EXPLANATORY MEMORANDUM TO

THE COMPETITION ACT 1998 (PUBLIC TRANSPORT TICKETING SCHEMES BLOCK EXEMPTION) (AMENDMENT) ORDER 2005

2005 No. 3347

1. This explanatory memorandum has been prepared by the Department of Trade and Industry and laid before Parliament by Command of Her Majesty.

2. Description

2.1 This order varies and extends for a further five years an existing block exemption, established in 2001 by the Competition Act 1998 (Public Transport Ticketing Schemes Block Exemption) Order 2001 (SI2001/319). The current order, which is due to expire on 28 February 2006, provides that agreements between public transport operators on certain ticketing schemes falling within the terms of the block exemption are exempt from the prohibition in Chapter I of the Competition Act 1998. In addition to extending the block exemption to 28 February 2011, this order also makes two substantive changes to the block exemption: reducing the degree of prescription over revenue sharing arrangements between operators providing multi-operator travelcards and removing the requirement on operators to provide their own single and return tickets in addition to providing multi-operator individual tickets.

3. Matters of special interest to the Joint Committee on Statutory Instruments

3.1 None.

4. Legislative Background

4.1 Chapter I of the Competition Act 1998 (the Act) prohibits decisions, practices and agreements by parties that would have as their object or effect, the prevention, restriction or distortion of competition or trade within the United Kingdom (or any part thereof).

4.2 Section 9(1) of the Act sets out the conditions whereby a restrictive agreement is exempt from the Chapter I prohibition.

4.3 Section 6 of the Act empowers the Secretary of State, acting on the recommendation of the Office of Fair Trading (OFT), to make a block exemption order exempting from the Chapter I prohibition agreements that fall within a category the OFT considers are likely to satisfy the conditions for exemption set out in Section 9(1) of the Act.

4.4 On 8 February 2001, the Secretary of State exercised this power by making the Competition Act 1998 (Public Transport Ticketing Schemes Block Exemption) Order 2001 (SI2001/319).

4.5 As required under Section 8(4) of the Act, the OFT has consulted on its proposals for varying and extending this existing order before making a recommendation to the Secretary of State under Section 8(3) of the Act.

5. Extent

5.1 This instrument applies to all of the United Kingdom.

6. European Convention on Human Rights.

6.1 As the instrument is subject to negative resolution procedure and does not amend primary legislation, no statement is required.

7. Policy Background

7.1 In 2001, the then Director General of Fair Trading (now Office of Fair Trading) concluded that agreements between public transport operators on certain types of integrated public transport ticketing schemes were likely to satisfy the conditions for exemption set out in Section 9 the Act. Ticketing schemes are considered to promote higher quality bus services and transport networks and improve the viability of public transport networks with resultant reductions in road congestion, air and noise pollution. Following a public consultation, the OFT recommended the Secretary of State make a block exemption order for such agreements, providing greater legal certainty for operators and avoiding the need for large numbers of benign agreements to be notified unnecessarily to the OFT.

7.2 The OFT continues to consider that the benefits ticketing schemes bring to the consumer outweigh any negative effects such schemes have on competition. Following consultation[2], the OFT considers the block exemption for such agreements should be extended so as to retain the legal certainty it provides. While the move to a legal exception regime for agreements (effective from 1 May 2004), means the original concern about unnecessary notification to the OFT of benign agreements no longer applies, the OFT is concerned that a decision not to extend the block exemption may have the effect of dissuading operators from participating in ticketing schemes. Operators and local authorities might misinterpret a decision not to extend the block exemption as an indication that the OFT considers such schemes no longer meet the criteria for exemption. Removal of the block exemption would make it difficult for the OFT to convey the change in approach about how it considers ticketing arrangements should satisfy the exemption conditions in Section 9(1) of the Act. This could lead to significantly greater resources being expended by the OFT to provide informal guidance on the matter than would be required if the block exemption were varied.

7.3 Ticketing schemes covered by the block exemption are multi-operator travel cards (MTCs), through tickets (TTs), multi-operator individual tickets (MITs), and short and long distance add-ons.

[2] Competition Act 1998 – Public Consultation on proposals to recommend the varying the public transport ticketing schemes block exemption – 1 April 2005

7.4 In addition to extending the duration of the block exemption for a further five years to 28 February 2011, this order also varies the block exemption in two ways. The first is to replace the current condition that revenues from MTC schemes must be distributed, as far as possible, on the basis of passenger miles with a less prescriptive condition that allows any method provided it does not create an incentive for operators to set their own fares higher than they would have been in the absence of the MTC, and does not significantly reduce the incentive for operators to compete for passengers. Respondants to the consultation strongly supported the OFT's conclusion that a more flexible approach would not incentivise operators to increase their own single and return fares while still enabling efficient and equitable sharing of MTC revenues.

7.5 The second variation is to remove the requirement that operators offer for sale tickets that are valid for use only on their own services in addition to selling MITs valid on the services of all operators on the route. The sale of tickets that can be used only on an individual operator's services was included as an additional restraint on MIT prices. However, the OFT has accepted the argument that there is sufficient competition between operators on the price of MITs to mean the additional restraint is not required.

8. Impact.

8.1 A regulatory impact assessment is attached to this memorandum.

9. Contact

9.1 Paul Bannister at the Department of Trade and Industry Tel: 020 7215 5009 or e mail: paul.bannister@dti.gsi.gov.uk can answer queries regarding the instrument.

dti

Regulatory Impact Assessment

The Competition Act 1998 (Public Transport Ticketing Schemes Block Exemption) (Amendment) Order 2005

1 December 2005

URN 05/1900

dti

The DTI drives our ambition of 'prosperity for all' by working to create the best environment for business success in the UK. We help people and companies become more productive by promoting enterprise, innovation and creativity.

We champion UK business at home and abroad. We invest heavily in world-class science and technology. We protect the rights of working people and consumers. And we stand up for fair and open markets in the UK, Europe and the world.

ORDER VARYING THE PUBLIC TRANSPORT TICKETING SCHEMES BLOCK EXEMPTION

Purpose and intended effect of the Order

I. In 2001, the then Director General of Fair Trading (now Office of Fair Trading) concluded that agreements between public transport operators on certain types of integrated public transport ticketing schemes were likely to satisfy the conditions for exemption set out in section 9 the Act. Ticketing schemes are considered to promote higher quality bus services and transport networks and improve the viability of public transport networks with resultant reductions in road congestion, air and noise pollution. Following a public consultation, the Office of Fair Trading ('OFT') recommended the Secretary of State make a block exemption order for such agreements, providing greater legal certainty for operators and avoiding the need for large numbers of benign agreements to be notified unnecessarily to the OFT.

II. The purpose of this order is to extend by a further five years the existing Competition Act 1998 (Public Transport Ticketing Schemes Block Exemption) Order (SI 2001 No 319) ('the block exemption') and introduce certain amendments to it. The block exemption allows operators to develop integrated ticketing schemes subject to conditions designed to maintain competition and protect the interests of passengers. The amendments this order introduces are intended to make it easier for bus operators to develop integrated ticketing schemes, particularly travelcards.

OFT's Public Consultation

III. In April 2005, pursuant to sections 8(1) and 8(4) of the Competition Act 1998 ('the Act'), the OFT consulted interested parties on proposals to extend and make amendments to the block exemption in the consultation paper set out in the OFT consultation paper *Proposals to recommend varying the public transport ticketing schemes block exemption* ('the Consultation Paper')[1]. The Consultation Paper was sent to 276 public transport operators and organisations with an interest in public transport. The OFT received a total of 22 responses, mostly from bus operators and local authorities. All respondents agreed that without the block exemption, there is a risk that operators would not choose to participate in ticketing schemes. There was also broad support for the other amendments OFT proposed to make to the block exemption. A summary of the responses that the OFT received is contained in the *Recommendation to vary the public transport ticketing schemes block exemption*[2].

[1] The consultation paper is available from http://www.oft.gov.uk/nr/rdonlyres/056d25ee-7c59-4759-896b-720763073525/0/oft784.pdf

[2] The document is available from: http://www.oft.gov.uk/NR/rdonlyres/D00DB623-9B61-43F3-8827-57C4BED3DD5E/0/oft817.pdf

Options

IV. In broad terms the options available to the Secretary of State concern the following questions:

- Whether or not to allow the block exemption to expire;
- Whether to extend the duration of the block exemption by the further 5 years OFT recommends or for another period of time; and
- Whether to make the amendments to the block exemption recommended by the OFT or to make different amendments or none.

Reasons for extending the block exemption

V. The original block exemption has operated for nearly 5 years and is due to expire on 28 February 2006. In its Consultation Paper, the OFT sought views on the extent to which there is a continued need for a block exemption and whether the types of integrated ticketing schemes under consideration continued to satisfy the conditions for exempt agreements under the Act.

VI. The OFT's recommendation (see footnote 2) is that the block exemption should be extended - giving the following reasons:

- There are no alternative means of concluding ticketing agreements that could provide greater benefits to passengers. Respondents to the OFT's Consultation Paper unanimously agreed that this is the case;
- The benefits to consumers from ticketing schemes are much greater than the benefits the operators obtain from them. Any barrier to participation, either actual or perceived, is likely to discourage operators from establishing new schemes. All respondents to the OFT's Consultation Paper agreed that without a block exemption there would be a risk to the establishment of new schemes. The majority of respondents indicated that without a block exemption there is also a risk that operators would not participate in existing schemes. Local authorities, who are often the driving force in the introduction of these schemes, indicated in their responses to the OFT that, absent a block exemption, operators are likely to consider that entering into such arrangements is too risky;
- The additional protection the block exemption provides against enforcement action under the Act was an important factor in encouraging transport operators to enter into ticketing scheme agreements. The OFT expressed concern that a decision to allow the block exemption to expire rather than

extend it might be taken as an indication that it considers such schemes are no longer appropriate. This would have the effect of deterring operators from participating in such schemes; and

- If the block exemption was allowed to expire, it would make it difficult for the OFT to convey the change in approach to how the OFT considers ticketing arrangements should satisfy the Section 9(1) conditions. This could lead to significantly greater resources being expended by the OFT in providing informal guidance to local authorities and operators than would be required if the block exemption remained in place and was varied.

VII. Additionally, the OFT took the view that it is appropriate to have a block exemption for ticketing schemes because they continue to satisfy the conditions for exempt agreements set out in section 9(1) of the Act and that the benefits of these types of ticketing agreements are likely to outweigh any negative effects on competition. A detailed discussion on the extent to which ticketing schemes fulfil these four conditions is set out in the OFT Consultation Paper.

VIII. The Secretary of State agrees with the arguments made by the OFT and does not consider it appropriate to allow the block exemption to expire in February 2006.

Reasons for extending the duration of the block exemption by five years rather than another period

IX. The OFT considered proposals for extending the block exemption for a period of more than five years, for example 10 years. However, this would have given the block exemption a total duration of more than 15 years which would have been inconsistent with the general approach taken with regards to EC block exemptions. These typically have a duration of 10 years. The OFT concluded, that a five-year period would provide sufficient legal certainty to enable operators to invest in ticketing schemes, while allowing for the opportunity for subsequent review to consider changing circumstances.

X. The Secretary of State agrees that 5 years is the optimum time period for which to renew the block exemption.

Reasons for amending the block exemption as recommended rather than make other amendments or none

XI. The OFT recommended to the Secretary of State that two substantive changes be made to the block exemption:

- the current condition requiring revenue distribution for multi-operator travelcard (MTC)[3] schemes to be on the basis of "passenger miles, as far as reasonably practicable" be replaced with a less prescriptive condition, allowing any method provided (a) it does not create an incentive for operators to set their own fares higher than they would have been set in the absence of the MTC, and (b) it does not significantly reduce the incentive for operators to compete for passengers; and

- the requirement for operators to sell their own operator tickets when they issue multi-operator individual tickets (MITs) be removed[4].

XII. The OFT's recommendation to the Secretary of State was slightly different from the proposal originally set out in the Consultation Paper. The differences, which reflect concerns expressed by respondents to the consultation, are that OFT now considers:

- it is not necessary to continue to require operators to offer tickets that may be used only on the individual operator's services in addition to the MIT, valid for use on the services of all operators on the route; and

- rather than include a condition relating to the setting of MTC prices in the block exemption which may not be appropriate in all circumstances, it would be better to provide explanatory text and examples in revised guidance setting out what operators should avoid doing when setting MTC prices.

XIII. The OFT has received strong support for its proposed change to the method of distribution of revenue arising from the MTC. Respondents to the OFT's Consultation Paper agreed that the OFT's flexible approach to the method in which MTC revenue is distributed would not incentivise operators to increase their own single and return fares, while still enabling operators to share revenue on an efficient and equitable basis. Respondents to the 2003 review of the block exemption had indicated that the condition that revenue should be distributed on the basis of passenger miles had increased the cost and complexity of operating such schemes.

XIV. The OFT considers that it is not necessary to have a requirement that operators must offer their own ticket allowing the same journey to be made as a MIT. The rationale for requiring operators to provide their own single and return tickets was to provide an additional constraint on the price of the MIT. However, the result of the consultation and the OFT's analysis indicates that competition between operators on the price of the MIT should provide a sufficient constraint. The

[3] MTCs entitle the holder to make multiple journeys on a number of different operators' services across a number of different routes.
[4] MITs entitle ticket holders, where two or more different operators provide services on the same route, to use whichever service they choose.

combination of the conditions in the block exemption providing that revenue lies where it falls and that the price of MITs cannot be agreed amongst operators provides operators with an incentive to compete. Moreover, the OFT considers that if a MIT is priced above the competitive level then it would be open to operators to introduce their own tickets priced at a level below the price of the MIT. Therefore, the potential for individual operators to offer their own tickets provides an additional constraint on the price of MIT.

XV. The OFT consulted on whether there are any alternatives to the ticketing schemes covered by the block exemption that would provide greater benefits to consumers. The majority of respondents indicated that they could not think of any alternative schemes that could provide greater benefits to consumers. Only one respondent identified some other ticketing schemes that could provide some benefits to consumers, although this would have been to a smaller more specialised group, and as a result was not considered any further.

XVI. The Secretary of State does not consider that any other substantive changes need be made to the block exemption other than those recommended by the OFT. The Secretary of State has informed the OFT of some minor modifications made to Article 11 of the block exemption and has taken OFT's comments into account.

Minor variations

XVII. The OFT also recommended the following minor changes to the block exemption[5]:

- the definition of 'register' in Article 3 should be amended so that it refers to the OFT's Rules which have replaced the Director's rules;
- Article 21 should be amended so that the provisions by which the OFT must give notice in writing if it wishes to cancel the block exemption in respect of a particular scheme reflect similar provisions in the OFT's Rules for giving notice in writing; and
- A typographical error in Article 8 should be corrected so that the text 'object or effect or limiting' is replaced with 'object or effect of limiting'.

XVIII. These changes have been accepted by the Secretary of State.

Risk assessment

[5] Article 19 is amended to refer to section 9(1) rather than section 9 of the Act, in accordance with changes to the Act made by the *Competition Act 1998 and other enactments (Amendment) Regulations 2004.*

XIX. The amendments change some of the conditions in the existing block exemption but do not create significant new risks. While the agreements entered into by operators are likely to be restrictive of competition, the OFT considers that as the schemes will satisfy the conditions in section 9(1) of the Act, any detriment to competition will be offset by the benefits to passengers. A detailed analysis of the risks and benefits under the section 9(1) conditions of the Act is provided in Chapter 4 of the OFT's Consultation Paper.

Economic assessment of the amendments

XX. The OFT considers the amendments to the block exemption will result in more ticketing schemes being agreed, delivering economic benefits to transport users and prospective passengers, in particular through quicker journey times, improved transport networks, lower costs and improved services. Benefits to transport operators include improved incentives to make investments and improved security against fraud. The amendments will continue to allow for competition between operators, ensuring that the benefits to passengers arising from such competition are retained.

XXI. The OFT considers that the amendments do not impose significant implementation costs on the transport operators as they are free to participate in schemes or not depending on their own interests. Extending the duration of the block exemption should provide legal certainty for operators helping to keep the costs of participating to a minimum. The introduction of less prescriptive requirements on methods of distributing MTC revenues will give greater freedom to operators to design mechanisms that are cost efficient and appropriate to their needs. Removing the requirement on operators to sell their own operator tickets when they issue MITs are likely to result in reduced costs to operators, for example in terms of reduced administration costs.

Social and Environment assessment

XXII. Amending and extending the block exemption in this way is expected to encourage more ticketing schemes, promoting greater use of public transport and delivering associated environmental benefits. Improved public transport networks also improve social cohesion and inclusion, particularly for the less affluent.

Impact on equity

XXIII. The amendments apply to all operators participating in ticketing schemes. The block exemption requires that schemes do not, directly or indirectly, have the object or effect of preventing any operators from participating in schemes (this includes ensuring that the costs and benefits of schemes are shared according to an assessment of each operator's contribution to the scheme).

Monitoring and review

XXIV. The OFT recommends extending the duration of the block exemption by five years to 28 February 2011 but plans to review the case in 2009 to consider changing circumstances.

Summary and recommendation

XXV. Following consultation, the OFT considers that the risks of reduced competition arising from an increased number of ticketing agreements will be outweighed by the benefits to passengers from improved services and other benefits and that the amendments to the block exemption will continue to allow for competition, ensuring passengers continue to benefit from lower prices and improved services.

DECLARATION AND PUBLICATION

I have read the regulatory impact assessment and I am satisfied that the benefits justify the costs

Signed Gerry Sutcliffe **Date 5th December 2005**

Gerry Sutcliffe
Parliamentary Under-Secretary of State for Employment Relations and Consumer Affairs
Department of Trade and Industry

Contact
Jonathan Cook
Assistant Director – Mergers & Competition Regime
Consumer and Competition Policy Directorate
Department of Trade and Industry
1 Victoria Street
SW1H 0ET
Tel: 020 7215 5514
Fax:020 7215 2837