

Statement to Parliament: Update on the East Coast, West Coast and East Midlands rail franchises

On 10 January I informed the House that my department was preparing contingency plans for running train services on the [East Coast](#) in the event of the existing franchise failing. Despite delivering significant returns to the taxpayer and having some of the highest passenger satisfaction scores in the country, the lead operator of the franchise, Stagecoach, has been incurring significant losses.

In that debate I promised to return to the House to provide an update statement on the situation, and I am doing so today (5 February 2018).

Since 2015 the franchise has met all its financial commitments to the taxpayer, returning nearly £1 billion to the public purse. But this has come at a substantial cost of nearly £200 million to Stagecoach.

I have already informed the House that the franchise will in due course run out of money and will not last until 2020. But it has now been confirmed the situation is much more urgent. It is now clear that this franchise will only be able to continue in its current form for a matter of a very small number of months and no more.

Last week, following detailed analysis, my department issued the franchisee with notification that the franchise had breached a key financial covenant.

Now, it's important to be clear with the House, this will not impact on the railway's day-to-day operations. The business will continue to operate as usual with no impact on services or staff on the East Coast.

But it does mean I will need to – in the very near future – end the contract and put in place a successor arrangement to operate this railway.

Given the imminent financial pressure the existing franchise is under, I am taking action now to protect passengers who depend on these train services and ensure continued value for money for taxpayers.

And, given the urgency of the situation, I would like to take this opportunity to update the House on my plans.

Our [franchising system](#) as a whole has delivered great benefits to passenger:

- new private investment totalling £6.4 billion over the last 11 years
- passenger journeys on the rail network have more than doubled

The private sector is paying for new trains all round the country.

There has been much misinformation about this franchise so it is worth

stressing again at the outset that – because payments to the government have been subsidised by Stagecoach – the taxpayer has still profited financially from this franchise. Passenger satisfaction is high and preparations are well under way to deliver state-of-the-art new trains on the route.

The problem is that Stagecoach got its numbers wrong. It overbid and is now paying a price.

Contrary to widespread speculation, no deal has been done and I have not yet made a decision on the successor operator to run the East Coast railway until the long-term plans for the integration of track and train can begin in 2020. There is no question of anyone receiving a bailout. Stagecoach will be held to all of its contractual obligations in full.

As the [Brown Review](#) said 5 years ago, this is what you would expect in a competitive franchise system – private businesses risk substantial amounts of their own capital, and if they fail to live up to their stretching targets they lose out, not the taxpayer.

To anyone who thinks that the nearly £200 million that Stagecoach will lose is insignificant, let me put it into some context. The combined profit of every single train operator in the country was only £271 million last year. The loss equates to over 20% of Stagecoach's total market value. So it is a significant amount of money by any measure, and it should also act as a stark warning to any company tempted to over-bid in future. Moreover the franchising system has been adjusted to further deter over optimism when bidding.

The priority now is to ensure the continued smooth running of the East Coast franchise for its passengers.

I have therefore asked my officials to conduct a full appraisal of the options available to the government to ensure continuity of service until we implement the East Coast Partnership on the route from 2020.

My decision on which option to choose will be made in accordance with the key principles set out in the statement on how I use my rail franchising powers. This includes:

- protecting the interests of passengers
- preserving the interests of taxpayers, by ensuring value for money
- supporting investment and improvement in the railway, including the deployment of the new Intercity Express trains on the East Coast

In order to inform this decision, the department will assess the extent to which each option performs against these principles. Our value for money assessment will be based on a number of criteria, including which option returns most money to the taxpayer, the risks attached to each, and the value of any improvements in passenger services.

I will also have regard to the effect of my decision on other franchises.

This decision will be taken in a transparent way. The department's assessment

of the options will be published and will include be properly validated.

At this stage, one of the options is to consider the possibility of Stagecoach continuing to operate services on the East Coast under a very strictly designed and short-term arrangement. The current management has a strong record of customer service and to rule out their involvement now would go against the principles I set out above.

However, given the circumstances in which the government is having to step in to protect passengers on this line, I am only prepared to consider this option on the basis that the franchise would be operated on a short-term, not-for-profit basis. The only acceptable financial reward for Stagecoach would be received at the end of the contract and only in return for clearly specified passenger benefits being delivered. The company cannot be allowed to continue running this franchise and making a profit given what has happened. They got their sums wrong and they will pay the price for that – not the taxpayer.

The alternative option is that the East Coast franchise would be directly operated by the Department for Transport through an Operator of Last Resort. My department will subject this option to the same rigorous assessment to establish whether it will deliver value for money for taxpayers and protect the interests of passengers. This option is currently on the table and will be selected if the assessment that I have set out determines that it offers a better deal for passengers and taxpayers than the alternative.

In either scenario, the East Coast Mainline is expected to deliver substantial revenue to the taxpayer. The line will also continue to deliver premium payments to the government once the East Coast Partnership is in place from 2020. Let me be absolutely clear: the East Coast franchise will deliver a healthy operating profit for taxpayers. It has over the course of this franchise so far and it will in the future.

Mr Speaker, there will be those who claim that because Stagecoach overbid, it should be excluded from bidding for future franchises. The legal advice on this is clear.

As Stagecoach is meeting its financial obligations to support the franchise, including with the full parent company support, and because it has operated the services on the East Coast successfully, the department has concluded that there are no adequate legal grounds to restrict it from bidding on current and future franchise competitions on this basis.

I will therefore follow that legal advice. But let me be clear – we will keep its eligibility for current and future bids under close scrutiny and constant review.

Mr Speaker, it is vital that we continue to focus our attention on delivering benefits for passengers across the network and secure the benefits of privatisation.

So, in addition to the transparent, rigorous process I have set out for the

East Coast, I am making some additional franchising announcements that will deliver benefits to passengers on the [West Coast](#) and East Midlands routes.

In December 2016, we set out our plans to award the [West Coast Partnership](#) – the franchise that will deliver the first passenger services on HS2. In that announcement, we made clear our intention to agree a short direct award with the incumbent to allow us the time necessary to design the West Coast Partnership.

These negotiations have been completed and we have agreed a direct award with the existing operator, Virgin Trains West Coast.

Let me be clear, the East Coast and West Coast franchises should not be confused. As with the East Coast, the operator is meeting all its financial obligations, but the West Coast franchise has a completely different corporate structure, where Virgin Trains is the majority shareholder.

As set out 14 months ago, this is a sensible bridge between the existing contract and the West Coast Partnership – and once that partnership is ready this direct award will cease to exist.

Virgin has transformed the West Coast from a poorly-performing service requiring a subsidy of over £75 million a year to the franchise with one of the highest passenger satisfaction rates, at 91%, and returning over £200 million per year to the taxpayer.

This has included introducing trains every 20 minutes between London and Manchester and London and Birmingham, hourly services between London and Scotland, installing wifi on all trains, lengthening Pendolinos from 9 to 11 carriages to accommodate growing passenger numbers, and introducing a free at-seat entertainment service.

My decision is also in keeping with the 3 key principles I set out earlier in protecting passengers, ensuring value for money and supporting investment. I look forward to the release of the invitation to tender for the West Coast Partnership in due course and I am confident we will see strong competition for this exciting new franchise, which will help transform rail travel in this country through the delivery of the first HS2 services.

We are also transforming the [East Midlands franchise](#) in the coming years, with the biggest investment in the Midland Mainline since it was completed in 1870.

Passengers will benefit from more seats, new trains and dramatically reduced journey times from Nottingham and Sheffield to London. Once complete, there will be almost twice as many seats into London St Pancras in the peak compared to today.

The next operator will be required to deliver many of these improvements so I am today setting out the next step of the competition that will award this new contract.

Abellio, Arriva, Stagecoach (the current incumbent) and a joint venture

between First and Trenitalia have all been shortlisted to run the East Midlands franchise that will deliver these improved services.

As I have previously said, the government has no adequate legal grounds to restrict Stagecoach from bidding. But the competition will be run on a fair, transparent basis, including new safeguards against overbidding. Ultimately, the winner will be the firm that offers the best service to passengers and best value to the taxpayer.

Mr Speaker, in a competitive market, franchises will sometimes fail. When that happens my duty is to protect passengers and taxpayers and ensure continued investment in the railway. Stagecoach has paid the price for failure as stipulated in its contract. Passengers on the East Coast Mainline can be assured that services will continue as normal. This government will undertake a transparent appraisal of the options available to ensure passengers and taxpayers are protected.

Passenger numbers have doubled.

We have one of the safest railways in Europe.

Passenger satisfaction is high across the network.

And other countries are now adopting Britain's model for running the railways.

The plans I have set out today will allow the British public to continue to benefit from an ever improving railway into the future.