

SPECIAL DELIVERY 9AM

Secretary of State for Transport
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Your Ref:

Our Ref: RWS/EAK/00173458/1

Date: 16 April 2018

Dear Sir

Pre-action letter – Bring Back British Rail re a proposed claim for judicial review

This letter has been prepared under the Pre-Action Protocol for Judicial Review (“**the Protocol**”) and accordingly adopts the form set out in the Annex to the Protocol.

Summary

We represent Bring Back British Rail (“**the Proposed Claimant**”).

The Proposed Claimant is very concerned about the Secretary of State’s position that the complete failure of the East Coast franchise does not constitute a reason to restrict the ability of and / or prevent Stagecoach or Virgin, the operators of the franchise, from qualifying for, bidding and / or otherwise obtaining current / future franchise awards. Each of Stagecoach and Virgin hold and have been allowed, to date, to retain Passports allowing them to qualify for current and future rail franchises despite the failure of the East Coast franchise.

The Secretary of State is asked to treat the wholesale failure of the East Coast franchise as a reason to revoke the Passports held by Stagecoach and Virgin. In the alternative, he is invited to at least suspend those Passports pending a full investigation of what went wrong and satisfactory evidence from the operators that all necessary steps have been taken to ensure that it cannot happen again, i.e. that they are suitable operators to hold the significant benefits of rail franchising passports.

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The proposed claim

1. **To:** Secretary of State for Transport (the “**SoS**”), Department for Transport, Great Minster House, 33 Horseferry Road, London SW1P 4DR
2. **The claimant:** Bring Back British Rail, <https://www.bringbackbritishrail.org/>
3. **The defendant’s reference details:** to be confirmed by the Defendant
4. **The claimant’s legal advisers:** Leigh Day, Priory House, 25 St John’s Lane, London EC1M 4LB
5. **Interested parties:** Stagecoach Group plc; Inter City Railways Limited; East Coast Main Line Company Limited and Virgin Holdings Limited. Please confirm you agree with this list and/or let us know if you think others should be added.
6. **The details of the matters being challenged:**
 - 6.1. The Secretary of State’s:
 - 6.1.1. decision not to and/or continuing refusal to revoke the rail franchising Passports held by the failed operators of the East Coast Line in response to the franchise failure;
 - 6.1.2. failure to suspend the Passports and / or conduct an investigation into what went wrong on the East Coast Main line. In particular, only after a full and thorough investigation of what went wrong and what steps the operators have taken to prevent a recurrence of such a failure can an informed decision be taken on whether Stagecoach and Virgin should continue to hold and/or be re-awarded Passports; and / or
 - 6.1.3. decision not to and / or the fettering of his discretion to take account of the East Coast franchise failure in relation to the award of current and future franchises.

7. Background

(1) *The Proposed Claimant*

7.1. Since 2009, the Proposed Claimant has been campaigning for a re-unified, publicly-owned national rail network run for public benefit. The Proposed Claimant's aim is to highlight the negative consequences of the privatisation of essential public services, specifically public transport.

(2) *The East Coast franchise*

7.2. In 2015, the East Coast franchise was awarded to a consortium made up of Stagecoach (90%) and Virgin (10%). The franchise agreement is dated 9 December 2014, and was between the SoS, Inter City Railways Limited and East Coast Main Line Company Limited.

7.3. As Stagecoach explained in its own press release following the award of the franchise:

“The new franchise will start in March 2015 and is planned to run until 31 March 2023, with the option for a one-year extension at the DfT's discretion. It includes a commitment to deliver £2.3bn* in real terms in premium payments to the Government between 2015 and 2023, providing a higher return to the taxpayer than under the current arrangements.”¹

7.4. As set out below, the SoS announced the failure of the franchise in February 2018, with the franchise to end imminently. Thus, the franchise reached the point of failure within circa 3 years of its commencement, and 5 years before the agreement was supposed to expire.

7.5. It also failed circa 2 years before the new end date set for the franchise agreement as recently as November 2017. During that month, the SoS published “*Connecting people: a strategic vision for rail*”. As part of that Strategy, the SoS announced he would introduce a new ‘East Coast Partnership’. This earlier decision to allow Stagecoach and Virgin to simply exit the franchise in 2020 was

¹<http://www.stagecoach.com/media/news-releases/2014/2014-11-27.aspx>

already reported as a 'bailout'. For example, on 29 November 2017, the Guardian reported as follows:

**“East Coast rail 'bailout' could cost taxpayers hundreds of millions
Unions and Labour criticise government as Virgin Trains East Coast's
contract is terminated three years early**

The East Coast rail franchise will be terminated three years early, avoiding the embarrassment of another private firm handing back the keys to the government but potentially forfeiting hundreds of millions in premiums due to the Treasury...

Andy MacDonald, the shadow transport secretary, told the Commons that the strategy announcement was “a total smokescreen”. He said: “The real issue is that the East Coast franchise has failed again and the taxpayer will bail it out.”

Pointing to the share price rise, he said: “Markets don't lie. The secretary of state has let Stagecoach off the hook for hundreds of millions of pounds. He's tough on everyone except the private sector.”

Grayling responded: “As we bring this franchise to a close and as we move to the new arrangements, no one is getting any bailout at all. Stagecoach will meet in full their commitments made to the government as part of this contract.”²

(3) *The failure of the East Coast Franchise and the SoS' response*

7.6. On 5 February 2018, the Secretary of State made a statement in Parliament saying that:

“Since 2015, the franchise has met all its financial commitments to the taxpayer, returning nearly £1 billion to the public purse, but that 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 that the situation is much more urgent. It is now clear that the franchise will be able to

² Bold emphasis in the original; underlined emphasis added; <https://www.theguardian.com/uk-news/2017/nov/29/east-coast-rail-franchise-terminated-three-years-early-virgin-trains>

continue in its current form for only a very small number of months and no more.

Last week, following detailed analysis, my Department issued the franchisee with notification that the franchise has breached a key financial covenant. It is important to make it clear to the House, and indeed to the public, that that will not affect 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 that in the very near future, I need to put in place a successor arrangement for operating the railway and to end the current contract..."³

7.7. In terms of what went wrong, the SoS made clear that:

"...The problem is very straightforward: Stagecoach got its numbers wrong. It overbid and it is now paying the price. Contrary to widespread speculation and rumour, no deal has been done on this railway, and I have not yet made a decision on the successor operator to run the east coast railway until the longer-term plans for the integration of track and train can begin in 2020. There is no question of anyone receiving a bail-out. Stagecoach will be held to all its contractual obligations in full. But, as the Brown review said five years ago, this is what we 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. For anyone who thinks that the nearly £200 million that Stagecoach will lose is insignificant, let me put it into context: the combined profit of every train operator in the country was only £271 million last year, and the loss equates to more than 20% of Stagecoach's total market value. So this is a significant amount of money by any measure, and it should also act as a stark warning to any company tempted to overbid in future. Moreover, the franchising system has now been adjusted to deter further optimism when bidding..."⁴

7.8. In short, the franchise failed because Stagecoach got its numbers wrong. Presumably, its consortium partner, Virgin, bears the same responsibility for this

³ Emphasis added; <https://hansard.parliament.uk/Commons/2018-02-05/debates/228EB6B2-2FD1-40AB-87C0-D6AEDA785DE5/RailUpdate>.

⁴ Emphasis added; <https://hansard.parliament.uk/Commons/2018-02-05/debates/228EB6B2-2FD1-40AB-87C0-D6AEDA785DE5/RailUpdate>.

failure. As a result of overbidding, it is clear that the East Coast franchise breached a “*key financial covenant*”. It is vital to underscore that the franchise did not fail because of external factors and/or other long-term risk management issues that are balanced through the tendering process (see below). The SoS made clear that the operators submitted an unworkable bid – and one that did not work within three years of the franchise starting. This was either: (a) a deliberate move on the behalf of the operators in order to win the tender over other competitors; or (b) a clear example of incompetent, negligent and/or reckless bidding. Whatever the reason for the overbidding, it is a matter of serious concern.

- 7.9. Despite the fact that Stagecoach and Virgin overbid, resulting in an avoidable franchise failure, this is to have **no** future consequences for either operator. The SoS stated:

“There will be those who claim that because Stagecoach overbid, it should be excluded from bidding for future franchises. I have to be clear that the legal advice on this is clear. As the company is meeting its financial obligations to support the franchise, including with the full parent company’s support, and because it has operated services on the east coast line 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. Members will understand that it is my duty to follow legal advice, but let me be clear that we will keep its eligibility for current and future bids under close scrutiny and constant review.”⁵

- 7.10. Extraordinarily, the current competitions / awards of franchises referred to by the SoS include the potential decision to permit Stagecoach and Virgin to operate the East Coast franchise under a short term agreement until 2020 (when the franchise was supposed to end in light of the new reduced franchise period).

- 7.11. In justifying his position, the SoS also stated before Parliament that “*the company is meeting its financial obligations to support the franchise, including with the full parent company’s support*”, and that the franchise “*has operated services on the east coast line successfully*”. The successful operation of a

⁵ Emphasis added; <https://hansard.parliament.uk/Commons/2018-02-05/debates/228EB6B2-2FD1-40AB-87C0-D6AEDA785DE5/RailUpdate>.

franchise does not involve the failure to meet key financial covenants, resulting in its collapse, within approximately 3 years of the franchise having been awarded.

7.12. The SoS denied that there was any record of National Express being banned from bidding for franchises in 2009 following a past franchise failure. Lord Adonis made clear in the House of Lords that his understanding is that such a ban was in place.⁶

(4) Request for answers and the SoS's response

7.13. On 5 March 2018, the Proposed Claimant, together with We Own It, wrote to the SoS seeking answers to the following key questions:

7.13.1. What is the cost to the taxpayer of the East Coast franchise failure?

7.13.2. Why does the SoS deem the franchise failure to be irrelevant to the awarding of any future franchises, including the potential temporary re-award of the franchise to the same operators?

7.14. The SoS did not respond to this letter until 22 March 2018. In that letter, the SoS confirmed that the obligations imposed on Stagecoach in relation to performance / default totalled £200 million. In particular, the Performance Bond is intended to provide protection for the taxpayer against a number of situations, one of which is the SoS incurring additional costs as a result of the early termination of the franchise.

7.15. However, the SoS **did not confirm** whether the costs of terminating the franchise have in fact been met or could be expected to be met by the fulfilment of Stagecoach's obligations in respect of the Performance Bond and/or any other obligation imposed by the Franchise Agreement.

7.16. As noted below, the SoS is asked again to confirm in clear terms whether or not the taxpayer will suffer a loss, even if Stagecoach complies with its obligations. The SoS is also asked to provide a breakdown of how the £200 million is calculated – what is the amount attached to each relevant obligation, and when

⁶ Emphasis added; <https://hansard.parliament.uk/lords/2018-02-05/debates/C9220E9A-47A4-4ECB-960D-BF0A0D9C43BB/RailUpdate>.

was or will that obligation be fulfilled. The SoS is asked to confirm any current or projected cost to the taxpayer of the failure of the franchise.

7.17. It is vital to understand the cost to the taxpayer of the conduct of Stagecoach and Virgin because, as outlined below, the cost to the taxpayer of the overbidding and resulting default which has taken place is a relevant factor in any decision over whether there should be future consequences for that conduct.

7.18. In response to a query about whether National Express was banned from bidding in 2009, the SoS provided a copy of a letter sent to Lord Adonis. That letter confirmed that:

"... I would note that a letter has been identified indicating that, in March 2010, the Department for Transport declined to issue an Invitation to Tender for two franchises to a consortium in which National Express held a significant shareholding, on the basis that National Express did not meet specific criteria set out by the Department at that time, including in relation to the significance, materiality, and wider relevance of its breach of contractual obligations under the Franchise Agreement for the East Coast Main Line.

While the record shows that there was not a general or explicit ban, it is also clear that you followed your obligation under the Railways Act 1993 for any Secretary of State to be satisfied in relation to any specific franchise competition that any bidder meets the requirements to be a "suitable person".

Looking forward, this legal obligation applies equally of course to my own decisions as Secretary of State. On the issue of whether Stagecoach should be excluded from bidding for all future franchises, I have received clear legal advice that there are no adequate legal grounds for doing so. As you would expect, I fully intend to act lawfully in this matter. Equally however, as I have said, we will keep Stagecoach's eligibility for all current and future franchise bids under close scrutiny, and review in accordance with the even more robust processes in place now to ensure that all bidders meet relevant legal requirements."⁷

⁷ Emphasis added.

7.19. In response to the question why Stagecoach, or for that matter Virgin, are to be allowed to continue to bid for rail franchises without any consequences flowing from the East Coast franchise failure, the letter stated that:

“... Under the procedures for assessing the eligibility of potential franchisees which were introduced in 2015, the Secretary of State has the power to withhold, or to revoke, a company’s Passport (entitling it to bid in franchise competitions) on a number of grounds. One of those is that the company has shown significant or persistent deficiencies in the performance of a substantive requirement under a passenger transport contract or operation within the last three years which led to early termination of the contract or other sanctions...”⁸

7.20. Despite the SoS having reached the conclusion that Stagecoach and Virgin overbid such that the franchise failed within approximately 3 years of commencement, the SoS appears to have concluded that the resulting breach of a “*a key financial covenant*” is insufficient to justify any recourse at this time. This is because, according to the SoS:

“In the present case Stagecoach Group plc has to date complied with all its obligations under the East Coast franchise arrangements. Therefore while, as the Secretary of State has already confirmed, he will continue to keep Stagecoach’s eligibility for current and future bids under close scrutiny and constant review, my client’s view is that there are currently no adequate legal grounds to restrict it from bidding on current and future franchise competitions.”⁹

7.21. The highlighted text is wrong. It is inconsistent with the very decision to terminate the agreement. Even if it could be said that Stagecoach and/or Virgin have complied with obligations such as the Performance Bond or the Funding Deed, that does not mean it has complied with “all” of its obligation to date and/or under the agreement. The key overarching obligation to run a franchise until 2020 (or 2023) has been defaulted upon because the operators got their numbers “*wrong*”. This is why the Department issued the franchisee with notification that the franchise has breached a key financial covenant.

⁸ Emphasis added.

⁹ Emphasis added.

7.22. Concerns about the lack of apparent consequences for the operators of the franchise failure are not addressed by the SoS' vague reference to keeping Stagecoach's "*eligibility for all current and future franchise bids under close scrutiny*". As outlined below, both operators have rail franchising Passports designed to allow them to qualify for current and future franchises. No action has been taken in respect of those Passports. Further, the complete omission of any reference in the SoS' announcements / correspondence to Virgin is unexplained and unjustifiable. It was a consortium partner and its past performance is just as relevant to its future ability to run a franchise successfully.

(5) The Brown Review

7.23. The SoS refers to the January 2013 Brown Review in justifying his approach to the failure of the East Coast franchise, stating, *inter alia*, that "*as the Brown review said five years ago, this is what we 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...*"

7.24. The problem with the SoS' argument is that the comments of the Brown Review on franchise failure are not apposite in this case.

7.25. The Brown Review recommended that franchise agreements should usually consist of a 7-10 year initial term with pre-contracted continuation, subject to agreed franchise criteria, for a further term of 3-5 years. He recognised that franchise periods could be shorter. But he also stated that the term should not be less than 5 years.¹⁰ As first agreed, the East Coast franchise agreement was consistent with this guidance. As reduced in November 2017, the franchise was at the very cusp of failing to comply with the guidance provided by the Brown Review.

7.26. The Brown review concluded that franchisees should be responsible for "*risks they can manage and should not be expected to take external macroeconomic, exogenous, revenue risk...*"¹¹ Essentially, the Brown Review found that capital requirements should be imposed on bidders to, *inter alia*, deter default.¹² In particular, the franchising system should operate to ensure that bidders have an

¹⁰ Paragraph 1.134.

¹¹ Paragraph 1.14.

¹² Paragraph 1.15.

incentive to make their projections realistic. i.e. to prevent them overbidding.¹³ As the Brown Review stated at paragraphs 4.45-4.46:

“The combination of shorter initial franchise terms, protection from exogenous revenue risk, and parent company support and bonding proportionate to endogenous revenue risk, will together greatly reduce the scope for bidders to ‘game’ franchise competitions by overbidding and allow the Department to dispense with the need to risk adjust bids for revenue risk.

The removal of the majority of exogenous macro-economic revenue risk should enable bidders to bid lower profit margins and should encourage them to focus more on the cost lines of their bid in order to differentiate themselves. Both of these outcomes would increase value for Government.”

7.27. This is important because the comments made by the Brown Review on risk management have to be understood in their proper context. At paragraph 4.28 the Brown review stated:

“In my view, therefore, for franchising to function effectively and for the market to function competitively, Government should accept that there can be failure. Value for money can still be achieved in such situations and passengers protected. The Department should be judged by how it deals with failure, should it occur, rather than attempting to over-prescribe, over-specify or create expensive and complex risk transfer mechanisms to avoid such a possibility. It is unrealistic to assume that there will never be failure by franchisees, or to try to design a system which removes this risk entirely.”¹⁴

7.28. This conclusion rests on the assumption that the franchise has been managed in accordance with the recommendations made by the Brown Review. Some risk of failure has to be tolerated. Franchise bids involve the management of risk, while driving performance, over a long period. Sometimes things will go wrong over time as projections are proved to be inaccurate and / or external factors change the market landscape. Recognition of this reality does not equate, as the SoS

¹³ Paragraphs 4.25

¹⁴ Emphasis added.

suggests, to a conclusion that it is simply acceptable for franchises to fail, as long as the operators made payments to the Government in accordance with the Franchise Agreement up until the point of default/under the parental guarantee. The breach or breaches giving rise to the default still need to be addressed.

7.29. Here, the East Coast franchise started out as a relatively short-term agreement. It was then cut down. The highest premiums would have been due during the latter part of the agreement. Yet, the franchise failed within in or around 3 years of commencement. This means that the deterrents put in place to prevent overbidding did not work (as a result of deliberate, incompetent, negligent, and / or reckless conduct). The Department, and ultimately the SoS now has to be judged on the basis of how they deal with that failure. What the Brown Review does not say, in any way, is that simply because failure can happen a bidder should be able to walk away from a major franchise failure without current or future consequences for its ability to bid.

(6) *Developments since the announcement of the East Coast franchise failure*

7.30. The Proposed Claimant understands that since the SoS was aware of and/or announced the East Coast franchise failure he has:

- 7.30.1. decided that Stagecoach and /or Virgin may be permitted to run the East Coast franchise again under a further arrangement (otherwise the line will need to be rung by the Government; a decision on how the line will be operated in the light of the franchise failure is yet to be announced. The SoS announcement only refers to Stagecoach, however, we assume that it is the consortium that may be permitted to continue to run the line under a new arrangement, please confirm);
- 7.30.2. decided that Stagecoach may be included on a shortlist of bidders for the East Midlands franchise due to begin in August 2019; and
- 7.30.3. awarded Stagecoach's joint venture with Virgin on the West Coast Mainline a one year extension to March 2020 when a new contract will begin.

7.31. On 26 March 2017, the Transport Committee announced that it will be conducting an inquiry into the failure of the East Coast franchise.¹⁵

8. Legal Framework and the Rail Franchising Passport Process:

8.1. Section 26(3) of the Railways Act 1993 stipulates that the Authority may not issue an ITT to and/or entertain a tender from any person unless it considers that such person has the appropriate financial position, managerial competence, and is otherwise suitable to be the franchisee for the relevant rail franchise.

8.2. The pre-qualification questionnaire (“PQQ”) passport for rail franchising covers all rail franchise competitions held between September 2015 and September 2019. Passport holders can express an interest for any future franchise competition without having to submit the same detailed technical information each time – saving time and reducing costs. As the National Audit Office explained in its report *Reform of the rail franchising programme* of 24 November 2015:

“... a ‘PQQ passport’ which the Department launched in September to reduce the administrative burden and cost of bidding, and to encourage new entrants to the UK market. Rather than having to complete a pre-qualification questionnaire (PQQ) each time they want to bid for a franchise, bidders who have demonstrated managerial competence and a strong track record will be awarded a ‘PQQ passport’. This will allow them to express an interest in a franchise without having to repeat a managerial competency test...”¹⁶

8.3. The Government’s aims and expectations in respect of the franchising framework were published on 10 May 2016.¹⁷ In respect of what the Government says it expects of bidders, the guidance states that: “*As well as fulfilling their contractual and other legal responsibilities, we will be looking for delivery partners to exemplify certain behaviours and values which we believe will contribute to the success of our rail franchising programme...*” which include “*a commitment to the*

¹⁵<https://www.parliament.uk/business/committees/committees-a-z/commons-select/transport-committee/inquiries/parliament-2017/intercity-east-coast-rail-franchise-inquiry-17-19/>

¹⁶ Emphasis added; <https://www.nao.org.uk/wp-content/uploads/2015/11/Reform-of-the-rail-franchising-programme.pdf>

¹⁷<https://www.gov.uk/government/publications/rail-franchising-aims-and-expectations/aims-of-rail-franchising-and-what-we-expect-from-our-delivery-partners>

*sustained success and good reputation of rail franchising and of our railways as a whole.*¹⁸

8.4. The Passport Process Document of September 2015¹⁹ outlines the following key points:

8.4.1. The PQQ process involves the Department assessing whether the Applicant for a passport / tender can deliver the rail franchising services. This includes assessing whether there are grounds for mandatory and discretionary rejection of the application, as well as whether the Applicant's capability, competence and experience justify the granting of the application.²⁰ As a result, the Questions covered by the Passport PQQ include whether there are grounds for the discretionary rejection of the application due to past performance (Part C), and it asks numerous questions about the applicant's capability and technical ability (Part D).²¹ Applications are assessed on a Pass / Fail basis.²² The financial standing of the applicant is considered through the qualifying questions included in the Franchise Expression of Interest.²³

8.4.2. Once a company has a Passport, in response to a Franchise Expression of Interest it only needs to: (a) re-submit Parts B and C of its application; and (b) issue a declaration that Part D is correct.²⁴

8.4.3. The Department may not require Passport Holders to complete further technical ability and capability questions included in the Franchise Expression of Interest.²⁵

8.4.4. Pending the validation of a Passport following a change in circumstances, the Department may exclude the holder from further participation in any

¹⁸ Ibid.

¹⁹ https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/464050/Passport_Process_Document.pdf

²⁰ Paragraph 2.2.

²¹ Paragraph 2.5.

²² Ibid.

²³ Paragraph 2.8.

²⁴ Ibid.

²⁵ Ibid.

rail franchise competition and will consider cancellation of the Passport in accordance with Section 5.4.²⁶

8.4.5. Section 5.4 confirms that: *“If the Authority determines at any time that the Passport Holder no longer continues to meet the Passport requirements (i.e. that a Passport would not be awarded on the basis of the evaluation process outlined in this Passport PPD if a fresh Passport Application was made at the relevant time), the Authority reserves the right to cancel the Passport Holder’s Passport.”* See also Section 5.8.

8.4.6. Section 5.9 confirms that the Department may suspend the validity of a Passport: (a) where the authority is entitled to cancel a Passport, in accordance with this Passport Process Document; and/or (b) where the Authority is exploring concerns about continued compliance with the requirements of the Passport. The suspension may apply for a set period or until certain steps have been taken, for example, steps taken by or on behalf of the Authority to investigate the relevant circumstances. The Department also reserves the right to attach conditions to the continued validity of a Passport or lifting of a suspension.

8.5. The Passport Pre-Qualification Questionnaire was also published in September 2015.²⁷

8.6. Part C includes the following grounds for discretionary rejection of the application for a passport:

8.6.1.C1.3: The Applicant is guilty of grave professional misconduct, which renders its integrity questionable.

8.6.2.C1.7: The Applicant has shown significant or persistent deficiencies in the performance of a substantive requirement under: (i) any passenger transport contract or operation in which the Applicant has been engaged within the last three years and which has an annual revenue of at least £40million; or (ii) any other contract or operation which has been referenced in the Applicant’s response to Part D or Part E in which the Applicant has been engaged within the last three years, which led to early

²⁶ Paragraph 5.2.

²⁷ https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/464051/Passport_Pre-Qualification_Questionnaire.pdf

termination of that prior contract, damages, enforcement action taken pursuant to Section 55 of the Railways Act (or equivalent under the laws and regulations of any State), failure to be awarded a contract renewal or extension that would otherwise have been awarded, or other comparable action or sanctions.

- 8.7. Part C.10 of the Questionnaire provides that if an applicant has to answer yes to the questions outlined above, the applicant has to put forward a justification for being granted a passport, including by explaining whether they have taken concrete technical, organisational and personnel measures that are appropriate to prevent recurrences.
- 8.8. Part D outlines detailed questions seeking evidence showing that the applicant is capable of running a railway franchise, including showing that the staff available are competent (D1.2), and that the applicant is capable of maintaining high levels of service delivery (D4).
- 8.9. Stagecoach Group Plc and Virgin Holdings Limited were 2 of 11 companies granted a PQQ Passport on 15 December 2015 for all future franchise competitions within the lifetime of the Passports. The Minister told Parliament that:

“The quality of the submissions evidenced that we had explicitly sought high standards, integrity and professionalism from the national and international market. During the assessment stages we scrutinised and scored technical ability, strict safety standards and exemplary management practices. Our approach has resulted in a diverse and competitive market bidders from the UK and overseas who now hold the passport.”²⁸

- 8.10. The lifetime of the Passports is four years. Thus, it is understood that the passports currently held by Stagecoach and Virgin will run until December 2019. **Please confirm.**

- 8.11. The Department issued an OJEU notice on 19 July 2017 in respect of the Passport PQQ, which states, inter alia, that

“... For each specific rail franchise competition Passenger Services will, at a later stage, require Passport Holders that express an interest to respond

²⁸ Emphasis added; <https://www.gov.uk/government/speeches/rail-franchising-pre-qualification-questionnaire-pqq-passport-award>

to an additional set of pre-qualification questions that is specifically tailored to that franchise. This will include questions in respect of economic and financial standing. This Franchise EoI may also include further questions in respect of capability and technical ability, although Passenger Services reserves the right not to require Passport Holders to complete these. Passport Holders may be down-selected on the basis of the scoring of the further capability and technical ability questions in order to generate a shortlist of bidders for the competition...

... Each of the franchise agreements to which the competitions covered by the Passport System relate will be a "public services contract" for public passenger transport by rail for the purposes of Regulation (EC) No 1370/2007 on public passenger transport services by rail and by road (Regulation 1370/2007)...

Passenger Services reserves the right not to award any Passports, to make whatever changes it sees fit to the structure and timing of the Passport application process (including issuing any further notice or notices), to the Application Dates or to the structure and timing of a Franchise EoI stage, to cancel the Passport System in its entirety at any stage or to use any additional or alternative method of selecting Bidders for any or all future rail franchise competitions...²⁹

9. The Issue:

9.1. The SoS' position is that the complete failure of the East Coast franchise should not involve consequences for either Stagecoach or Virgin in respect of their participation in current or future franchises. This on-going and forward-looking refusal to take action to revoke, suspend, investigate and/or otherwise limit the ability of these companies to bid for franchise agreements is unlawful and / or irrational in that:

9.1.1. the failure of the franchise through a breach of a key financial covenant / overbidding plainly amounts to a significant deficiency in the performance of a relevant agreement. *Prima facie*, neither Stagecoach nor Virgin are suitable bidders for franchises. As a result, the SoS was entitled to, and should have, revoked the Passports of Stagecoach and Virgin as a consequence. If the franchise failure is to result in losses to the taxpayer, the existing significance of the breach will only be amplified;

9.1.2. the SoS erred in law by directing himself that past compliance with the agreement meant that the wholesale failure of the franchise could not

²⁹ Emphasis added. See also the Passport Process Document.

qualify as a significant deficiency, thereby justifying the termination of, or at least suspension of, the Passports held by Stagecoach and / or Virgin. His position is also contradicted by the claim that he will keep under constant review the eligibility of Stagecoach to bid for franchises. If, for example, the failure could be counted as an example of a 'persistent' deficiency (but for the points made in paragraph 9.1.5 below) for the purposes of revoking a company's Passport, it necessarily follows that the incident could qualify as a 'significant' deficiency. Yet, the SoS' position is that the complete failure of the East Coast franchise does not so qualify because Stagecoach has met other obligations;

9.1.3. there is no evidence or suggestion that the SoS suspended the Passports of either company pending a full investigation of what went wrong, requiring Stagecoach and Virgin to justify the resumption of their Passporting rights. The failure to undertake such an investigation and/or apply such a suspension was irrational given the significance of the failure. It is also a direct result of the misdirection outlined above;

9.1.4. there is no evidence or suggestion that the SoS required Stagecoach and / or Virgin to re-submit the relevant parts of their Passport Application for wider consideration of their past performance in the last 3 years. If, as the Proposed Claimant contends, the franchise failure is a relevant deficiency within the meaning of Part C of the PQQ Application, then it should have been assessed whether in combination with other identified deficiencies, it should result in the revocation or at least suspension of the Passports held by both companies; and / or

9.1.5. whilst the Secretary of State's position is that he will keep under constant review the eligibility of at least Stagecoach to bid for franchises, he has fettered his discretion to rely on the East Coast failure in future decision-making. Once the SoS has claimed publicly, by reference to legal advice, that the complete failure of the franchise is not relevant, it is unclear how he says it could be taken into account in the future.

10. **The details of the action that the defendant is expected to take:**

10.1. For the reasons given above, the SoS is invited to:

10.1.1. revoke the Passports granted to Stagecoach and/or Virgin; and / or

10.1.2. at least, suspend those Passports pending a full and thorough investigation of what went wrong / what caused the East Coast failure, including through requiring the operators to: (i) re-submit their applications for a Passport; and (ii) explain what steps they have taken to prevent any recurrence of the failures that led to the very early failure of the East Coast franchise.

11. **The details of any information sought:**

11.1. Please confirm:

11.1.1. Whether the Passports of Stagecoach and Virgin were suspended while an investigation was completed into what led to the East Coast franchise failure and / or whether any such investigation has taken place.

11.1.2. Whether Stagecoach and Virgin will be required to update their Passport Application to include the East Coast franchise failure (see para 5.2 of the Passport Process Document).

11.1.3. The means by which it is said that the SoS will keep [at least] Stagecoach's eligibility for current and future bids under close scrutiny and constant review. Please also explain the approach being taken to Virgin.

11.1.4. The answers to the queries posed at paragraphs 7.16-7.17, regarding the total costs to the taxpayer of this East Coast failure.

11.1.5. The answers to the queries posed at paragraphs 7.30.18.10 above.

11.1.6. What franchises Stagecoach and Virgin have been awarded and/or been granted the right to tender for, since the SoS was aware that the East Coast franchise would fail.

12. **The details of any documents that are considered relevant and necessary:**

12.1. Please provide copies of any and all relevant documentation that relates to the consideration of whether the Passports of Stagecoach and / or Virgin should be revoked, suspended, and/or limited, including in particular the outcome of any investigation into what led to the franchise failure.

12.2. Please also provide copies of the Passports (excluding any genuinely confidential information) held by Stagecoach and Virgin.

13. **The address for reply and service of court documents:**

As per above letterhead.

14. **Proposed reply date:**

We look forward to hearing from you shortly and certainly no later than by **4pm on 30 April 2018.**

Yours faithfully



Leigh Day