10 Views of Stagecoach and Busways

Contents

10.1. This chapter summarizes the views of Stagecoach and Busways, each of which gave written evidence and attended a hearing.

Stagecoach

Jurisdiction

10.2. In Stagecoach's view the MMC should use registered vehicle miles as the most appropriate surrogate for market share in this inquiry. It was the most relevant measure and it could be verified with the DOT's fuel duty rebate returns, unlike turnover which might not be recorded consistently by all operators. Stagecoach thought a supply-side measure such as registered vehicle mileage ought to be of more interest to the MMC in their considerations of market power abuses of monopoly, oligopoly and predatory behaviour. It was well known that demand-side measures were far more prone to statistical error.

10.3. Stagecoach believed the ideal measure of market share was passenger mileage but the data were not readily available. The MMC might wish to consider using the number of current licences an operator held. The Traffic Commissioner would be able to verify these figures and also to confirm changes in number over time. The reason Stagecoach quoted turnover when publicly comparing its market share with other companies was because this was the measure the City understood best. Turnover offered a guide to earnings and growth potential.

Stagecoach's strategy

10.4. The deregulation of the bus industry was intended to replace public capital with private capital. Central and local government had substantially reduced the subsidies provided to bus operators. Bus companies had to convince the capital markets that they were not in decline. Stagecoach had done this; its operating margins were in the 15 to 20 per cent range. Its improved performance had been achieved chiefly through savings in maintenance, labour costs and overheads. Annual payments to operators for tendered local bus services had fallen from over £900 million before deregulation to less than £300 million today. Fuel duty rebate had been frozen since November 1993 and concessionary fare reimbursements had remained virtually unchanged.

10.5. It was incorrect to assume that there were not sizeable economies of scale in the bus industry. Stagecoach had benefited through its centralized finance and procurement policies, and by reducing overheads. It was able to achieve substantial savings through the purchase of large numbers of new buses, leading in turn to reductions in maintenance costs. It was also able to raise capital more cheaply than smaller companies, and to obtain more favourable insurance rates.

10.6. At the time of deregulation Stagecoach came into an industry where labour costs had been historically high. It had not withdrawn recognition from its trade unions and believed that to do so would harm industrial relations. By contrast small operators had lower overheads; they were not usually unionized and offered no pension schemes or other benefits. Stagecoach prided itself on its management philosophy in that it did not attempt to suppress the individual character of its management teams. However, they were encouraged to learn from best practice in other parts of the group.

10.7. Stagecoach had not copied the industry norms of network pricing. It aimed to set fares according to the circumstances of individual routes and its fare increases were no more than in line with the RPI. There were many instances where it had frozen its fares for lengthy periods. It had also reduced its operating costs per mile so that they were typically well below the industry averages as published by the DOT. Its policies were designed to curb fare increases. But it did not believe experiments in cutting fares should continue much beyond six months without full costs being covered.

Competition with other modes of transport

10.8. Stagecoach said that the MMC reports on National Express/Scottish Citylink (Saltire Holdings)[1] and S B Holdings/Kelvin Central Buses[2] had both considered other transport modes in evaluating competition. In the current inquiry, the influence of the Tyne & Wear Metro and taxis were particularly relevant and, arguably, weakened the conclusions about Stagecoach's market share. The MMC should also consider the extent of the PTE subsidy for the Tyne & Wear Metro and for the British Rail Newcastle-Sunderland link and contrast this with the lower subsidies which were available to bus operators. The major competitor to all bus operators, however, was private transport.

10.9. Most people preferred to use a car to travel to work. Without effective disincentives, few of them would change their established patterns of commuting. One of the factors giving rise to the public's poor perception of value for money in the bus industry was its record-in contrast to Stagecoach's-of raising fares in excess of RPI. Most of the new smaller operators had done nothing to challenge these fare practices.

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[1] *National Express Group PLC and Saltire Holdings Ltd*, Cm 2468, HMSO, February 1994, paragraph 6.21 *et seq*.

[2] *S B Holdings Limited and Kelvin Central Buses Limited*, Cm 2829, HMSO, April 1995, paragraph 2.27 *et seq*.

Darlington

10.10. To gain a proper understanding of the Darlington bus market the MMC needed to examine the key events which had occurred since deregulation, beginning with the entry of United in 1986. They should be aware that DBC had failed to proceed with the privatization of DTC in 1992 (at a time when it could have obtained a good price for the company) and bear in mind that Your Bus had set up in competition with United in 1993.

10.11. But it was the events in the six months preceding Stagecoach's entry which were most important. Stagecoach was concerned that the OFT, in its recent Competition Act investigation (see paragraph 6.14), had not correctly quantified the effects of United's actions on the market. For example, Your Bus's loss was over four times higher than the OFT assumed and DTC's bus operating loss was over £300,000, more than two and a half times the level assumed by the OFT.

10.12. Stagecoach had been aware since the beginning of 1994 that Westcourt was seeking to sell North East Bus, the parent company of United. Stagecoach had considered buying it but had decided that to do so would probably have brought unwelcome attention from the OFT. Busways had been a more attractive proposition. After it acquired Busways, Stagecoach had shared the knowledge about North East Bus's imminent sale with Busways' directors.

10.13. Stagecoach's prior knowledge of the sale of North East Bus was one of the reasons which prompted Busways to register four routes in Darlington in September 1994. Stagecoach had believed that events in the market-place could overtake the sale process of DTC and prevent it being completed. Stagecoach had decided that one way or another it intended to operate in Darlington. It would not have regarded it as a problem if DTC had been sold to a third party. At the very least Stagecoach would have been able, from its Darlington operations, to bring extra income to its Cleveland group.

10.14. Unlike the other bidders for DTC, which would not have been able to gauge the strength of the opposition, Stagecoach was aware of the future shape of the bus market in the North-East. In August 1994 it had entered into negotiations with Cleveland Transit. It followed this up by offering to buy Hartlepool Transport in September. (Stagecoach exchanged contracts with Cleveland Transit in October 1994 and with Hartlepool Transport in November 1994, subject to shareholder and employee ballots.) In addition, Busways was probably the only bidder for DTC which would have known that United was about to change hands.

10.15. Decisions about Busways' eventual entry to the Darlington market were taken by Busways' Board, whose non-executive Chairman, Mr Souter, was also the Chairman of Stagecoach. It was Busways, not Stagecoach, which had made the decisions about Darlington although the Stagecoach Board was made aware of what was happening. With hindsight, Stagecoach believed some errors of judgment had been made; for example, the offer of free fares had probably not been necessary (see paragraph 10.28). But Busways had acted in Stagecoach's best commercial interests and had taken the right decisions at the time.

10.16. Stagecoach did not dissociate itself from any of Busways' actions. Stagecoach's non-executive directors had approved of the decision to enter Darlington by mounting a competing operation rather than by paying too much for an acquisition. They considered that the interests of shareholders had been well served and that Stagecoach had been unfairly criticized by the media and by politicians. Stagecoach had succeeded in becoming the number two player in Darlington, and in doing so at the right price.

10.17. DTC had been suffering from competition from United for three years and had certainly been put on the market too late. Stagecoach thought DBC had been badly advised and should have gone to the big groups for a fast sale, rather than putting the company out for sale on the open market. It was an exaggeration to say that KPMG had accelerated the sale of DTC. Other local authority bus company sales had been handled far more expeditiously. Stagecoach had warned DBC that the situation was volatile and that DTC was vulnerable: this was the reason for Busways' bid based on exclusivity.

10.18. Stagecoach had believed the acquisition of DTC would present it with a good opportunity; it could achieve savings in overheads by combining functions in Darlington and Cleveland. It was confident that it would have been able to restore DTC to profitability and gain a reasonable return although this would have taken some time. But given its weak market position DTC ought not to have been such an attractive proposition to small or medium-sized operators with no other interests in the area.

10.19. Stagecoach saw no financial sense in the level of Yorkshire Traction's final bid and believed it would not have completed at the sale price quoted. At first Stagecoach had not been convinced by Busways' suspicions that Yorkshire Traction was acting on behalf of United. But after its own financial analysis of the trading position of DTC, and having seen the level of Yorkshire Traction's final bid, it came to the conclusion that Busways' hypothesis was correct.

10.20. Stagecoach would like the MMC to agree with its belief that there had been collusion between Yorkshire Traction and United. Any reasonable bidder, confronted with up-to-date information on DTC's escalating trading losses, would have withdrawn or reduced the amount of its bid. Stagecoach believed the level of Busways' indicative offer, £850,000, was the right price for DTC but realized that it needed to go higher in order to secure the deal.

Recruitment of drivers

10.21. It was not Stagecoach's policy to seek to run services against, and recruit drivers from, an operator which had refused its bid. It would not be a party to a deliberate attempt to recruit unilaterally from another operator. That was not how Stagecoach conducted its business. The situation in Darlington was that Busways had responded to an approach from the workforce. Stagecoach always made known its intentions to begin operating in a new area ahead of a privatization: it had done so, for example, not only in Darlington but also in Lancaster and Northampton.

10.22. Stagecoach knew that there was no shortage of capital from potential bidders for DTC. But everyone except Busways had overlooked the importance of the labour force. Busways' relationship with the TGWU was good and its union representatives were on good terms with their counterparts in DTC and Cleveland Transit. At an early stage DTC's workforce had expressed their views on the future of DTC but they had been ignored.

10.23. Stagecoach first told us that the circumstances in Darlington were unique. At the hearing it said that there was always the potential that a similar situation could arise elsewhere. It recalled that in 1991 the employees of Highland Scottish Omnibuses Limited based in Inverness had joined Stagecoach *en masse*, although in that case the employer had been involved in an industrial dispute with its employees and had issued redundancy notices. But in normal circumstances employees would not want to take the risk of moving; the situation in Darlington had occurred because of a badly handled privatization and a failure to consult with the employees.

10.24. Busways had not triggered the exodus of DTC's drivers. The first move was made by DTC's workforce representatives. Mr Tait, the TGWU Branch Chairman at DTC, met Busways' Chairman, Mr Souter, and its Finance Director, Mr Conroy, on 25 October and told them that the workforce did not want to work for Yorkshire Traction. Mr Souter had commented that Busways would need drivers for the four services it had registered in September. Mr Tait then said that his concern was for the future prospects of the whole DTC workforce.

10.25. In its written submission Stagecoach said that it was not aware that Busways' recruitment of drivers was aimed at a particular rival operator. At the hearing it said that it was immediately following the meeting with Mr Tait, when it knew that the whole DTC workforce wanted to join Stagecoach, that Busways decided to register all DTC's routes and to offer the £1,000 `non-training bonus'. Stagecoach sent us a cutting from a London newspaper of 2 March 1995 which contained an advertisement placed by another leading bus company for fully-trained PCV drivers, offering a £1,000 bonus. This confirmed its own estimates of the labour-market value of trained drivers.

10.26. The recruitment of the labour force was the key to Busways' success in Darlington. Mr Souter was able to offer advice based on Stagecoach's experience in Inverness. The workforce's decision to leave was the final nail in DTC's coffin, but DTC's weakness had been caused by two years of predatory pricing by United.

Free fares

10.27. Stagecoach said the MMC should understand that Busways' decision to operate free fares had denied United the opportunity of achieving a virtual monopoly situation in Darlington. Busways' decision should be seen in the light of United's conduct between 1989 and 1994; of the imminent sale of its parent, North East Bus, to one of the large groups; and of the withdrawal of Your Bus. These were the reasons Busways had been willing to accept trading losses during the free-fares period.

10.28. At the hearing Stagecoach said that, with the benefit of hindsight, Busways had made an error of judgment in offering free fares. It would have been better to have challenged the Traffic Commissioner's decision not to advance the registrations, pointing to the fact that Busways had employed 70 drivers who had no work to do, and who could be deployed to restore bus services to former DTC passengers. Within seven days the Traffic Commissioner would probably have waived the registration period.

10.29. The administrator's report on DTC had confirmed that the enforced operation of free services by Busways had not been the sole reason for DTC's failure.

Stagecoach in Darlington

10.30. In an article in the press Mr Souter was quoted as saying that Darlington could only support two operators, but Stagecoach said that the statement had been made after the exit of Your Bus from the market. It was true that with the present structure the market probably could only support two operators but Stagecoach would not rule out the opportunity for a third, provided that operator was able to offer a genuinely distinct product and was not seeking to target the other operators' most profitable routes.

10.31. Stagecoach had succeeded in becoming the number two player in Darlington and in doing so at the right price. Busways had incurred losses in introducing Stagecoach Darlington but Stagecoach expected the operation to be profitable within six months. This was a perfectly normal example of market entry: there was nothing predatory about it.

10.32. There was no evidence to support the view that United and Busways would now share the Darlington market and that fares would be increased. Stagecoach's policy was to reduce running costs and improve the quality of its product. It would not necessarily raise fares in response to a competitor's actions. Stagecoach was more interested in achieving the profitability targets it had set for its businesses. Its aim was to increase its market share by offering the best product.

South Shields

10.33. When Stagecoach acquired Busways, Mr Souter visited South Shields and observed that Busways had a tacit work-sharing arrangement with Hylton. He came to the conclusion that the arrangement with Hylton was putting Busways at a disadvantage. He also noted that Busways' network ticket accounted for a much lower share of its sales in South Shields than did the equivalent tickets in Newcastle and Sunderland. In a normal market Stagecoach expected that an operation with 66 per cent of vehicle mileage would generate 70 to 75 per cent of the patronage. Busways' existing network ticket had not been properly used to secure the market share Stagecoach would have expected.

10.34. Mr Souter proposed changes to the weekly-ticket fares in line with Stagecoach's market-pricing policy. The opportunity existed to improve Busways' market share and Stagecoach did not believe that the live-and-let-live approach which Busways had adopted would bring this about. Busways' action was not directed at Hylton, however-there were others in the market as well, including Go-Ahead.

10.35. Busways told Stagecoach that it believed Hylton would be prepared to sell its business and proposed that an approach should be made to Hylton to discuss this before it introduced any fares incentives. Stagecoach had raised no objection as it believed this was a matter for the Busways Board to decide. But it told Busways that the present situation was not satisfactory.

10.36. Busways' £1.99 saver ticket had been an introductory offer. It proved popular. Passenger numbers and income increased. Unexpectedly, however, the PTE reduced its concessionary fares subsidy, treating Busways less favourably than any other operator in the North-East. Busways had priced its network tickets in good faith, in the expectation that it would be able to increase its market share at the expense of Go-Ahead and other operators. Had the PTE not changed its concessionary fares policy, Busways would have increased its profits as well as its market share.

10.37. Following Mr Souter's visit to South Shields Busways had examined the high-volume corridors it shared with Hylton. It concluded that there were gaps in its timetable which were being filled by Hylton, and that passengers should be offered a choice of product. Busways believed there was sufficient volume to justify a choice of operator on these routes and it had therefore registered additional services.

10.38. In response Hylton had registered extra services against Busways on other corridors. Busways, too, was unable to meet its profit forecasts. By competing with Busways on these lower-volume corridors Hylton must have reduced its own profits as well as Busways'. In Stagecoach's view Busways could not have expected that this would happen because Hylton's response did not make commercial sense. Nevertheless Stagecoach believed Busways should not be denied the opportunity to experiment with new pricing policies which were designed to meet the market conditions prevailing in South Shields.

10.39. Stagecoach said that it was not part of its policy to force any operator out of business. If it saw an opportunity to improve its profitability and increase its market share it would do so within the parameters of any market. Its objectives were to maximize shareholder wealth in the long term. South Shields had provided it with such an opportunity.

Busways

The inquiry

10.40. Busways expressed concern about the initiation and conduct of the inquiry. It said that the OFT had consulted other operators prior to the reference being made, but Busways had been given no opportunity to comment other than on the boundaries of the proposed reference area. It also objected to the OFT Press Release which commented on Busways' actions in Darlington (Appendix 2.1). It said that the allegations about its role in the collapse of DTC were unsubstantiated and in some cases clearly wrong.

10.41. In Busways' view the MMC had concentrated on its activities and, to a lesser extent, those of Go-Ahead, to the exclusion of other operators. But there were three other major operators in the reference area competing in the same market: British Bus (owner of Northumbria), West Midlands Travel/National Express (owner of North East Bus, including United) and the Tyne & Wear Metro.

10.42. Busways did not believe it was rational to confine the inquiry to the supply of bus services. Other modes of transport were relevant, particularly in considering public interest issues, for example raising fares or reducing service levels to the public. The view apparently taken by the MMC that a monopoly of bus services led to higher prices and lower quality of service ignored the trends towards other means of transport. It also ignored Stagecoach's record of restricting fare increases, and its policy of asset investment and replacement.

10.43. Busways reserved the right to seek judicial review of any findings on events which it believed were not within the MMC's jurisdiction, or generally about the manner in which the inquiry had been conducted, or any conclusions which the MMC reached.

Jurisdiction

10.44. Busways believed Stagecoach had less than 25 per cent of the market in the reference area before 12 December 1994, when Stagecoach acquired Hartlepool Transport, and that the MMC therefore had no jurisdiction to investigate events prior to that date, in particular:

(a) events in Darlington prior to 11 November (when DTC ceased its operations); and

(b) events in South Shields which occurred before 12 December 1994.

10.45. In Busways' view, the MMC were wrong to depart from using registered vehicle miles to establish jurisdiction which they had consistently used for this purpose in the past. The alternative measure of turnover proposed was an inadequate and unrepresentative test of market share, and overstated Stagecoach's market power, in particular.

10.46. The reasons put forward for this view included the following:

(a) Registered vehicle mileage, despite being a measure of capacity, was in practice a good proxy for supply. Busways' experience, supported by a comparison of an urban and an inter-urban service supplied to the MMC, was that there were direct correlations between passenger miles, which the MMC seemed to agree with Busways would be the best market share test if accurate data could be collated, and registered vehicle mileage. There was no such correlation for turnover. The reason for this was that, in a market with a variety of large and small competitors, supply would be matched to demand, so that less populous areas received less frequent service and vice versa. Differences in bus size were not an important factor as there had not been time for many operators to rationalize their fleets since deregulation so as to use the most appropriate size of bus for each service.

(b) The share of turnover did not provide an accurate picture of the respective strength of different operators, which was derived from profitability, not revenue. Accordingly, whilst an urban operator like Busways might have higher turnover per mile, this was more than offset by greater costs of operating in urban areas, due to the frequency of stops and traffic congestion. The MMC's contention that greater weight should be given to urban services than shire and inter-urban services, because of the greater turnover per mile, was misconceived. Customers typically paid more for similar lengths of journey for inter-urban and shire journeys than for urban journeys. Moreover urban turnover was substantially enhanced by local authority subsidies to passengers for concessionary travel and to operators for tendered services, and was thus not directly related to any price/demand equation.

(c) As the purpose of the Act was the promotion of competition, the criterion for supply should take account of potential market power and any allegedly anti-competitive behaviour under investigation; since in this case the focus of the inquiry was on predatory pricing, use of turnover as a measure would have the perverse effect of understating the share of supply of any operators engaging in this practice.

(d) Busways was concerned that, by altering the market share criterion from registered vehicle mileage, which had been used in all previously reported decisions of the MMC in relation to merger inquiries and (although turnover data were available) the only previous monopoly inquiry in the bus industry, the MMC were predominantly motivated by an intention to ensure that Stagecoach was identified as a scale monopolist from an earlier date. Changing the criterion simply to bring one operator within the investigatory powers of the MMC was not a proper exercise of the MMC's power to select an appropriate criterion.

Company background

10.47. Busways told us that it became an employee-owned company in 1989. It realized that it had to speed up investment and produce better margins to give it security and stability and a longer-term presence. In late 1993 Busways' management shareholders had considered an approach from its employee representatives to extend the existing workforce shareholding in Busways (49 per cent of the total shareholding) by selling part of the management shareholding to one of the Busways employee trusts. Discussions about such a purchase continued until March 1994. Even before March 1994 the evident difficulties of financing such a purchase, and developments in the bus industry generally, caused its Board to reconsider whether such a buy-out would be in the long-term interests of Busways or its employee shareholders. It was already clear that the industry was becoming dominated by a few large groups and Busways reviewed its options including expanding its business into new geographical areas, acquiring other bus companies, merging with other ESOP companies and selling Busways to one of the existing national groups.

10.48. In March 1994 Busways' Board resolved to investigate the prospect of merging with other bus companies. It was concerned that it might be left behind by changes in the industry which were gathering pace. Some groups, including Go-Ahead which was based within three miles of Busways' centre of operations, had obtained a Stock Exchange Listing and other regional operators had merged to form large national groups. Busways thought United and Northumbria were potential targets for the national groups. Busways' three principal competitors in the region would then have access to funds for investment in expansion, further company acquisitions and assets. Busways, with its borrowings from the 1989 buy-out, would be unable to compete with them.

10.49. Busways carried out negotiations with Stagecoach and another national group between March and June 1994. An offer by Stagecoach, unanimously recommended by Busways' Board, for the entire issued share capital of Busways was posted on 27 June 1994 and approved by over 97 per cent of those employees voting in an employee ballot on the issue. The sale was completed on 26 July 1994.

10.50. Since joining Stagecoach Busways had seen margins broadly stabilize against a declining market. To maintain and improve profitability it was intent on cutting costs through improving efficiency, introducing profit-related pay and benefiting from the group's economies of scale in purchasing. Its objectives over the next two years were to move towards the margins achieved by well-established Stagecoach companies of 15 per cent or higher. To achieve this it was also necessary to arrest the decline in the market. It was investing heavily in new buses and believed it was in a position to improve the quality and reliability of its service, but equally to benefit from economies in maintenance, through its use of new buses.

10.51. Management and operational decisions were taken by Busways' directors and its management team. Mr Souter, Stagecoach's Chairman, was non-executive Chairman of Busways. Stagecoach set Busways goals and objectives, particularly about financial performance. Locally, managers took decisions as they always had done in the past. All decisions about Busways bus services, including decisions to register or deregister, were authorized by its Commercial Director, Mr Nash.

10.52. Busways' two low-cost units, Blue Bus Services and Favourite Services, had two purposes. One was to go for the tendered market, particularly for the miscellaneous workings contracts awarded by the PTE, and the other was to operate commercially-marginal services which would not be profitable for the other divisions. It would continue to use the units if they were able to produce the returns Busways was aiming for, but because of its policy of quality improvement it did not envisage increasing their use.

Competition in the reference area

10.53. Busways said that the principal challenge facing bus operators was the steady decline in the number of passengers using local bus services. The conclusion for any bus operator to draw was that passengers needed to be attracted from the car to public transport. In the past, as a company whose services were concentrated predominantly in Tyne & Wear and particularly Newcastle, Busways had benefited from the fact that car ownership was far lower than in many other areas. But the latest figures produced by Newcastle City Council showed that over the period 1988/89 to 1993/94 12-hour car traffic flows increased by 23 per cent whilst bus and coach usage declined by 28 per cent. This meant that Busways and other Tyne & Wear operators had still more to lose from the diversion of passengers to the car than operators in areas which had already become accustomed to higher car ownership.

10.54. It was the trend, not the absolute level, of car ownership which was relevant to bus operators. For the first time since the 1930s the North-East was achieving economic growth comparable to the rest of the UK and Tyne & Wear residents would follow the rest of the country in acquiring their own vehicles. It was vital for a bus operator to respond by market pricing, investment in new vehicles and the provision of a stable and reliable network of services if the continuing trend from public transport to the car was to be halted in the North-East.

10.55. The decline in bus usage was not necessarily irreversible. It depended on how successful a partnership could be achieved between bus operators and local authorities in managing the infrastructure, for example by giving buses priority over private cars. The major deterrents to potential customers were unreliability caused by traffic delay, waiting times and the travelling environment, together with a perception that bus fares were poor value for money. Busways' planned investment in new vehicles and its lower pricing initiatives were designed to encourage passengers to prefer a Busways service.

10.56. Busways was concerned that the MMC were not attaching enough weight to the importance of the Tyne & Wear Metro as a competitor to bus operators in the reference area. Until recently the Metro's fares had been similar to local bus fares. But the Metro had recently reduced some of its fares in areas which competed with Busways. In Busways' view this was a misuse of the subsidy which the Metro attracted from the PTE. The Metro competed with Busways in the Newcastle area and had some effect on Busways' town services in South Shields, but its chief impact in South Tyneside was on inter-urban services to Newcastle, where bus operators could not compete with the speed and subsidized fares offered by the Metro. Buses therefore tended to feed into the Metro via the interchange station at Heworth.

10.57. It would be against the public interest to restrict fair competition by Busways, or to discourage Busways and other Stagecoach companies from fares innovations which were intended to reverse passenger decline. A bus operator could not be certain of the effects of reduced fares on new routes until they had been tried. Fares had to be adjusted to halt the decline in passenger numbers; this might mean that a route did not cover its full cost but Busways should not be penalized for trying.

10.58. Competition in the reference area was such that any challenge by a large operator to one of the others would immediately provoke an aggressive response from the affected rival and neither would benefit. This was inevitable because of the nature of the market. Competition between large operators was therefore subtle and gradual rather than head-to-head, for example through the offering of a variety of own-brand tickets.

10.59. Busways saw little advantage in introducing a statutory scheme to require registration of different liveries. The right to preserve a distinctive presentation of vehicles was adequately protected by general law. Busways itself had successfully taken legal action against another operator for `passing off'.[1]

Darlington

The Darlington bus market prior to Busways' entry

10.60. Busways urged the MMC to look at the Darlington bus market before Busways entered it, asking themselves what would have happened otherwise. The entry of Your Bus in May 1993, and the reaction to it by DTC and United, had provoked public concern about traffic congestion. But the intervention of the Traffic Commissioner, the police and the local authorities had not reduced the numbers of buses operating in the town. All the operators were making losses between May 1993 and October 1994.

Busways' entry to the market

10.61. It was in January 1994 that Busways had first considered operating in Darlington. Its view had been that United was likely to drive Your Bus and DTC out of the market before long, because they were not financially strong. However, Busways considered that if it entered the market as a serious contender, United would be likely to retrench.

10.62. Busways also reckoned that the proximity of its Head Office in Newcastle to Darlington could enable it to reduce overheads. It therefore decided to undertake a feasibility study of the prospects of creating a new Darlington division. But in March 1994 the Busways Board had resolved to investigate the prospect of merging with another company, and the feasibility study was suspended. On 26 July Stagecoach acquired Busways.

10.63. On 31 August 1994 Busways' Chairman, Mr Souter, and executive directors had met to discuss the approach they would adopt to the sale of DTC. Mr Souter was aware at that time that North East Bus (including United) was for sale. Busways was concerned that United might eliminate competition in Darlington by acquiring DTC, either directly or through what Busways called a `stalking horse purchaser',

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[1]Use of a trade mark, name or get-up designed to make the public believe the service is connected with that of another operator.

meaning a company acting on United's behalf. It was agreed that if the price was right, Busways should buy DTC. If not it should establish a new division in Darlington.

Busways' September registrations

10.64. Following that meeting Busways registered four routes in Darlington on 8 September. It deferred the start date until 12 December to avoid causing a further deterioration in DTC's operating performance before the company could be sold. To commence its operations earlier might have been viewed by DBC as an attempt to drive down the price at which Busways could acquire DTC. The circumstances in which Busways registered the services did not indicate predatory behaviour designed to deter or eliminate other operators, or to drive the price down. It had been a sound commercial decision. The likely bidders for DTC would have been other strong national groups, which would not have been intimidated by Busways' registrations. But Busways also argued that if Yorkshire Traction had drawn proper conclusions from Busways' registrations, its bid would probably have been lower than Busways' bid-if it had bid at all.

10.65. In registering the four routes Busways had committed itself to a relatively small operation which it could service from within its existing resources. The ultimate size of Busways' operation would have depended to some extent on the outcome of the bidding process and other developments in the market such as the availability of drivers.

The bids for DTC

10.66. In Busways' view there had always been the risk that potential purchasers of DTC would set up a new business instead. The failure of DBC to obtain a price for DTC which was not justified, and which the preferred bidder might well not have been willing to pay in any event, should not be viewed as a distortion of the market.

10.67. On 14 September Busways submitted an indicative bid of £600,000 for DTC, based broadly on net asset value, together with an `exclusivity' bid of £1 million (see paragraph 6.26). In the light of DTC's rapidly deteriorating financial position, Busways expected DBC to take the exclusivity bid very seriously. However, DBC rejected that bid and, following encouragement from KPMG, Busways raised its non-exclusive offer to £850,000.

10.68. Busways was short-listed and began its analysis of DTC by examining the information which KPMG gave it in the information memorandum, and by taking up DBC's offer to visit DTC. At a meeting with DTC's directors on 29 September, at which DBC and KPMG were also represented, DTC reported a sharp deterioration in its financial position from that shown in the information memorandum.

10.69. On 14 October Busways submitted its final bid for DTC. This was based on a price:earnings ratio of seven and was for £1,033,333 (see paragraph 6.31). In making this offer its considerations were, on the one hand, DTC's losses which its management accounts indicated were about £10,000 per week and, on the other hand, the costs Busways would incur if it set up its own organization. The cost of setting up a separate operation would have been substantially less than the proposed cost of acquiring DTC but Busways decided to continue with the bidding process in order to preserve goodwill with DBC, to make certain it had sufficient drivers and to avoid wider adverse political reaction.

10.70. On 24 October DBC told Busways that Yorkshire Traction was the preferred bidder. Busways had not believed Yorkshire Traction's bid was genuine: it thought it was acting on behalf of United. DTC was worth more to United, its main competitor, than to anyone else. Busways could see no other reason for Yorkshire Traction having increased its bid from £925,000 to £1,440,000 despite DTC's worsening financial position. Busways said that it was clear from DBC's subsequent report that Yorkshire Traction had then sought to reduce its bid as soon as it learned of Busways' continued intention to operate in Darlington, and before it knew about Busways' recruitment of DTC's drivers, its registration of all DTC's routes, and the possibility of Busways running free services.

Plans for Stagecoach Darlington and the recruitment of drivers

10.71. After the meeting with DTC's directors on 29 September (see paragraph 10.68) Busways was invited to meet DTC's union representatives and individual employees. The workforce told Busways that they no longer had confidence in DTC's management and wanted Busways to buy DTC.

10.72. On 24 October, immediately it heard that its bid had been unsuccessful, Busways considered withdrawing from the bidding process and setting up a new operation in Darlington. But it was concerned about the availability of trained drivers. It had heard that United had been forced to delay the implementation of its July registrations because of a shortage of drivers. Busways therefore decided to offer an incentive bonus of £1,000 to any fully-trained driver prepared to join it. The cost of the bonus would be matched by savings in training costs. The following day it withdrew its bid.

10.73. Early on 25 October Mr Tait, the Chairman of DTC's branch of the TGWU, telephoned Busways' Finance Director, Mr Conroy, to say that the workforce were disappointed that Busways was not the preferred bidder. Later that day Mr Souter, who was in Newcastle on other business, and Mr Conroy met Mr Tait who indicated that a majority of DTC's drivers would probably be prepared to give in their notice immediately and agree to join Busways.

10.74. On 27 October Busways advertised for drivers in the local press. It attended a meeting with the full-time officer of the TGWU on that day to discuss the terms of employment it would offer new recruits. Mr Tait and one other DTC trade union representative were also present. Busways told them that DTC drivers who joined it would receive a 3 per cent wage increase, making their rate of pay roughly comparable with that offered by United, and a guarantee of no compulsory redundancy for three years. Busways viewed the pay increase as an important tool for improving the morale of the drivers, who had become frustrated by DTC's inability to provide them with security of employment or a stable standard of living.

10.75. Busways first interviewed prospective employees for its new operation between Friday 28 October and Sunday 30 October. Drivers were recruited on the basis of their knowledge of Darlington services and their previous employment records. The posts were open to all, but Busways believed the DTC applicants would probably be the most suitable because of their detailed knowledge of the services Busways intended to operate. It was this, coupled with their enthusiasm to work for it, that led Busways to recruit DTC employees first, before it considered other applicants. Busways did not accept all the applicants from DTC, and it subsequently recruited seven drivers from other companies and 17 from the unemployed register. It said that, if large numbers of drivers from United or Your Bus had approached it, they would have received a similar welcome to that given to former DTC employees.

10.76. The new recruits had been engaged as soon as their notice periods with their existing employers expired. For most DTC drivers recruited during the weekend of 28 to 30 October the start date was 7 November. It was true that the DTC drivers had been engaged to start before Busways had known whether the Traffic Commissioner would grant a dispensation for it to run services earlier than the normal 42-day registration period. But Busways wanted to avoid the risk that drivers' enthusiasm to join it would be dissipated by a long delay and by approaches from United or other employers.

10.77. Busways had also believed DTC was on the brink of financial collapse; if Busways did not commence operations quickly, United would have a monopoly in the town. By 30 October, 55 of DTC's total complement of 90 drivers had agreed to join it. Busways knew then that DTC would be unable to operate a full service from 7 November. Busways withdrew the `non-training bonus' and the three-year employment guarantee on 10 November, the day after DTC announced that it was going into administration. It knew that there would no longer be a potential shortage of drivers.

10.78. The intervention of DTC's workforce in the sale process had been crucial to DTC's collapse. The employees wanted to join Busways because they believed it could provide security of employment and Yorkshire Traction could not. They had communicated their views to DBC when the short-listed bidders were announced. In Busways' view it would have been commercially unthinkable to reject such willing recruits. It was true that this contributed to DTC's collapse, but its erstwhile employees had acted freely in accordance with the law and with good sense.

Registration of services and the offer of free fares

10.79. On 28 October Busways submitted its new registrations to the Traffic Commissioner. It did not have time to design a new route network and therefore replicated DTC's existing commercial routes. It submitted the new registrations to the Traffic Commissioner on 28 October, and cancelled the earlier September registrations.

10.80. The new registrations had been intended to take effect from 12 December, the same start date as the earlier ones. But Busways sought a dispensation from the Traffic Commissioner to commence its new operations from 7 November. This was because it was concerned that, in the interim, United would exploit any service gaps left by DTC's failure to operate a full service and make it more difficult for Busways to attract former DTC passengers when its services began. Moreover, some passengers would be left without any service. Busways also needed to find work for its new recruits from the date they joined, thus maintaining their morale.

10.81. Busways decided, however, that if the Traffic Commission did not grant a dispensation, it would operate free services to circumvent the need for registrations to take effect. This was solely a commercial decision. Other influencing factors included:

(a) the fact that Busways had surplus operator licence discs, enabling it to operate the required level of service;

(b) the relatively trifling costs of acting in this way;

(c) legal advice confirming the legality of the action; and

(d) the prevalence of free short-term introductory offers in other commercial sectors as a legitimate commercial tactic.

10.82. Busways began operating free services on 7 November, trading as Stagecoach Darlington. It had not expected the free-fares offer to last more than two weeks because it believed the Traffic Commissioner would grant a dispensation quickly. But he did not. DTC announced that it was seeking to go into administration two days later, on 9 November, and ceased operations on 11 November. Busways contacted the Traffic Commissioner again and was granted dispensation to run services (and charge fares) from 28 November.

10.83. The offer of free fares was not, Busways told us, Stagecoach's general policy but simply a step which was taken to meet the unique circumstances of Darlington. It was the only way, at that time, that Busways could provide a service to the public which was within the law and which the incumbent operator could not provide. It agreed that running free services for three weeks went beyond anything that could be described as an introductory offer.

10.84. Market circumstances, and the inflexibility of the Transport Act, had forced Busways to commence services before its registrations became effective. Not to have done so would have left United with a monopoly. Following its July registrations, United already operated on most of DTC's routes and could have legitimately run duplicate services to take up any demand left by DTC's departure from the market. Busways had believed, too, that the Traffic Commissioner might have been more sympathetic to granting a dispensation to United, as an existing operator in the Darlington market, to run DTC's routes. Busways' free fares offer should not be compared with the additional services provided in 1993 and 1994 by United, which had forced Your Bus out of the market and brought DTC to the brink of insolvency. The effect of Busways' three-week free-fare offer on DTC's finances was negligible in the light of DTC's poor financial position. Busways had restored fares as soon as it was able to do so and had donated its first week's takings of some £25,000 to a local charity.

10.85. Busways said that there was no prospect of Stagecoach Darlington forcing United out of the market or raising fares above a competitive level. In commenting on the OFT report (see para-graph 10.11), however, it noted that United had found it worthwhile to eliminate Your Bus (by acquisition) in December 1994, knowing that Stagecoach would also be in Darlington. In Busways' view, any suggestion that Stagecoach Darlington should not have entered the Darlington market other than on the basis that all services introduced should cover their full costs immediately would, in reality, have meant that it should not have entered the market at all. If the OFT genuinely wished large operators to compete, it was strange that Busways should have attracted such opposition by simply giving United a necessary dose of its own medicine.

10.86. Incurring losses during an initial entry phase was, in Busways' opinion, a common feature of commercial life and was unobjectionable for a market entrant not intent on forcing competitors out of business. In Darlington the losses were only short term and had to be viewed against a market in which uneconomic fares had been a feature for a considerable time. The additional cost of the free fares was minimal. As drivers had already been recruited to start employment from 7 November, the only additional costs were fuel and tyres (about £2,500 per week). Stagecoach Darlington was now trading profitably.

DTC's collapse

10.87. DTC's failure had been the result, not of any actions by Busways or Stagecoach, but of United's behaviour in running an uneconomically high level of services, which the OFT had now decided was anti-competitive; the decision of its drivers to leave, *en masse*, for better job security; and its management's poor operational and policy decisions. Busways believed the breakdown of the bidding process was largely attributable to failures on the part of DBC and its advisers. But it did not believe DTC could have survived as an independent company for more than a few months at the most. DBC had allowed the sale of DTC to be delayed until DTC was on the brink of insolvency; it had been willing to allow the value of DTC to decline and to support it financially, until it realized, too late, that even such support could not preserve DTC as a viable business. As soon as the prospect of finding a purchaser faded, DTC could not trade solvently even in the absence of additional competition from Stagecoach Darlington.

Developments in the Darlington market since November 1994

10.88. In Busways' view there was insufficient revenue to support three separate comprehensive town networks in Darlington. It was only when United had been confronted with an operator capable of surviving a fares war that economic viability had been restored to services in the town. But it was not Stagecoach's policy to enter into cosy duopolies, or any other sort of anti-competitive arrangements with any of its competitors.

10.89. West Midlands Travel bought Your Bus's vehicles in December 1994 and Busways and United agreed with DCC to reduce the number of town services with effect from March 1995. The level of service and competition on routes was now at least equivalent to that which prevailed in April 1993, before Your Bus entered the market. The service changes had brought considerable relief to Darlington residents.

10.90. Events in Darlington had demonstrated that, where financially stable operators served the same market, they would be motivated by their economic interest and the need to procure public goodwill. The problems in Darlington had resulted from a competitive imbalance between operators. The introduction of Stagecoach Darlington had rectified that problem in a manner which regulatory action never could.

10.91. One of Busways' hopes from the current inquiry was that the MMC would provide clear guidance on permissible methods for operators to enter new markets. In particular it was interested to know how it could have been expected to carve a niche in the Darlington market without hitting United hard and forcing it to revise its competitive strategy.

South Shields

10.92. Busways said that the previous intensive competition between itself and Hylton had lessened in 1989 because Busways had been concerned to maximize its more profitable routes elsewhere in the preparation for its management buy-out. It had reduced the level of its services in South Shields. Hylton had also withdrawn some routes.

10.93. Between 1990 and 1993 the South Shields division was Busways' best performer; it had therefore concentrated its efforts on other less profitable operations. During this period Go-Ahead increased its services in South Shields and became a major competitor. However, in the early summer of 1994 passenger numbers in Busways' South Shields division began to fall faster than in any other division. During discussions with Stagecoach, Busways had learned of Stagecoach's belief that market pricing could regenerate passenger numbers and that fares should be fixed at more affordable levels. Busways decided to experiment with fares in South Shields, an area of high unemployment where all bus operators were suffering passenger decline.

Introduction of new network tickets

10.94. On 5 September 1994 Busways had introduced a weekly network ticket, the `Shields Saver', for £1.99 on all services within South Shields, and the `Whitburn Saver' for £2.99 on its services E1, E2 and E3 between South Shields, Whitburn and Sunderland. These new saver tickets were available only from the driver on the bus which was made possible by the introduction of new ticketing technology. The prices compared with £5.40 (all day) and £4.35 (off-peak) for its existing weekly network ticket. The tickets had not been introduced selectively, but were available on all routes in South Shields whatever the level of competition and whoever the competitor. At the time of setting the fare levels for the saver tickets, Busways had not been aware of a proposed change of policy on concessionary fare reimbursements planned by the PTE.

10.95. The publicity for the saver tickets made it clear from the outset that they were not transferable and would be withdrawn if misused. Busways had learned from another operator that when it introduced a season ticket which could be bought from the driver, sales had increased. Busways knew there was no simple technology that would enable drivers to key-in photocard numbers to ticket machines. If it had insisted on a photocard, the drivers would have had to write photocard numbers on tickets. To do so would have been impractical.

10.96. Furthermore, because most tickets were issued on a Monday for the week, the delays which would be incurred in issuing the tickets would cause service unreliability and this was unacceptable. Busways considered the risk of transferability and took the view that, with an initial price of £1.99, the incentive to transfer the ticket was not great. It acknowledged that the tickets could be transferred without detection (no photograph or signature was required). But it had no evidence that this was happening on a widespread basis.

10.97. Shortly after the introduction of the new tickets, Busways drivers reported that passengers were confused about which ticket related to which service. But sales figures were encouraging. On 9 October the Shields Saver and the Whitburn Saver were combined in a single Shields Saver ticket at a price of £2.49, to remove the confusion and improve revenue.

10.98. In its first submission Busways told us that the introduction of the Shields Saver ticket had resulted in an increase in patronage of 14 to 16 per cent and revenues had stabilized. In the period from August 1994 to January 1995 all services had covered their variable and semi-variable costs (with two small exceptions where a seasonal reduction in revenue always occurred), and made a positive contribution to overheads. Most services had fully covered apportioned depot and central overheads. It believed the introduction of the Shields Saver had demonstrated that pricing offers could generate extra demand. It was probably true that many of the extra journeys generated had come from passengers making additional journeys rather than switching from other operators.

10.99. Despite the success of the saver ticket, Busways had been concerned that its returns in South Shields were still below target. At the end of November, when the effects of the PTE's unexpected change of policy for calculating concessionary fares reimbursement became clear (see paragraph 7.21), Busways decided to increase the price of the Shields Saver ticket as soon as practicable; its revenue expectations in South Shields had been considerably reduced. On 8 January it increased the price to £2.99.

10.100. It had still believed its services would continue to cover both variable and semi-variable costs, although their financial performance might be retrospectively depressed because of the PTE's change of policy. It had always intended to increase patronage to a level which would have more than offset the discount represented by the saver ticket-the introduction of the ticket was not intended to reduce revenue or profitability and there was no evidence that its effect had been predatory.

10.101. The increased competition from Hylton since 28 November had adversely affected Busways' trading results too. In the light of that competition, the PTE's change of policy, and the resulting revenue performance, Busways had increased the price of the Shields Saver ticket to £3.99 with effect from 26 February.

10.102. At its hearing with us, Busways said that it had struggled to find the optimum combination of patronage growth and revenue per passenger. It agreed that it had made losses since introducing the Shields Saver tickets but the losses had occurred largely as a result of the PTE's changed policy on concessionary fares, which it could not have predicted and which it was disputing with the PTE. Without the unforeseen effects on its income which had resulted from the PTE's change of policy Busways' South Shields division would probably have broken even.

10.103. In a later submission Busways told us that its whole approach to the saver ticket experiment had been one of trial and error. Its initial price of £1.99 had, with hindsight, been too low. As the PTE's intentions had unfolded and the impact of additional competition had become clear, Busways had continued to reprice the ticket to a point where, in March 1995, it had restored profitability whilst still maintaining a 10 per cent improvement in patronage.

Competition with Hylton

10.104. Busways had offered to buy Hylton in 1991. Nothing came of this but the companies agreed that they would keep in touch in case Hylton changed its mind. On 16 September 1994 Busways met Hylton and invited it to reconsider the matter. This was a follow-up to the 1991 offer and had nothing to do with Busways' acquisition by Stagecoach. At the meeting Busways told Hylton that it had merged with Stagecoach because the market was becoming dominated by a few large groups. If it had not merged with one of the big operators it might have been forced out of business by its large local competitors, particularly if United and Northumbria were to join national groups. This had not been an express or implied threat to Hylton, and Busways denied using any expression that might be so construed.

10.105. Busways had indicated to Hylton that Stagecoach wished to increase its market share in the reference area. This, too, was not a threat, but simply an explanation of Stagecoach's policy (subsequently implemented in the acquisition of Cleveland Transit and Hartlepool Transport). But Hylton was not interested in pursuing the offer. Busways' meeting with Hylton had no relevance to public interest consideration. It had simply sought to negotiate the purchase of a business. Hylton had since intensified competition with Busways. This indicated that the meeting had had no tangible effect on Hylton's willingness to compete actively with Busways.

10.106. Busways complained about a television programme (BBC *Newsnight*, 21 December 1994) which had purported to investigate Stagecoach's allegedly predatory activities, and in particular its competition with Hylton. Stagecoach had complained to the BBC about the programme and asked the MMC to disregard it in considering Hylton's allegations of predation.

10.107. Hylton resented any additional competition from Busways, and seemed to believe both companies had a tacit arrangement to maintain services broadly at existing levels. This was not the case: such an arrangement would be against Busways' and Stagecoach's policy. Busways did not believe it was the MMC's role to preserve such arrangements. Despite Hylton's concerns, Busways had not materially increased competition with other operators in South Shields.

10.108. Hylton's drivers received incentive bonuses based on fares they collected on the bus. As a result its drivers frequently operated services earlier or later than their registered times, departed from registered routes, and occasionally endangered Busways' passengers and employees by dangerous driving. They sometimes blocked access to its positions at South Shields market. Busways was not willing to operate in the same way. As a result Hylton's services often succeeded in running in front of Busways'. It believed its response had to be the provision of a better-quality service, and attractive fare options.

10.109. Three service changes had been made by Busways to its services since the merger with Stagecoach and, of these, only one was on a route where Hylton was its principal competitor. In contrast, Busways believed Hylton's recent service changes had been directed exclusively at it. Busways neither intended, nor believed it was possible, to drive Hylton from a market where Hylton had proved its ability to sustain competition for several years.

Busways' new services

10.110. On 6 November 1994 Busways introduced a new service, 18A, which extended its coverage of estates in Brockley Whins. Both the service 18A and the existing service 18 competed with Hylton. The introduction of service 18A was intended to increase Busways' patronage, but any increase in service levels and the introduction of a regular frequency was bound to be timed closely to a Hylton service at one end of the route if it was evenly spaced at the other. It was also a response to Hylton's persistent failures to operate to its registered timetables.

10.111. Busways said that on routes between South Shields and Sunderland competition from Go-Ahead, Redby and Hylton was intense. But Busways' services on this route remained amongst its most profitable. Its new service E6, South Shields-Sunderland, was introduced on 13 November. It served different communities from its existing coastline services E1, E2 and E3. In timing the new E6 service two minutes before Hylton's service 6, Busways was regaining part of the competitive advantage which had been won by Hylton in timing a service one minute before Busways' services E1, E2 and E3 from South Shields, and by filling the ten-minute gap in services from Sunderland. In Busways' view any principle that one operator had the right to operate one minute in front of another operator in perpetuity, or had the right to be left a gap in which to operate, was irrational and anti-competitive.

10.112. On 28 November Hylton had started a new service to Fellgate Estate, in direct competition with Busways' X20 service. Hylton had also increased its service frequencies on its circular services 1 and 2 (which competed with some of Busways' services). The increased competition had had an adverse effect on Busways' financial performance.

Sunderland

10.113. Commenting on its discounted return fares in Sunderland, Busways said that it had not directed the discounts at any particular operator. It was another example where it was following Stagecoach's policy of market pricing. The routes chosen were those serving housing estates in the depressed parts of the town which had what Busways believed to be the highest levels of unemployment. Since 22 August 1994, the date on which it introduced discounted fares on certain routes in Sunderland, revenues on each of the services chosen had steadily increased.

10.114. Busways told us that it regarded Redby, a competitor in Sunderland, as a typical opportunist operator which would operate a service wherever it believed a small margin could be obtained, and would cease operating that service as soon as a margin ceased to be available. Competition with Redby had been made more difficult by Redby's regular changes of route structure. It had a record of running services which did not keep to the registered routes or schedules, and of lengthy stop-overs at key bus stands to abstract passengers from other operators' services. Its drivers had a tendency to run just in front of any Busways service, irrespective of the registered schedule or route. This behaviour was encouraged by the bonuses paid to its drivers, which were linked to fares taken on the bus.

10.115. It was only in response to Redby's failure to operate its timetable that Busways had operated occasional duplicate buses. This was done to make it more difficult for Redby's buses (which departed later than their scheduled departure times) to stay in front of Busways'. Since amendments to the Traffic Regulations had come into force in February 1995, Busways had ceased running duplicates unless passenger demand warranted it.

10.116. Busways said that none of its practices in Sunderland had been designed to eliminate competition. They were introduced in response to Redby's behaviour. Busways' services in Sunderland had never run uneconomically. Its occasional use of duplicate buses had been a legal response to irregular activities on the part of another operator.

Remedies

10.117. We invited Busways to comment, on a hypothetical basis, on some possible remedies were we to find public interest detriments. Busways said that, should this be the case, it would be rational to direct any remedies at the areas of Stagecoach's operations from which the chief complaints had emanated, Darlington and South Shields, rather than throughout the reference area.

10.118. If Busways were forced to divest Stagecoach Darlington, it would look for the best available price, which would be likely to be provided by another national group with a presence in the reference area. However, any purchaser was unlikely to pay a realistic price for Stagecoach Darlington without a restrictive covenant barring Stagecoach from the area. Any such sale would therefore either bar Stagecoach from the market or result in a substantial loss to it. Busways failed to see why divestment would improve competition in Darlington. The effect of three-way competition in the town, in terms of financial performance and overbussing, had been amply demonstrated. A sale of Stagecoach Darlington was unlikely to alter that position. Divestment would result in a loss to the community and prevent Stagecoach Darlington's workforce from remaining with their chosen employer. Stagecoach had one of the best records of the large operators in controlling costs, keeping fare levels down, and investing in modern assets. Furthermore, the DGFT had concluded in his report in March 1995 (see paragraph 10.11) that he saw no case for any remedy (for United's predatory behaviour) because of the present competitive situation in Darlington (between Stagecoach Darlington and United).

10.119. We sought Busways' view on a change in the law to enable the sale by local authorities of their bus companies to proceed without risk of frustration. The change might include the banning of new registrations of bus services in the area concerned during, and for a short time after, the period of sale; and the banning of operation of free services in that area during the same period. Busways did not think a change in the law was necessary. It believed the same results could be achieved by a more confidential sales procedure and appropriate undertakings from bidders, as had already been successfully adopted by some local authority vendors. This could be further enhanced, in order to prevent an operator acting covertly on behalf of another, by the adoption of covenants which prohibited subsequent sales to third parties within a specified time period. If intensified competition was prohibited during the sale, many local authority companies would remain for sale permanently. Busways saw no reason why local authority vendors should have protection which was denied to others.

10.120. Busways had no objection in principle to a remedy under which it would give certain behavioural undertakings. But it thought some of them would be difficult to apply to an urban network where service frequencies were high, and the identification of competing services was difficult (several services operated along similar corridors). It asked us to bear in mind that the most significant competition, to it and to the other Stagecoach companies in the reference area, came from large national groups. It believed that some of the possible behavioural undertakings mentioned (eg relating to increased frequencies, reductions of fares and free services) should not be applied where it was responding to competition from operators or groups with more than about 100 vehicles in the reference area.

10.121. We put to Busways a hypothetical undertaking under which, if a competitor entered a route operated by Stagecoach in the reference area, Stagecoach would not timetable, register or operate additional or rescheduled services before the competitor's service within a shorter interval than the competitor had itself timetabled, registered or operated before an existing Stagecoach service. Busways commented that, if it was unable to register services within a shorter interval than a competitor had itself timetabled, this would provide further encouragement to operators such as Hylton and Redby to run outside their scheduled times. They would know that Busways would be unable to increase its service registrations in response.

10.122. Busways was concerned about the hypothetical undertakings under which, if Stagecoach increased its frequencies on any route or part of a route in the reference area operated by another company, or on which another company had announced its intention of operating services, and the competitor withdrew, Stagecoach would not subsequently reduce commercial frequencies for a period of at least three years after the competitor's withdrawal. It feared that competitors could seek to increase frequencies to draw Busways into a response.

10.123. It was also concerned about a possible undertaking that if Stagecoach reduced fares to below those of a competitor on any routes or part of a route in the reference areas, it would not subsequently increase fares, should the competitor withdraw, for a period of at least three years after the competitor's withdrawal. Busways believed competitors could seek to introduce cut price services in the knowledge that Busways would be forced to operate the service at a loss for three years when the competitor had withdrawn.

10.124. The hypothetical undertakings which Busways regarded as most suitable for the South Shields and Darlington markets were those under which Stagecoach would:

(a) not operate (or plan to operate) services on any routes in the reference area which did not (or would not be expected to) cover at least the avoidable costs of operating them; and

(b) not operate for a continuous period of longer than six months any services which, notwithstanding that they covered avoidable costs, did not in addition make a contribution to other costs.

The problem of identifying competing routes would not arise, and the undertakings would not give the opportunity for competitors deliberately to abuse them. But Busways believed Stagecoach should not be precluded from responding to competition from other national groups which had the financial strength to run services at a loss to obtain market share.

10.125. It could not envisage circumstances in which Stagecoach would offer a long-term free fares offer. But Busways would prefer any limitation on its being able to offer free fares as a marketing device to be extended from the one day's normal operation we had suggested to five days. It would wish, too, to have the opportunity to respond to any free-fare offer introduced by another operator.

10.126. A possible remedy that Stagecoach would not conduct recruitment compaigns in the reference area aimed at recruiting staff from particular competitors drew the response from Busways that it believed restrictions on recruitment of staff were contrary to common law principles of freedom of trade and might be subject to legal challenge on that basis. The identification of a recruitment campaign designed to recruit particular staff would be difficult, as a group response to advertisements for staff could not be excluded. And in such circumstances their trade union representatives would wish to clarify the terms available to them.

10.127. Busways said that it was Stagecoach's policy not to enter into agreements which restricted its freedom to operate in any area, at the service levels it chose, and at the fare levels it deemed appropriate. But there were circumstances where it believed it would not be in the public interest to restrict operators from co-operating to co-ordinate service reductions, or from providing joint services.