The Sale of London Transport's Bus Operating Companies
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This report has been prepared under Section 6 of the National Audit Act 1983 for presentation to the House of Commons in accordance with Section 9 of the Act.

John Bourn
Comptroller and Auditor General

National Audit Office
17 November 1995

The Comptroller and Auditor General is the head of the National Audit Office employing some 750 staff. He, and the NAO, are totally independent of Government. He certifies the accounts of all Government departments and a wide range of other public sector bodies; and he has statutory authority to report to Parliament on the economy, efficiency and effectiveness with which departments and other bodies have used their resources.
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Introduction, summary and conclusions

1 Between September 1994 and January 1995, London Transport sold their ten bus operating companies. Gross proceeds from the sale totalled £233 million. Excluding VAT and internal project costs, London Transport incurred costs of some £9.7 million and the Department of Transport costs of some £719,000 (Figure 1).

2 The sale was conducted under the provisions of the London Regional Transport Act 1984. Ministers set the sale objectives and gave London Transport guidance on the conduct of the sale. London Transport prepared the companies for sale and sold them, subject to approval by the Secretary of State.

Objectives of the sale

3 The Department set London Transport the following objectives:

- to manage the privatisation so as to promote sustained and fair competition in the provision of bus services in London;

- to complete the privatisation process, if practicable, by 31 December 1994;

- to provide an opportunity for the management and staff to take a stake in the privatised companies; and

- subject to the achievement of the first three objectives, to maximise as far as practicable the net proceeds of privatisation.

Sale announcements

4 The Secretary of State announced the sale in December 1992 and set a target to complete it by September 1994. At that time the Secretary of State said he expected to deregulate London’s bus services shortly after the sale. In November 1993, however, the Government postponed deregulation of London’s bus services in the current Parliament. This decision led to further work and the target to complete the sale was extended to December 1994.
The Sale of London Transport’s
Bus Operating Companies

Scope of the National Audit Office examination

5 The National Audit Office examined whether the Department and London Transport achieved the sale objectives. This report is based on an examination of the Department’s papers and discussions with their staff and their financial advisers, Price Waterhouse. London Transport and their financial advisers, BZW, and other parties involved in the sale, were also consulted.

6 The National Audit Office have no direct access rights to the papers and officials of London Transport other than information held by the Department. The National Audit Office are grateful for the assistance provided by the Department, London Transport and other parties in producing this report.

7 A map of the operating areas of the ten companies and their garages is at Appendix 1. A chronology of the main events in the sale is at Appendix 2.

Conclusions

8 The National Audit Office concluded that the Department and London Transport achieved the sale objectives. No purchaser achieved more than a 25 per cent share of the London bus market. The Department and London Transport completed the sale virtually on target and successfully promoted employee participation in the sale. Four of the ten companies were purchased by management and employee teams.

9 At £233 million, gross proceeds were substantially higher than expected. A high level of interest was generated by London Transport’s marketing campaign and some bidders were more optimistic than expected about the prospects for their targeted business. London Transport, the Department and their respective advisers successfully devised a bidding process which took advantage of this. They generated substantial bidding competition and obtained final prices which were some £30 million higher than the eventual purchasers’ initial indicative bids and some £70 million higher than the mean of all indicative bids.

10 Both London Transport and the Department controlled their advisory costs by agreeing work requirements and related costs with their advisers and monitoring outturn against budgetary targets. As a result of the decision to postpone deregulation in November 1993, London Transport absorbed unanticipated costs of more than £0.5 million. They exceeded a revised budget of £7.25 million by £2.1 million, largely as a result of a higher than expected success fee payment to their financial adviser. The success fee was higher because as noted above proceeds were much higher than expected.
Overall, the sale was managed effectively. London Transport and the Department took account of best practice from previous sales and the recommendations of the Committee of Public Accounts. For example, they set clear sale objectives, clearly defined responsibilities, established a project steering group and project director, introduced clawback arrangements on property and commissioned a benchmark valuation.

**Points to consider in future sales**

The National Audit Office consider that three main points arise for consideration by departments in future sales. These concern the purpose of a benchmark valuation, the use of a success fee and a department’s role in decisions on the privatisation costs of other public sector vendors. Corporate Valuations and Pannell Kerr Forster assisted the National Audit Office in examining the benchmark valuation and its use in the success fee arrangement in this sale.

**Point 1 The purpose of a benchmark valuation**

a) Vendors must be clear about the purpose of a benchmark valuation, particularly where it may be used, as in this sale, as a reference point for a success fee arrangement. In this sale, the valuation (£112 million to £154 million) was intended to provide an indication of the level of proceeds below which the vendor should consider carefully whether to continue with the sale. It did not set out to estimate most likely proceeds. The valuation was based on conservative assumptions and excluded market factors specific to particular bidders such as their willingness to offer a higher price for strategic reasons, as appears to have occurred in this sale. The National Audit Office believe that the instructions to the valuer and the valuation report could have more clearly separated out and presented the message that the valuation was not intended to be an estimate of likely proceeds. London Transport, the Department and their advisers maintained that they all clearly understood the purpose of the benchmark valuation in this sale but agreed that it is important that vendors clearly specify their requirements and the valuation report sets out the basis of the report clearly.

*In commissioning benchmark valuations, vendors should clearly specify the purpose of the valuation which they require particularly as regards whether the valuation is an estimate of likely proceeds or an estimate of the level of proceeds below which the vendor should consider carefully whether to continue with the sale. This distinction should also be clearly drawn out in the valuation report.*
Point 2 Success fee arrangements

b) In accordance with usual practice, London Transport’s financial adviser carried out the benchmark valuation at the vendor’s request. The Department’s adviser co-operated in aspects of the work and endorsed the valuation. London Transport and their adviser also agreed that the valuation should be used as the reference point for a success fee arrangement. The Department and their adviser were, however, unaware of this and therefore unable to comment on the use of the valuation in this way. In the event, because proceeds were higher than expected the size of the fee also exceeded expectations and London Transport and their adviser reached a negotiated settlement. The National Audit Office believe this demonstrates that there are clear risks in linking success fees to benchmark valuations as these may focus on a vendor’s minimum expectations and will not necessarily reflect best estimates of likely proceeds.

Where success fees are deemed of value in a sale, vendors should consider carefully the risks involved in linking them to benchmark valuations. In particular, in setting thresholds which trigger success fee payments, they should seek to ensure:

i) that the valuations used reflect best estimates of likely proceeds rather than lower benchmarks; and

ii) that consideration is given to the need for endorsement by an independent party aware of all the purposes of the valuation, including any link to success fees.

Point 3 Departments’ role in decisions on the privatisation costs of other public sector vendors

c) London Transport, as a nationalised industry, are responsible for the commercial management of their own operations. They therefore met their own costs of sale. The Department required them to remit gross proceeds to the Exchequer with an adjustment for the effects of an incentive arrangement but without deducting their costs of sale. They therefore had an incentive to minimise costs. The Department did not seek to become involved in detailed control of London Transport’s costs although they monitored these costs against budgets. Although unaware of London Transport’s success fee arrangement until late in the sale, the Department consider that they would nevertheless not have intervened in its agreement if they had known. The National Audit Office consider, however, that given
that the success fee could have had a material impact on the Department's objective to maximise net proceeds there may have been benefit in the Department being aware of the arrangement before it was agreed and offering a view on the arrangement if necessary.

Where privatisations are handled by nationalised industries or other public sector businesses, departments should consider the case for ensuring that they are made aware of all factors, such as success fee arrangements, that may have a material impact on the achievement of the sale objectives and should be prepared to offer a view on them if necessary.

Structure of this report

13 Part 1 of this report examines how the Department and London Transport sought to promote sustained and fair competition in the sale. Part 2 examines sale completion, employee participation and proceeds. Part 3 examines the costs of sale.
1. Promoting sustained and fair competition

1.1 The objective to promote sustained and fair competition required London Transport to sell companies that were financially sound and able to compete with, but not dominate, their competitors. The achievement of this objective had to take account of:

- the Government's decision to privatise the companies before deregulation of the London bus market;

- the Government's later decision in November 1993 to postpone their original aim to deregulate the market within the current Parliament; and

- the existence of a competitive tendering programme for London Transport bus routes, which had been introduced by London Transport in 1985.

1.2 The decision to privatise the companies before deregulation required London Transport to put all the companies' bus routes on a contractual basis. When the Department announced the sale, in December 1992, they then expected London Transport to sell the companies into a market based on contracts with the privatised companies (and other operators) for all of London Transport's bus routes. This was expected to operate briefly, enabling purchasers to obtain experience of managing the newly privatised companies and their routes before deregulation.

1.3 The decision to postpone deregulation meant that the Department had to consider London Transport's post-sale regulatory role. In particular, the decision required the creation of a long-term contract tendering regime. The Department aimed to promote sustained and fair competition, within a competitive tendering environment after the sale, by building on London Transport's existing competitive tendering programme for route contracts.
1.4 This part of the report shows how the Department and London Transport set out to promote sustained and fair competition, within a post-sale market regulated by London Transport on the basis of a competitive tendering programme for route contracts. It shows in particular that:

**London Transport**

- put all the companies' then so far untendered routes (some 60 per cent of the London Transport route network) on a contractual basis by March 1993;

- in doing so, achieved wider aims:

  i) they were able to improve the cost structure of the companies in line with savings achieved in recent route tendering exercises; and

  ii) introduced net cost contracts designed to provide incentives for operators to improve services;

**the Department**

- approved the sale of the companies on the basis of the existing structure of the companies which had been created in 1989 with a view to their privatisation;

- with the involvement of the Office of Fair Trading, set market share and other ownership limits which successfully prevented monopoly ownership through acquisition in the sale (three major bus operators entered the London bus market which comprised 30 competitors after the sale, none of which achieved more than a 25 per cent share of the market); and

- approved the creation of a route tendering programme which requires London Transport to retender routes on a five year cycle (more frequently if operators fail to meet quality standards).

**Contracts for untendered routes**

1.5 London Transport began to consider the nature of the contracts for untendered routes in October 1992. Negotiations with the companies began in February 1993. At that time, of the 40 per cent of London Transport’s bus network already subject to competitive tendering, private contractors had won 37.5 per cent of the routes representing 15 per cent of all routes.
1.6 An alternative to negotiating contracts was to put all the untendered routes out to tender. This was rejected as impractical because:

a) the market could not have absorbed so many routes so quickly and competitive tendering on such a scale would have imposed a high administrative burden on London Transport;

b) London Transport would have incurred redundancy costs for company employees employed on routes won by the private sector; and

c) the market share of the companies would have been reduced eroding the likely proceeds of privatisation.

1.7 The Department required London Transport to:

- complete negotiations and agree contracts with the companies by March 1993;

- negotiate contracts against stated cost reduction targets (with a minimum five per cent of the routes put out to competitive tender); and

- agree net cost contracts, rather than gross cost contracts (hitherto in place on all tendered routes).

Timing of negotiations

1.8 In October 1992, the Department had planned to deregulate the market, subject to the necessary legislation, in 1995. To allow purchasers a year to prepare for deregulation after the sale and meet that deadline meant that the sales had to be completed in 1994. To meet that target, London Transport had to negotiate contracts for the untendered routes by March 1993, so that a full year’s financial results with those contracts could be made available to potential purchasers before the sale. Contracts were negotiated by that date.

Cost reduction targets

1.9 The Department required London Transport to negotiate contracts against cost reduction targets based on savings achieved in recent route tendering exercises. In addition, irrespective of success in negotiations to reduce costs London Transport were also required to put routes representing at least five per cent of the total network out to competitive tender.
1.10 Negotiations between London Transport and the companies met the cost reduction targets for all except 26 of the untendered routes. They were successful in this because the companies were generally able to obtain staff acceptance of reduced terms and conditions of employment in return for a compensation package. London Transport spent £38 million in compensation for changes in pay and conditions for operating staff and £4.7 million on voluntary redundancy for operating and engineering staff in 1992-93. As a result, London Transport reduced their annual contract costs by £20 million a year.

1.11 The 26 routes on which London Transport and the companies failed to reach agreement on cost reductions, together with two other routes jointly operated by more than one company, were put out to tender to meet the minimum five per cent target. Of these routes, the companies lost 15 to private operators, retained eight, and five changed hands between the companies. This outcome reduced London Transport's annual contract costs by a further £6 million at a one-off redundancy cost of £14 million.

**Gross and net cost contracts**

1.12 All routes previously subject to contract with London Transport through the competitive tendering programme were operated on a gross cost basis. Under gross cost contracts London Transport pay the operator a fixed rate for operating the route (less certain deductions, if they apply) and take all of the revenue. The main drawback to this arrangement is that there is no incentive for operators to increase revenue or improve quality of service.

1.13 To remedy this London Transport negotiated net cost contracts for all of the companies’ previously untendered routes. Under net cost contracts, London Transport pay (or receive from) the operator a settlement figure representing the difference between the operator’s projected costs and revenue. The operator keeps all on-bus revenue (net of certain deductions, if they apply) and is allocated a share of off-bus revenue (derived mainly from Travelcard use).

1.14 London Transport plan to put all route contracts due to be retendered from April 1997 on a net cost basis, reflecting the expected development of electronic ticketing to ensure greater accuracy in allocating off-bus revenue.

**Company structure and ownership**

1.15 The Department considered that sustained and fair competition would best be achieved by privatising the existing companies. The companies had been incorporated in 1988 and commenced trading
in April 1989 with a view to their future privatisation. None presented monopoly threats within the London market and all were judged to be potentially sustainable as independent entities in the medium to longer term. To prevent monopoly ownership arising through acquisition in the sale, the Department provided London Transport with guidance on ownership restrictions to be applied in approving bids.

Ownership restrictions

1.16 Following consultation with the Office of Fair Trading, the Department decided that potential purchasers should be allowed to bid for as many companies as they wished, subject to the following safeguards against monopoly ownership:

- purchasers should not generally be permitted to acquire a company or combination of companies if that increased their share of scheduled route mileage in London to more than 25 per cent;

- purchasers should not generally be permitted to buy adjacent companies; and

- the competition implications of a purchase in an area where the purchaser already had a significant presence (including in adjacent areas of the deregulated market outside London) should be discussed by the potential purchaser with the Office of Fair Trading.

1.17 London Transport made these guidelines clear to potential purchasers in a procedures letter inviting indicative bids. They also listed which companies were considered to be adjacent. No buyer gained control of more than 25 per cent of scheduled mileage. Figure 2 opposite shows the market share gained by each purchaser.

Future route tendering

1.18 London Transport, at Group level, are responsible for setting fare levels for bus services. Through London Transport Buses, a newly created body, they are also responsible for setting quality and service requirements for bus services and for managing the route tendering programme (see Appendix 3). They plan to put routes representing 15 per cent of scheduled mileage out to tender by April 1997, and all routes out to tender by March 2001. Contracts will be for a period of up to five years so tendering will be continuous, and will only be discontinued if the market is deregulated.
### Figure 2: Purchasers' market share after privatisation

<table>
<thead>
<tr>
<th>Purchaser</th>
<th>Company</th>
<th>Sale completion date</th>
<th>Market share as a percentage of scheduled mileage as at November 1994</th>
</tr>
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<tbody>
<tr>
<td>Stagecoach</td>
<td>East</td>
<td>6.9.94</td>
<td>10.1</td>
</tr>
<tr>
<td></td>
<td>Selkent</td>
<td>6.9.94</td>
<td>6.7</td>
</tr>
<tr>
<td>Cowie 1</td>
<td>Leasey</td>
<td>29.9.94</td>
<td>8.1</td>
</tr>
<tr>
<td></td>
<td>South</td>
<td>10.1.95</td>
<td>6.3</td>
</tr>
<tr>
<td>Go-Ahead</td>
<td>Central</td>
<td>17.10.94</td>
<td>7.9</td>
</tr>
<tr>
<td>MTL</td>
<td>Northern</td>
<td>26.10.94</td>
<td>5.1</td>
</tr>
<tr>
<td>Mebo 2</td>
<td>General</td>
<td>2.11.94</td>
<td>9.3</td>
</tr>
<tr>
<td>Mebo</td>
<td>United</td>
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<tr>
<td>Mebo</td>
<td>Metroline</td>
<td>7.10.94</td>
<td>5.6</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>74.2</td>
</tr>
</tbody>
</table>

Source: London Transport

**Notes:**
1. Only Cowie operated tendered routes in London prior to the sale having a market share of 2.6 per cent. Their market share after the sale was 17 per cent. 22 operators run the remaining route mileage.

1.19 London Transport published a tendering programme for all routes for the years 1995-2001 in the Information Memorandum for the sale. They will promote sustained and fair competition through route tendering in accordance with this programme.

1.20 Under the Fair Trading Act 1973 the Office of Fair Trading has the power to examine mergers that result in any single company obtaining control of more than 25 per cent of scheduled mileage within London, or within a particular area within London (or within a particular area within London and the adjacent deregulated market) constituting a "substantial part" of the United Kingdom for the purposes of the Act. The Director General of Fair Trading may advise the Secretary of State for Trade and Industry to refer a merger to the Monopolies and Mergers Commission for investigation.
2. Sale completion, employee participation and proceeds

2.1 This part of the report deals with the achievement of the Department's sale completion, employee participation and proceeds objectives. It shows that London Transport:

- completed the privatisation virtually on target;

- provided an opportunity for the management and staff to take a stake in the privatised companies; and

- took steps to maximise proceeds (the control of the costs of sale is considered separately in Part 3).

2.2 In particular, this part of the report shows that:

the Department

- set London Transport a demanding target for sale completion which they virtually achieved;

- in recognition of the contribution to improvements in financial performance and quality of service by management and employees, approved the extension of a limited price preference and financial support to management and employee bids (which helped promote bids for all ten companies, including four successful bids);

- approved sales following careful review of the case made for each sale by London Transport;

London Transport

- in preparing the companies for sale:

  i) took account of advice requested from the Department on the handling of pensions provisions;
ii) retained inessential properties for sale or redevelopment within London Transport's general property portfolio;

iii) with the aim of maximising proceeds in the sale, transferred surpluses on distributable reserves of £7.2 million from seven of the companies and eliminated deficits of £11.7 million in three of the companies, and retained capital allowances rather than sell them with the companies;

iv) indemnified purchasers against an estimated liability of some £20 million for personal injury and damage to property prior to 30.6.94 and put in place insurance arrangements which helped management and employee bidders to compete in the sale;

• in selling the companies:

i) devised a marketing programme and a bidding process which generated substantial interest and price tension throughout the sale;

ii) obtained 102 indicative bids ranging in total from £104.9 million to £224.3 million with a mean price of £164 million; and

iii) conducted negotiations with final bidders in a way which led to final prices some £30 million higher than the eventual purchasers' indicative bids (aggregate proceeds represented some 60 per cent of the companies' turnover, which was some ten per cent higher than the average ratio in recent bus company sales outside London).

Target date for completion

2.3 The Department originally set a completion target of 30 September 1994, to allow purchasers of the companies as much time as possible to prepare for a deregulated market in London, then expected to be introduced in 1995. The decision to postpone deregulation in November 1993 required a three month extension to 31 December 1994, to allow time to agree London Transport's future role and the nature of future route tendering in London. The companies also had to re-work their business plans.

2.4 London Transport met the completion target completing four of the sales even before the original target date. The last sale was approved by the Secretary of State and the terms contractually
agreed in December 1994. That sale was completed on 10 January 1995 after the successful completion of a rights issue by the purchaser (Figure 2).

2.5 Ministers decided to give management and employees an opportunity to participate in the sale in recognition of their contribution to improvements in financial performance and quality of service. They considered, however, that without experience of management in the private sector, management and employees might find greater difficulty than private sector bidders in raising finance and be discouraged by the financial commitment involved in preparing a bid. They therefore agreed that London Transport should offer management and employees a limited price preference in the sale and financial support to encourage them to bid.

2.6 London Transport gave management and employee bidders a pre-announced price preference of up to five per cent over other bidders. This meant that if a management and employee bid was at least 95 per cent of the value of the highest offer, and provided the bid was no less favourable in other respects, the lower management and employee bid would be accepted. London Transport also gave unsuccessful management and employee teams financial support of up to £72,000 on a staged basis (including VAT) for the costs of mounting an unsuccessful bid.

2.7 Both forms of assistance were only available in respect of bids by management and employees for their own company, and were limited to only one management and employee bid within a company. In addition London Transport agreed to provide the assistance only if they were satisfied that the management and employee plans were robust.

2.8 Management and employee teams submitted indicative bids for all of the companies. One team bid for two other companies and two bid for four others. Four teams were successful in buying their own companies. Three of the trade buyers proposed that staff would be eligible to participate in their share option schemes. The fourth proposed to make 20 per cent of the shares in their purchase available to staff.

Pensions

2.9 In response to a request by London Transport, the Department provided guidance to cover:

- future benefits provided by successor schemes to the London Transport scheme; and
- preservation or transfer of accrued pension benefits.

**Future benefits**

2.10 The sale of the companies meant that staff would cease to be active members of the London Transport pension scheme. The Department advised London Transport that purchasers should seek to provide pension benefits for future service which were broadly comparable with those in the London Transport scheme. Social security legislation is uncertain whether and how far successor schemes should match benefits provided in the schemes of purchased companies.

2.11 The Department regarded the demonstration of broad comparability and agreement to specific terms of successor schemes as a responsibility of purchasers. They accordingly advised London Transport to put the onus firmly on purchasers to demonstrate to staff that successor schemes were broadly comparable to the London Transport scheme or otherwise compensate staff for reduced benefits. London Transport advised bidders of their responsibilities in this respect in the procedures letter inviting indicative bids.

2.12 Throughout the sale, London Transport also reminded bidders of the need to take account of staff views. They allowed purchasers, if they wished, to remain in the London Transport scheme for an interim period of up to six months after privatisation. This was intended to allow purchasers time to negotiate detailed pension arrangements with employees, and establish any new pension scheme. Three purchasers took up this option.

2.13 London Transport offered purchasers no indemnities against potential claims for constructive dismissal. During the sale London Transport persuaded some purchasers to improve their pension proposals.

2.14 As the onus was on purchasers to demonstrate to staff the broad comparability of their proposals, neither the Department nor London Transport undertook an actuarial review of purchasers’ schemes. The Secretary of State nevertheless took into account the proposal on pension provision in approving each sale.
Accrued pension rights

2.15 London Transport offered members of the London Transport scheme the following options to preserve or transfer their accrued pension entitlements:

a) to transfer them to their new employer's scheme;

b) to transfer them to a personal pension plan;

c) to leave their accrued rights in the London Transport scheme with entitlement to a deferred pension;

d) if aged 50 or over, to exchange a deferred pension for an immediate pension (reduced for early payment if aged below 60); or

e) if membership was less than two years, to have their employee contributions refunded.

2.16 These options accorded with the requirements of social security legislation. Where a member opted for a pensions transfer, London Transport agreed to transfer pension rights on a basis allowing accrued benefits to be uprated in line with increases in an individual's future earnings thus maintaining final salary linkage on the accrued benefit.

Asset transfer

2.17 Before selling the companies, ownership of the assets used by the companies was formally transferred to them. Completed in December 1993, this involved the transfer from London Transport to the companies of title to operating properties, buses and other assets, at a balance sheet value of £152.32 million, in exchange for shares and debt.

2.18 Certain properties, no longer essential to the businesses, were retained for sale or redevelopment within London Transport's general property portfolio. Receipts from the sale of these properties will be retained by London Transport and not counted as privatisation proceeds.

Distributable reserves and capital allowances

2.19 In March 1994, London Transport transferred surpluses on distributable reserves of £7.2 million from seven of the companies and eliminated deficits of £11.7 million in three of the companies. This step aimed to maximise proceeds in the sale. London Transport judged that purchasers would be unlikely to recognise the full value...
of any surplus on distributable reserves in bids for the companies and that they would heavily discount bids for companies with deficits.

2.20 Capital allowances were not sold with the companies. London Transport considered that although purchasers would be prepared to increase their bids if allowances were included (as they would be able to offset them against tax liabilities) the increase was unlikely to represent the full value of the allowances. The value of tax foregone by the Exchequer would, therefore, be greater than any increase in proceeds.

**Insurance arrangements**

2.21 In recognition of an estimated liability of some £20 million for claims arising from injury to people and damage to property in relation to bus operations up to 30.6.94, London Transport announced before the sale that they would indemnify purchasers against these claims. Because of the high cost of insurance for future claims (in a contracting market for its provision), London Transport also set up and sold the companies with cover provided through a captive insurance company owned jointly by all ten companies.

2.22 The ten companies each contributed £100,000 to set up an insurance fund and were obliged to insure with the insurance company for at least three years. London Transport considered that this action protected the interests of management and employee bidders and a number of trade bidders in the sale (though not necessarily large trade bidders who may have been able to integrate the companies into their existing insurance arrangements). If they could not obtain commercial cover, the companies could only have obtained self insurance secured by a bond at a cost of £500,000.

**Marketing the companies**

2.23 Marketing of the companies effectively began in June 1993 with the wide distribution of a booklet, “London Buses - The Road to Privatisation”. Following this, London Transport obtained 304 pre-registrants for the sale. Later in 1993, London Transport held market testing meetings with major trade purchasers, management teams, and operators already running contracted services.

2.24 After the official launch of the sale in March 1994, London Transport required interested parties to pre-qualify before receiving a copy of the information memorandum, a draft sale and purchase agreement and a procedures letter. Pre-qualification required bidders to submit outline information about themselves and a non-returnable payment of £250. 43 applicants pre-qualified.
Selling the companies

2.25 The sale itself was conducted in several bidding stages:

- indicative bids, which were required by 27 May 1994;

- interim bids, which were required in two tranches for separate groups of the companies by 26 June and 6 July respectively; and

- final bids, which were again required in two tranches by 4 and 11 August respectively.

2.26 The bidding stages were followed by the appointment of preferred bidders, final negotiations and formal completion. Three bidders (following interim bids) and one (following final bids), were appointed preferred bidders (for five of the companies) on payment of exclusivity premiums. The ability of London Transport to obtain the agreement of these bidders to pay such premiums reflects effective management of the bidding process. Proceeds substantially exceeded bids by the eventual purchasers at indicative stages.

Indicative bidding

2.27 Figure 3 shows the number of indicative bids for each company. These bids were based on the information provided in the information memorandum. In total 10 management and employee and 12 trade bidders submitted 102 indicative bids ranging in total from £104.9 million to £224.3 million with a mean price of £164 million. The considerable strength of indicative demand enabled London Transport to change plans to move directly to final bidding. They instead introduced an interim bidding stage, thus enhancing their prospects of exploiting competition in the sale.

Interim bidding

2.28 At interim bidding stage, London Transport encouraged bidders to improve their bids, on the basis of limited access to further information about the companies, in two separate bidding tranches. The first tranche of bids comprised bids for the five companies with some of the strongest indicative bidding lists. The second tranche comprised bids for the remaining five companies.

2.29 London Transport reasoned that offering the companies in two tranches would strengthen bidding, particularly for those companies in the second tranche. Bidders who failed to secure their target companies in the first tranche could be expected to strengthen bids in their efforts to ensure success in the second tranche.
2.30 This resulted in 57 interim bids, on average 20 per cent higher than indicative bids. Of these, 35 derived from five trade bidders and one management and employee bidder, who each bid for four or more companies. Following the interim bidding stage, the leading bidders for three companies were judged to be sufficiently better than competitors to be appointed directly as preferred bidders to complete these sales. In each case, London Transport, with the Department's agreement, obtained a price premium before going ahead with exclusive negotiations. In total, these premiums amounted to £2.5 million.

Final bidding

2.31 London Transport shortlisted between two and four bidders for each of the remaining seven companies. These bidders were invited to submit final bids following:

- meetings with company management and, separately, employee representatives;

- site visits to inspect the properties and assets of the companies; and

- further enquiries, including the review of detailed information on the companies in specially created data rooms.

2.32 London Transport sat in on bidders' meetings with management to ensure that a consistent and fair representation was made to each bidder. Trades union and employee representatives had the opportunity to listen to an explanation by each bidder of their plans for the employees of the company but not to negotiate with them. Management and employee teams were precluded from conducting site visits.

2.33 Following final bids, London Transport invited seven preferred bidders to complete these sales. Stagecoach offered a premium, which was accepted, if they were chosen as preferred bidders on the sales of both East London and Selkent. Both the London Northern and South London sales required further rounds of bidding.

London Northern

2.34 The highest bid for London Northern was very close to the management and employee bid after their price preference had been taken into account. Given the closeness of the bids the
Department approved another round of bidding, at which point the winning bid, by MTL, was clearly better than that of the management and employee team.

South London

2.35 The management and employee team were selected as preferred bidders in South London. However, in August 1994 the Traffic Commissioner for the South Eastern and Metropolitan Traffic Area announced a public enquiry into the company's maintenance record. In October 1994, before completion of the sale, the management and employee team declared that their offer would be dependent on the outcome of the public enquiry and much reduced. In November 1994, the Traffic Commissioner announced that the company's Operator's Licence would expire at 30 April 1995 and not run its full course until 31 October 1998.

2.36 As a result, the managing director and engineering director, leading members of the management and employee team, resigned. London Transport strengthened the board of the company, introduced new engineering and operating procedures and, with the agreement of the Department, invited new bids for the company.

Completion of the sales

2.37 During completion with preferred bidders the initiative in sale negotiations tends to swing away from the vendor. At this stage any material information not previously disclosed to bidders is likely to lead to pressure to amend the price or terms of sale in favour of the purchaser. London Transport had sought to disclose as far as possible all material information to bidders at final bid stage and resisted pressures to reduce bids.

2.38 In line with recommendations made by the Committee of Public Accounts, the terms on which the companies were sold included property clawback arrangements.

Price and other negotiated sale amendments

2.39 Five of the ten preferred bidders pressed for price reductions amounting to some £7.9 million. Agreed reductions amounted to some £5.4 million. In each case final prices remained higher than the next best bids. Agreements were reached with two purchasers to exclude certain properties from the sales. One purchaser was indemnified against environmental liabilities, and another against accrued business rates unclaimed by the relevant boroughs.
Clawback arrangements

2.40 All freehold and one leasehold property sold with the companies were subject to clawback arrangements which apply for ten years. Following an unsolicited bid, one company was sold to the preferred bidder with a clawback on potential gains arising from any onward sale of the company's shares within two years after the sale. The detailed operation of these clawback arrangements is explained at Appendix 4.

Gross proceeds

2.41 Sale proceeds exceeded both London Transport and the Department's expectations. London Transport sold the companies for a gross figure of £233 million with a cash settlement of £218.2 million after adjustments for outstanding working capital balances with London Transport (Figure 4).

<table>
<thead>
<tr>
<th>Company</th>
<th>Proceeds £m</th>
<th>Working capital adjustment £m</th>
<th>Cash settlement £m</th>
</tr>
</thead>
<tbody>
<tr>
<td>East</td>
<td>28.9</td>
<td>(2.409)</td>
<td>26.491</td>
</tr>
<tr>
<td>Selkent</td>
<td>13.3</td>
<td>(1.470)</td>
<td>11.830</td>
</tr>
<tr>
<td>Leaside</td>
<td>29.5</td>
<td>0.017</td>
<td>29.517</td>
</tr>
<tr>
<td>South</td>
<td>17.1</td>
<td>(0.989)</td>
<td>16.111</td>
</tr>
<tr>
<td>Central</td>
<td>24.5</td>
<td>(2.027)</td>
<td>22.473</td>
</tr>
<tr>
<td>Northern</td>
<td>20.55</td>
<td>(1.668)</td>
<td>18.882</td>
</tr>
<tr>
<td>General</td>
<td>28.05</td>
<td>(2.237)</td>
<td>25.813</td>
</tr>
<tr>
<td>United</td>
<td>25.6</td>
<td>(2.831)</td>
<td>22.669</td>
</tr>
<tr>
<td>Centrewest</td>
<td>25.6</td>
<td>0.285</td>
<td>25.885</td>
</tr>
<tr>
<td>Metroline</td>
<td>20.0</td>
<td>(1.471)</td>
<td>18.529</td>
</tr>
<tr>
<td>Totals</td>
<td>233.0</td>
<td>(14.800)</td>
<td>218.200</td>
</tr>
</tbody>
</table>

Source: London Transport.

Notes
1. Proceeds represented settlement in respect of: payment for shares and accrued profits in 1994-95; and the repayment of debt to London Transport.
2. Each company had a working capital account with London Transport, which was essentially a bank account intended to minimise cash balances at the companies. Bidders were invited to bid against an estimate of working capital balances at completion. The working capital adjustment is the difference between that estimate and the actual balance at completion.

2.42 This outcome appears to be due to a combination of good management of the sale by London Transport and the business optimism of the eventual purchasers. The prices paid for the companies reflected a premium in all cases over the net asset value of the companies and, for the companies as a whole, averaged 60 per cent of turnover (Figure 5 overleaf), some 10 per cent higher than the average for comparable bus company sales outside London between December 1992 and April 1994.
The Sale of London Transport’s Bus Operating Companies

<table>
<thead>
<tr>
<th>Company</th>
<th>Proceeds as a per cent of turnover</th>
<th>Proceeds as a multiple of net assets</th>
</tr>
</thead>
<tbody>
<tr>
<td>East</td>
<td>58</td>
<td>4.1</td>
</tr>
<tr>
<td>Selkent</td>
<td>40</td>
<td>1.6</td>
</tr>
<tr>
<td>Leaside</td>
<td>68</td>
<td>1.7</td>
</tr>
<tr>
<td>South</td>
<td>52</td>
<td>2.0</td>
</tr>
<tr>
<td>Central</td>
<td>60</td>
<td>2.8</td>
</tr>
<tr>
<td>Northern</td>
<td>73</td>
<td>4.7</td>
</tr>
<tr>
<td>General</td>
<td>56</td>
<td>2.4</td>
</tr>
<tr>
<td>United</td>
<td>69</td>
<td>2.9</td>
</tr>
<tr>
<td>Centrewest</td>
<td>65</td>
<td>4.6</td>
</tr>
<tr>
<td>Metroline</td>
<td>70</td>
<td>2.7</td>
</tr>
<tr>
<td>Average</td>
<td>61</td>
<td>2.95</td>
</tr>
</tbody>
</table>

Source: London Transport.

Note: Calculations are based on turnover for the year ending 31 March 1994 and on the value of net assets (fixed assets stated at net historic cost) as at that date.

Sale management

2.43 Proceeds exceeded the indicative bids submitted by the eventual purchasers of the companies by some £30 million. Although unquantifiable, some of this increase is due to effective management of the bidding processes by London Transport and their advisers, including:

a) London Transport’s strengthening of the bidding process by introducing an extra (interim) bidding stage to exploit the considerable strength of indicative demand (paragraph 2.27);

b) the design of the interim bidding stage, which comprised a first tranche of bids for the five companies with the strongest indicative bidding lists and a second tranche of bids for the remaining companies, resulting in 57 bids on average 20 per cent higher than at indicative stage (paragraphs 2.29 and 2.30); and

c) London Transport’s success in obtaining exclusivity premiums and resisting pressures to reduce proceeds during sale completion (paragraphs 2.30, 2.33, 2.37 and 2.39).

2.44 The strength of indicative demand (paragraph 2.27) also suggests that London Transport prepared the companies for sale and marketed them effectively.
Proceeds greatly exceeded a benchmark valuation of £112 million to £154 million carried out by London Transport's financial adviser, BZW, in May 1994, shortly before receipt of the indicative bids. Although the benchmark valuation was a cautious estimate of the level of proceeds below which the vendor should consider carefully whether to continue with the sale rather than an estimate of most likely proceeds, this is another measure of the unexpected success of the sale. The basis of the benchmark valuation is considered further in paragraphs 3.18 to 3.20.

**Business optimism**

In addition to London Transport's management of the sale, business optimism appears to have played a part in driving up prices. In discussions with the National Audit Office, several trade purchasers confirmed that their bids had taken account of opportunities for business synergies and rationalisation of working practices. Purchasers generally confirmed that they had taken an upbeat view of their prospects of winning future business and felt that Ministers were likely to seek to promote and improve public transport in London rather than contract it.

Trade purchasers emphasised the size and importance of the London bus market for companies with ambitions of growth in the industry. They predicted that major players in the industry without a foothold in London would increasingly tend to seek entry by acquisition and through route tendering. They expected a gradual consolidation of the market in London with those companies bought by management and employees likely to be targets for acquisition.

Since the sale efficiency gains have been reported by Cowie at Leaside. In their annual report for 1994, Cowie reported an increase in Leaside's operating margin (percentage excess of revenue over costs before tax) from around one per cent at the time of sale in September 1994 to 10 per cent over the period September-December 1994. Cowie told the National Audit Office that part of this increase was due to seasonal factors.
3. Costs of sale and incentives

3.1 The Department's objective to maximise net proceeds required effective control over costs. The main costs of the sale were incurred by the Department’s and London Transport’s advisers. Excluding VAT and internal project costs, London Transport’s total costs were some £9.7 million and the Department’s costs were £719,000. Together these costs amounted to £10.4 million or 4.5 per cent of gross proceeds.

3.2 London Transport incurred costs of £331,000 in support of unsuccessful management and employee bids. Not every management and employee team received the maximum assistance. The amount was determined with regard to actual costs and the progress each team had made in the bidding process. In addition, the Department established an incentive arrangement to reward London Transport in the event of a successful sale.

3.3 This part of the report examines how the Department and London Transport controlled these costs. It shows that:

the Department

- selected their adviser through competition, and controlled their costs by defining their work requirements in stages and agreeing fee caps for that work;

- required London Transport to meet the costs of their own advisers in the sale and took no part in selecting them or controlling their costs;

- established an incentive arrangement with London Transport by which London Transport benefited by £33 million from the sale of the companies;
London Transport

- selected their financial adviser and most of their other advisers through competition, but appointed their legal adviser and their reporting accountant, who already worked for London Transport and whose knowledge about the company they regarded as essential to the sale, on a single tender basis;

- appointed a project director directly responsible to the London Transport board who set regular fee caps on particular areas of the work of advisers and monitored outturn on the project against budgetary targets;

- arising from the decision to postpone deregulation in November 1993, absorbed unanticipated costs estimated at more than £0.5 million; and

- exceeded their revised budget for external advice (£7.253 million) by £2.11 million largely as a result of higher than expected success fee payments to their financial adviser which were linked to higher than expected proceeds.

3.4 This part of the report also summarises the results of a National Audit Office review of the basis of the benchmark valuation and its link to the success fee arrangement for London Transport's financial adviser. This has led to three points for consideration by departments in future sales (see paragraph 12 of the Introduction, summary and conclusions).

The Department's costs

3.5 The Department appointed a financial adviser, Price Waterhouse (at a cost of £712,000), to advise widely on the conduct of the sale and in particular to monitor and report on the decisions taken by London Transport. Price Waterhouse carried out the work under two contracts agreed in 1992 and 1993. Both contracts were placed following competition. The Department secured reductions in Price Waterhouse’s hourly rates on the second contract. The Department controlled costs by defining work requirements in stages and setting cost caps which could not be exceeded without agreement. The Department also employed the Government Actuary’s Department to advise them on pensions advice to be given to London Transport (at a cost of £7,000).
3.6 To encourage them to maximise proceeds, Ministers decided that London Transport should keep a percentage of receipts above a certain threshold. To inform a decision on the level of the threshold, the Department required Price Waterhouse, in October 1993, to provide an estimate of gross sale proceeds.

3.7 At that point, the Government had decided to defer deregulation, decisions remained to be taken about the future tendering regime and potential bidders had not yet been approached by London Transport. Given these uncertainties, Price Waterhouse could provide no more than a tentative estimate of proceeds, conscious that the sale was still some way off and that it was not yet possible to test market reaction to concrete sale proposals. They concluded proceeds might be between £112 million and £127 million.

3.8 The Department and Treasury Ministers agreed to use £100 million as the basis for an incentive. In agreeing this figure, the Department aimed to minimise the risk that London Transport would incur loss through failure to achieve this level of proceeds, but did not consider it too low a figure given the information then available about the sale. It was particularly difficult to predict the effect of the decision to postpone deregulation of the London bus market. It was then thought possible this could significantly reduce bids by restricting the scope of potential purchasers to manage key aspects of the future business.

3.9 To ensure that failure to meet the threshold had a disincentive effect, the Department required London Transport to meet a share of any shortfall in proceeds as well as benefit from any excess. If proceeds exceeded £100 million, London Transport were to surrender 75 per cent of the excess to the Exchequer and retain 25 per cent. If proceeds were below £100 million, the Department were to meet 75 per cent of the shortfall and London Transport the remaining 25 per cent.

Results of the incentive

3.10 Gross proceeds (£233 million) substantially exceeded London Transport’s £100 million target. London Transport therefore retained some £33 million (25 per cent of the difference between £233 million and £100 million).

3.11 The Department believe the incentive benefited the sale. They consider that the incentive encouraged London Transport not only to maximise proceeds but also to achieve the target date for completion of the sales, so that they could use the funds within the
1994-95 financial year. Having agreed the incentive arrangements with London Transport, the Department did not believe it was appropriate to alter them when it became clear that the threshold on which they were based was a significant under-estimate of likely proceeds.

**London Transport’s costs**

3.12 The Department took no part in the appointment or control of the costs of London Transport’s advisers. Ministers took into account in setting London Transport’s external finance limit, the fact that London Transport would face such costs. All of London Transport’s actual costs had to be met by London Transport and were not deducted from proceeds transferred to the Exchequer. London Transport kept the Department informed about advisory appointments and budgetary control.

**Selection of advisers**

3.13 London Transport appointed their financial adviser, BZW, and most of their other advisers through competition in which judgements of quality were made with regard to price. Some advisers, most importantly their legal adviser and reporting accountant, were appointed on a single tender basis because of their previous work for London Transport and knowledge of the organisation. London Transport secured discounts to the standard commercial fee rates for these advisers.

**Budgetary control**

3.14 London Transport appointed a project director to oversee all aspects of the privatisation, and to liaise with the Department. The project director set a budget for the costs of the sale and reported monthly to the London Transport board. The project director held monthly meetings with advisers to review the cost of their previous month’s work, agree the scope of their next month’s work, and determine financial caps for particular areas of work. Advisers were not allowed to exceed financial caps without his authority.

3.15 In March 1993 the London Transport board approved a budget of £9 million to cover both the advisory and internal project costs of the sale. In May 1994 the budget was increased to £9.5 million to take account of a success fee arrangement then negotiated with London Transport’s financial adviser. The adjustment assumed sale proceeds of £133 million - the mid-point of the adviser’s recently concluded benchmark valuation of the companies.
3.16 Arising from the decision in November 1993 to postpone deregulation, London Transport absorbed unanticipated costs estimated at more than £0.5 million within their original budget. On completion of the sale, advisory costs exceeded the revised budget based on estimates at May 1994 by £2.11 million (29 per cent). This was largely due to higher than expected success fee payments to London Transport's financial adviser (Figure 6).

**Figure 6: Costs of sale**

<table>
<thead>
<tr>
<th></th>
<th>Budget £'000</th>
<th>Actual £'000</th>
<th>Variance £'000</th>
</tr>
</thead>
<tbody>
<tr>
<td>Department of Transport</td>
<td>719</td>
<td>719</td>
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<tr>
<td>London Transport</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>External Advisers</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Financial</td>
<td>2,807</td>
<td>5,056</td>
<td>(2,249)</td>
</tr>
<tr>
<td>Legal</td>
<td>2,206</td>
<td>2,187</td>
<td>19</td>
</tr>
<tr>
<td>Reporting</td>
<td>1,024</td>
<td>926</td>
<td>98</td>
</tr>
<tr>
<td>Accountants</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Pensions</td>
<td>223</td>
<td>261</td>
<td>(38)</td>
</tr>
<tr>
<td>Property</td>
<td>251</td>
<td>240</td>
<td>11</td>
</tr>
<tr>
<td>Others</td>
<td>742</td>
<td>693</td>
<td>49</td>
</tr>
<tr>
<td>Total</td>
<td>7,253</td>
<td>9,363</td>
<td>(2,110)</td>
</tr>
<tr>
<td>Support for Management</td>
<td></td>
<td>331</td>
<td></td>
</tr>
<tr>
<td>and Employee buy-outs</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Overall Total</td>
<td></td>
<td>10,413</td>
<td></td>
</tr>
</tbody>
</table>

*Source: London Transport and Department of Transport*

*Notes:*
1. London Transport's budget is based on estimates as at May 1994.
2. London Transport also incurred internal project costs of £1,978,000 against a budget at May 1994 of £2,247,000.
3. All costs are shown net of VAT.

**Financial adviser's success fee**

3.17 London Transport paid their financial adviser £1.2 million for work undertaken on a time basis before the sale and £3.87 million as a success fee for the successful completion of the sale. The basis of calculation of the success fee took into account the range of values included in the benchmark valuation of the companies. London
Transport agreed to pay their adviser a fixed amount for gross proceeds up to £110 million, 1.5 per cent of proceeds between £110 million and £133 million, the mid-point of their valuation, and 3 per cent of any higher proceeds. In the event proceeds and consequently the success fee exceeded expectations and the parties negotiated a settlement.

National Audit Office review

3.18 Given that the benchmark valuation was significantly lower than actual proceeds. The National Audit Office commissioned Corporate Valuations and Pannell Kerr Forster to examine the basis of the benchmark valuation carried out by London Transport’s financial adviser and its link to the adviser’s incentive arrangement. The examination set out to answer two key questions:

- how well the benchmark valuation met its purpose; and

- how far the link between the benchmark valuation and the adviser’s incentive arrangement was appropriate.

3.19 The principal conclusions arising from this work were as follows:

- the valuation report set out its scope, methodology and assumptions, including factors excluded from consideration as well as those included. It also included sensitivity tests showing the effect of different assumptions. The National Audit Office believe, however, that the valuation report could have more clearly separated out and presented the message that the valuation was intended to provide an indication of the level of proceeds below which the vendor should consider carefully whether to continue with the sale rather than an estimate of likely proceeds. The valuation was based on conservative assumptions and excluded market factors specific to particular bidders such as their willingness to offer a higher price for strategic reasons. London Transport, the Department and their advisers maintained that they all clearly understood the purpose of the benchmark valuation in this sale, but agreed that it is important that vendors clearly specify their requirements and the valuation report sets out the basis of the report clearly;

- the strength of indicative demand and bidders’ optimism about the companies’ prospects was greater than London Transport, the Department and their advisers had expected. The benchmark valuation had incorporated an appropriate methodology for valuing the companies but some assumptions proved to be
conservative. The eventual purchasers appeared, in particular, to take a more optimistic view than the benchmark valuation about the prospects for the companies in a regulated market;

- the Department's adviser co-operated with London Transport's financial adviser in aspects of the latter's work on the benchmark valuation. They endorsed its conclusions but considered in the case of three companies the valuations were high when compared to the relevant net asset values and price earnings ratios and that this should be taken into account if bids below the valuation were received. They were, however, unable to comment on the use of the valuation as a basis for the success fee, as the Department were unaware of that link until October 1994 (although they had been aware in general terms that London Transport intended to agree an incentive arrangement);

- there are risks in linking success fees to benchmark valuations as these may focus on a vendor's minimum expectations and will not necessarily reflect best estimates of likely proceeds for the purposes of setting a success fee threshold. These risks are likely to be heightened if best estimates have not been set or endorsed by an independent party aware of all their purposes, including any link to success fees.

3.20 Given the successful outcome of the sale London Transport considered overall that the incentive arrangement operated effectively and led to a reasonable reward to their financial adviser.
## Glossary of terms

<table>
<thead>
<tr>
<th>Term</th>
<th>Definition</th>
</tr>
</thead>
<tbody>
<tr>
<td>Capital allowances</td>
<td>Allowances designed to give tax relief for capital depreciation of business assets.</td>
</tr>
<tr>
<td>Distributable reserves</td>
<td>Retained revenue reserves of a company. The companies' retained revenue reserves were eliminated by dividends paid to London Transport.</td>
</tr>
<tr>
<td>External finance limit</td>
<td>A ceiling on the amount of finance, whether grant, subsidy or borrowing which a nationalised industry may raise during a financial year to supplement the income from its trading activities.</td>
</tr>
<tr>
<td>Information memorandum</td>
<td>A formal document supplied to prospective purchasers which includes detailed financial and other information about the companies to be sold.</td>
</tr>
<tr>
<td>Management and employee buy-out</td>
<td>The purchase of an entity by new owners, in which the majority, or all, of the shares are held by or on behalf of existing managers and employees.</td>
</tr>
<tr>
<td>Off-bus revenue</td>
<td>Revenue allocated to bus services arising from the sale of Travelcards, concessionary permits, London Transport Cards, Bus Passes and scholars' travel passes.</td>
</tr>
<tr>
<td>On-bus revenue</td>
<td>Cash fares.</td>
</tr>
<tr>
<td>Preferred bidder</td>
<td>The bidder whose final bid is initially accepted by the vendor and who enters negotiations to complete the sale.</td>
</tr>
<tr>
<td>Property clawback</td>
<td>The inclusion in a sale agreement of provisions relating to a specific property or properties, giving the vendor the right to receive a proportion of any subsequent profit from the resale of the specified properties. Such provisions are normally time-limited.</td>
</tr>
<tr>
<td>Traffic Commissioner</td>
<td>Commissioner appointed by the Secretary of State for Transport for each traffic area responsible inter alia for issuing licences under the Transport Act 1985.</td>
</tr>
</tbody>
</table>
Appendix 1

London Transport’s bus operating companies and garages

- Subsidiary company boundary
- Operated by company pointed to
- River Thames
Appendix 2

Chronology of events

June 1984
London Regional Transport Act passed. Section 9 (1) of this Act gives London Transport the power to dispose of their subsidiaries. Under Section 9 (2) disposals require the consent of the Secretary of State for Transport.

July 1985
Introduction of competitive tendering for London bus routes.

December 1992
Government announcement of the sale of London Transport’s bus operating companies.

March 1993
Completion of negotiation of contracts between London Transport and their bus operating companies for untendered routes.

June 1993
Publication of “London Buses-the road to privatisation” inviting interested parties to pre-register for the sales.

November 1993
The Treasury and Department of Transport agree the financial incentive for London Transport to maximise proceeds.

8 November 1993
Government announced that they would not introduce legislation to deregulate London’s bus services in the current parliament.

March 1994
Formal launch of the sales.

9 May 1994
BZW benchmark valuation of the companies.

12 May 1994
Receipt of indicative bids.

23 June 1994
Interim bids due for the first group of companies: Centrewest; East London; Leaside; London United, and Metroline.

6 July 1994
Interim bids due for the second group of companies: London Central; London General; London Northern; Selkent, and South London.

4 August 1994
Final bids due for the first group of companies: East London; London United, and Metroline. Centrewest and Leaside proceeded directly to preferred bidder stage following second bids.
The Sale of London Transport's
Bus Operating Companies

11 August 1994

Final bids due for the second group of companies: London General; London Northern; Selkent, and South London. London Central proceeded directly to preferred bidder stage following second bids.

2 September 1994 to 10 January 1995

Completion of each of the sales.
Appendix 3

Objectives and activities of London Transport buses

Principal objectives

To provide a high quality comprehensive bus network to meet London’s bus travel needs, having regard to efficiency, economy and safety of operation;

To maximise passenger benefit and usage, within the funds available;

To support multi-modal travel facilities; and

To develop and improve the infrastructure and information services which support the bus network.

Activities

To promote and improve safety and security standards for bus passengers in London and to improve the environmental impact of buses in the community, recognising that bus operators have the prime responsibility for the safety of their employees, passengers and other road users affected by their operations.

To determine the routes and service levels for bus services in London, in consultation with the bus operators and the London Boroughs, London Regional Passengers Committee and other user groups having due regard to efficiency, economy and safety of operations and equity across London.

To oversee the tendering programme.

To implement the Passengers’ Charter.

To monitor the performance of operators to ensure satisfactory operation of procured bus services in terms of cost, reliability and receipts.

To provide properly maintained bus passenger infrastructure throughout London, ensuring a clean, safe and user friendly environment for passengers.

To promote bus services.
Appendix 4

Clawback on property

All the freehold, and one long leasehold, properties sold with the companies are subject to clawback provisions:

a) the companies entered into clawback debentures, and each property is subject to a legal charge;

b) the debentures are in force for a period of ten years from 1 April 1994;

c) the base value from which the clawback provisions are applied is the existing use value as at October 1993, with property based indexation;

d) the clawback liability will be calculated by reference to a proportion of the gain over base value, being:

75 per cent for the first three years from 1 April 1994;

60 per cent for the fourth year; and

50 per cent for the last six years.

Qualifying events triggering clawback on property

The principal qualifying events are:

• disposal of the property;

• disposal of the share capital of the relevant company;

• grant of planning permission;

• grant of an option or right of pre-emption in relation to the property;
The Sale of London Transport’s Bus Operating Companies

- entry into a conditional contract for the disposal of the property;
- grant of a lease or a licence; and
- receipt of insurance proceeds.

The disposal of a property or the share capital of the company owning the relevant property, outside its wholly owned group, will trigger clawback on the relevant property and release successors in title. The disposal of the relevant property or the shares of the company owning the relevant property as part of a sale of the original business of the company, as carried out at privatisation as a going concern, will not trigger clawback and the company’s original base value and accrued indexation for the relevant property will continue to apply in respect of future qualifying events.

Clawback on the onward sale of one company

London Transport agreed a two year clawback arrangement with the purchaser of one company, whereby the government’s share of any gains from an onward sale of the company would be as follows:

- up to one year after completion 90%
- 12 to 15 months after completion 70%
- 15 to 18 months after completion 50%
- 18 to 21 months after completion 30%
- 21 to 24 months after completion 20%

Clawback will be triggered by the sale of more than 25 per cent of the shares in the company.
Reports by the Comptroller and Auditor General
Session 1995-96

The Comptroller and Auditor General has to date, in Session 1995-96, presented to the House of Commons the following reports under Section 9 of the National Audit Act, 1983:

The Operations of the Student Loans Company Limited ............HC 13
Scotland’s National Museums and Galleries:
   Quality of Service and Safeguarding the Collections .............HC 14
Clinical Audit in England ..............................................HC 27
The Protection of Scottish Fisheries ..................................HC 28
The Sale of London Transport’s Bus Operating Companies .......HC 29