review the undertakings. The OFT is, however, awaiting the outcome of this inquiry before commencing its review.