

CMA review of the undertakings affecting FirstGroup’s bus business across southern and central Scotland

Statement of issues

Introduction

1. On 30 October the Competition and Markets Authority (CMA) announced its decision¹ to conduct a review of the undertakings given in 2002 by FirstGroup plc (FirstGroup). The undertakings were given following a review by the Monopolies and Mergers Commission (MMC)² of the 1996 completed acquisition by FirstGroup of SB Holdings Limited (SBH) (“the ‘undertakings’”).³ The undertakings were given under the Fair Trading Act 1973 (FTA). They apply to services operated by FirstGroup across the First Edinburgh and First Glasgow areas,⁴ where FirstGroup operates approximately 255 tendered and commercial routes.⁵
2. The CMA has a statutory duty⁶ to keep under review undertakings given under the FTA. From time to time, the CMA must consider whether, by reason of any change of circumstances the undertaking is no longer appropriate and either:
 - (a) the relevant parties can be released from the undertaking; or
 - (b) the undertaking needs to be varied or to be superseded by a new undertaking.
3. The CMA’s decision to conduct a review of the undertakings was made pursuant to the guidance in CMA11⁷ and follows receipt of an application from

¹ See [decision statement](#).

² [FirstBus Plc and S B Holdings Limited: A report on the merger situation](#).

³ These undertakings can be viewed at: [FirstBus plc – notice of undertakings \(CC\)](#).

⁴ The First Edinburgh area comprises the unitary authorities of Stirling, Clackmannanshire, Falkirk, West Lothian, Midlothian, East Lothian and the Scottish Borders. The First Glasgow area comprises the unitary authorities of the City of Glasgow, North Lanarkshire, South Lanarkshire, East Dumbartonshire, West Dumbartonshire and East Renfrewshire.

⁵ Commercial Services are bus services that are run on a commercially viable basis without tendered support. Tendered Services are services where a local authority has invited tenders for the operation of the service, and a contract exists as a result of that tender.

⁶ Sections 88(4) and (5) of the FTA (as preserved in Schedule 24 of the EA02).

⁷ CMA (January 2011, revised August 2015), [Remedies: Guidance on the CMA’s approach to the variation and termination of merger, monopoly and market undertakings and orders \(CMA11\)](#).

FirstGroup on 31 August 2015 setting out evidence of a change of circumstance and consideration of responses to a public invitation to comment on that application.⁸ This provided grounds for the CMA to consider that there is a realistic prospect of finding a change of circumstances.

4. In considering variation and release of undertakings the CMA will consider whether there has been a change of circumstances. CMA11 sets out that the change of circumstances must be such that the undertaking is no longer appropriate in dealing with the competition problem and/or adverse effects which it was designed to remedy, if it is to lead to either variation or release.⁹ If there has been such a change of circumstance the CMA will then consider whether the undertaking can be released or (if not) needs to be varied.
5. In this statement we set out the main issues that we are likely to consider in reaching our decision (although this does not preclude the consideration of any other issues that may be identified during the course of our investigation).
6. We are publishing this issues statement in order to assist parties submitting evidence to focus on the issues we currently envisage being relevant to our inquiry and to invite parties to notify us if there are any additional relevant issues that they believe we should consider.

Background to remedies and theories of harm

The 1997 MMC report and 2002 undertakings

7. The original version of the undertakings were given in 2002 to the Secretary of State for Trade and Industry under section 88 of the FTA. The MMC found in 1997 that the merger would reduce competition as a result of two theories of harm:
 - (a) The merger caused a loss of potential competition between FirstGroup and SBH and between FirstGroup and other parties.
 - (b) FirstGroup's resulting dominance in central and south-east Scotland would deter entry.
8. The 1997 report also considered whether the merger would remove actual competition between the Parties, but noted that there was little actual

⁸ See: [FirstGroup plc – request to release undertakings](#).

⁹ CMA11, paragraph 2.5.

competition between FirstGroup and SBH before the merger either in commercial services or tendering.¹⁰

9. On the basis of its findings the MMC stated that behavioural remedies would be inadequate and recommended a divestiture remedy. Following the entry of Stagecoach into the Glasgow bus market, the Secretary of State for Trade and Industry decided instead to pursue behavioural undertakings, which were agreed in 2002. These undertakings applied to any route operated by First Group within, or part within, the First Glasgow area; and any route operated by First Group within, or part within, the First Edinburgh area.
10. These undertakings required FirstGroup not to raise bus fares in excess of the Retail Price Index in all areas excluding the city of Edinburgh; required FirstGroup in the First Edinburgh operating area to operate a mileage of at least 95% of the mileage that FirstGroup was operated in January 2002 (excluding the city of Edinburgh); and contained some other anti-predatory behavioural restrictions.

The 2006 review and revised undertakings

11. In 2006 the Office of Fair Trading (OFT) recommended that FirstGroup should be released from the undertakings. The Competition Commission (CC) decided not to follow the OFT's recommendation but instead varied the undertakings by revising the fare cap and rebasing the mileage floor.¹¹
12. In summary the undertakings are now as follows:
 - (a) Price cap (increase based on H-CPT index)¹² in the First Edinburgh and First Glasgow areas.
 - (b) Mileage floor (no less than 75% of 2002 levels) in the First Edinburgh area.
 - (c) Other anti-predatory behavioural restrictions:
 - (i) A requirement for bus services to be evenly spaced between those of competitors' services.

¹⁰ *FirstBus Plc and S B Holdings Limited: A report on the merger situation*, paragraphs 2.57–2.59.

¹¹ See: [FirstBus plc / SB Holdings Ltd: Notice of acceptance of Undertakings varying Undertakings](#).

¹² The H-CPT index was created following the CC's review in 2008. It is calculated from the components of a cost index published by the Confederation of Passenger Transport UK (the CPT index). The H-CPT is calculated using the cost increases from the index used in Great Britain for all cost categories except fuel costs, and using the fuel increases from the CPT (Scotland) index.

- (ii) An obligation not to increase commercial competition against tendered services in areas where FirstGroup has been unsuccessful in tendered bids.

FirstGroup 2015 request for a review of the undertakings

- 13. FirstGroup made a number of submissions in relation to increased competition that was present in its area compared with when the undertakings were imposed. It argued that the original rationale for the undertakings was incompatible with the CMA's latest analysis of the market, stating that the CMA had found that potential competition and entry were not significant constraints on incumbent operators.¹³ FirstGroup said that recent reviews of bus mergers had focused on the effects on head-to-head competition as opposed to potential competition.
- 14. FirstGroup also submitted that reduction in demand and increases in costs that disproportionately affected the local bus travel market in Scotland meant that it had been unable to fully recover its costs, including the costs of financing investment.¹⁴

Issues to be considered in the review of undertakings

Theories of harm

- 15. Our initial view is that we will base our investigation into whether circumstances have changed sufficiently to justify releasing or varying the undertakings on the two theories of harm identified in the MMC investigation. These are detailed in paragraph 7.
- 16. To assess whether circumstances have changed sufficiently for these theories of harm to have been affected such that the undertakings can be released or varied, we will consider the following:
 - (a) Assessment of the extent of entry or expansion by competitors to routes operated by FirstGroup since the merger and its impact on competition.
 - (b) The effect of depot closures and depot ownership changes on the level of direct competition between First and its competitors and the impact on potential competition.

¹³ FirstGroup referred to the CC's final report (2011), [Local bus services market investigation](#), paragraph 11.54, pp11 & 12.

¹⁴ For more detail on FirstGroup's arguments and those of third parties see the [decision statement](#).

- (c) The impact of regulation (such as changes to the Bus Services Operators Grant, concessionary fare repayments and vehicle accessibility requirements) on the level of actual and potential competition.
 - (d) Any changes in the constraint placed on FirstGroup by other modes of transport such as train and tram.
17. We will also investigate whether, and if so the extent to which, the undertakings themselves may be having a distortive effect on competition or causing other consumer detriment by reason of changes in circumstance.
18. We may revise our theories of harm as our assessment of the acquisition progresses. The identification of these theories of harm does not preclude us identifying another area of investigation on receipt of additional evidence.

Potential variations to the undertakings

19. Should we conclude that the undertakings cannot be released but need to be varied we will issue a Notice of variation to allow parties to comment on our proposals.

Responses to the issues statement

20. Any party wishing to respond to this issues statement should do so in writing, by no later than 5pm on 11 December 2015. Please email firstgroup.undertakings@cma.gsi.gov.uk

Or write to:

Project Manager
FirstGroup undertakings review
Competition and Markets Authority
Victoria House
37 Southampton Row
London WC1B 4AD