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28 September 2007

Dear Sir or Madam,

Consultation conclusion: Market Study prioritisation criteria

1. On 29 June 2007, we consulted on our proposed market selection criteria for Phase 1 in-house desk studies. Following broadly positive feedback, we will apply the criteria as proposed. They are annexed for reference.
2. We received seven responses to our consultation: from rail service providers, Passenger Focus, and other regulators¹. The main focus of these responses was positive, and supported our aims in reviewing markets and in providing further detail on how we will select markets for review. The responses are available on our website.
3. Clarification was, however, requested on a number of points relating to the criteria and our processes. This is provided below.
4. A number of respondents² considered that we should take into account the possible cost and disruption to business. Porterbrook, in particular, thought that we should also consider whether possible problems could have alternative resolution by way of a changing regulatory or market environment. The Office of Fair Trading (OFT) identified the alternative options of taking sector-specific or competition enforcement action.
5. These concerns arise from a possible misunderstanding of what an ORR Phase 1 study is and what it is setting out to achieve. An ORR Phase 1 study is a short (one to two month desk study), which does not generally involve external parties. Its aim is to harness all readily available material to assess what further review is needed, if any. It does not, therefore, represent a burden on business. On the contrary, it is used to help us decide

¹ HSBC Rail (UK) Ltd. (HSBC), National Express Trains Division, Network Rail, Porterbrook, The Water Services Regulation Authority (Ofwat) and The Office of Fair Trading (OFT)

² HSBC, Porterbrook and Network Rail

whether it would be proportionate to progress to a Phase 2 Market Study which will inevitably incur some resource cost to industry parties.

6. We developed the criteria for the specific purpose of prioritising markets within our rolling review programme and to ensure that our resource is utilised effectively and where it is likely to achieve best value. This we believe accords with Network Rail's view of the importance of the desk study phase³.

7. We note Network Rail's view that in some circumstances it would be appropriate for ORR to seek stakeholders' views on the extent to which a proposed market study would interact with other initiatives and the extent to which it would help to improve overall railway value for money. We agree that input from the industry will help to ensure that our approach remains focused and effective and we will look for opportunities to harness external expertise and knowledge in this way. One such opportunity will be when we consult on our business priorities for 2008-09.

8. National Express has quite correctly pointed out that when conducting a Phase 1 study it would appear restrictive to limit ourselves to information and material in the public domain. We will, of course, have access to material provided to us in the exercise of our regulatory functions and there may be circumstances in which our Phase 1 study will be informed by a detailed complaint. Our April 2006 guidance on our approach to reviewing markets sets this out.

9. HSBC has asked for clarity on the circumstances in which the Phase 1 stage will be shorter than our published timescales of one to two months. The existence of a detailed complaint and/or the existence of detailed information held internally could enable us to progress to a Phase 2 Market Study very quickly.

10. The OFT has asked us to consider clarifying whether the proposed criteria will only apply at Phase 1. The criteria will be equally important to a Phase 2 study as will a consideration of proportionality, potential disruption to business and the appropriateness of conducting a Phase 2 Market Study in the light of other factors such as those identified by Porterbrook and the OFT (and referred to above at Paragraph 4). At the start of a Phase 2 Market Study, we will typically publish a provisional timetable and scope of the review. This document will also summarise our reasons for undertaking the study.

11. The OFT has, however, observed that our role as a regulatory body as well as a competition authority is sufficiently different to its own to justify a slightly different approach

³ Paragraph 7 of Network Rail's response.

to the prioritisation of markets for review. Ofwat has confirmed that the factors it will take into account, as a fellow sectoral regulator, in choosing markets to focus on in its '*Review of Market Competition in the water industry*' are consistent with those that we propose to adopt.

12. Several respondents⁴ sought more clarity on the weight we intended to assign to each criterion. Firstly, it is not necessary for all of the criteria to be met in order to prompt a study. In the absence of any competing priorities, for example, we would consider reviewing a market which met only one. Secondly, the criteria are not in any order of importance and the weight we assign to them in any particular circumstance will depend on a number of factors including the extent to which each criterion is met. For example, it is possible that there will be a set of issues where the level of stakeholder concern, in our opinion, outweighs any potential detriment. Similarly, an issue which has come under review at a European level might lead us to prioritise a market even though no concern has been raised domestically.

13. HSBC sought clarity on paragraph 6 of our consultation where we list a number of possible sources of information about markets to review. It queried whether the list indicated circumstances which would prompt a review without application of the criteria. A receipt of a 'super-complaint' of course brings with it certain statutory duties, including the duty to publish a response within 90 days setting out how we propose to proceed. This duty does not extend to us being obliged to take any action following that initial review but does oblige us to consider the complaint. We would characterise this initial review as a Phase 1 study, and can, therefore, confirm our duties under section 11 of the Enterprise Act 2002 would, in this instance, preclude the application of the criteria.

14. No such duties apply when a Phase 1 study is prompted by other more general sources of information listed. We are unable, therefore, to envisage circumstances in which the criteria would not be relevant.

15. Passenger Focus also wished to point out that under section 76 of the Railways Act 1993 it has a duty⁵ to refer matters to the Secretary of State, which it has not been able to resolve by the other statutory means available to it. If the Secretary of State considers it appropriate, he has a duty to refer the matter on to ORR. We then have the discretion to exercise those of our powers that we consider appropriate. Depending upon the circumstances of the case, we may decide to use our market review process to deal with the issue raised by such a referral.

⁴ HSBC Rail (UK) Ltd., National Express Trains Division and Network Rail

⁵ A duty which extends to London Travelwatch.

16. Passenger Focus and Network Rail welcomed criterion 4c, which states that we will take into account the level of stakeholder (including public) concern about particular markets as part of our selection criteria. In relation to this criterion, Ofwat noted that a risk of studying markets on the basis of stakeholder concerns is that stakeholders can have different interests and some stakeholders' priorities might not be primarily the development of effective competition. We note this risk, and welcome Ofwat's view that consideration of stakeholder views within the context of our other four criteria will facilitate better prioritisation of markets for review.

17. Following this public consultation we have not received any comments that would prompt us to amend our criteria, and they will, therefore, be applied to the selection of markets. We will keep the criteria and our approach to reviewing markets under review, publishing updates as appropriate in light of experience.

Suggested markets for review

18. National Express and Passenger Focus have made some helpful suggestions as to markets which we should consider under our newly adopted criteria. In this regard, we note that Passenger Focus identifies car parking at stations as an area for possible review. We are currently undertaking some work to review the scope for excessive pricing in a franchised passenger service context and this includes pricing at station car parks.

Yours faithfully

Annette Egginton

Annex

Office of Rail Regulation Market Study Prioritisation Criteria

- (a) The scale and significance of the possible problems (measured, for example, by market size or value or by the size of the potential detriment) and their contribution to whole industry costs, or significance to productivity and economic growth.
- (b) The extent to which studying this market adds value to our other business priorities.
- (c) The level of stakeholder (including public) concern about this market.
- (d) The extent to which studying this market presents us with an opportunity to influence external policy.
- (e) The extent to which knowledge of the market would progress our responsibilities to keep the supply of railway services under review and to fulfil our monitoring role under EU-driven legislation.