London Underground after the PPP, 2007-

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This note looks at the management of London Underground since 2007, covering the collapse of the Public Private Partnership (PPP) and the transfer of control of the Underground to Transport for London (TfL).

By the late 1990s there was general agreement that it should be a priority to secure investment in London Underground in order to improve services and bring the network up to modern standards. This could only be achieved with a stable funding regime to allow investment to be planned ahead.

While the previous Conservative Government announced its intention to privatise the Underground, the Labour Government that took office in 1997 opted instead for a PPP. In taking this decision it faced opposition from a number of quarters, including unions and safety campaigners and the first Mayor of London, Ken Livingstone. Mr Livingstone and his Transport Commissioner, Bob Kiley, took the government to court over the decision and championed an alternative method of raising money, via the issue of bonds secured against future fare revenues from London. This was rejected by the Treasury.

Mayor Livingstone was ultimately unsuccessful in his challenge and the PPP went ahead in 2003. The primary legislation for the PPP is contained in Part IV, Chapter VII of the *Greater London Authority Act 1999*, sections 210-239 and Schedules 14 and 15.

These matters are dealt with separately in HC Library note SN1307, available on the Railways Topical Page of the Parliament website.

Plagued by problems, the PPP collapsed in 2010 when Transport for London bought out the private companies in the Tube Lines consortia; this followed the administration of Metronet in 2007.

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1 Background: the PPP, 1997-2003

1.1 Letting the PPP

The then Deputy Prime Minister, John Prescott, announced the Labour Government's plans for the future of London Underground on 20 March 1998.[1] The proposal had three main elements: operation in the public sector, infrastructure investment in a PPP, and immediate extra investment. He explained that London Underground would remain as a unified public sector operating company that would: own the freehold of the system; be responsible for safety; and employ train drivers, station staff and line and network controllers.

It would let between one, two and three infrastructure contracts to the private sector to maintain and modernise the Underground's infrastructure. The infrastructure contractors would be under an obligation to eliminate the investment backlog and there would be a performance regime with incentives and stiff penalties; the aim being to return the assets to the public sector at the end of the contract in a much-improved condition. The PPP was expected to deliver £7 billion of investment over fifteen years. The target date for awarding new contracts was April 2000.

On 15 March 1999 LUL, in consultation with the Government, published a progress report on the PPP.[2] The progress report confirmed the basic structure of the PPP: the infrastructure would be leased to the private sector (Infracos) under 25 to 30 year concessions but operations would remain with a publicly-owned body (Opsco), formed by the restructuring of London Underground. The line groups offered to the private sector were as follows:

Sub Surface Lines (SSL)	Infraco BCV	Infraco JNP

1 HHC Deb 20 March 1998, cc1139-1556

2 London Transport, *PPP for London Underground: progress report*, 15 March 1999 [HC deposited paper DEP 99/579]

Circle	Bakerloo	Jubilee
District	Central	Northern
East London	Victoria	Piccadilly
Hammersmith and City	Waterloo and City	
Metropolitan		

The BCV and JNP infracos were for 'deep tube' lines, so-called because the tunnels on these lines are smaller, running through tunnels bored deeper under the centre of London. The sub-surface lines are only just below ground level, having been built in 'cut and cover' tunnels.

On 7 October 1999 London Underground published the shortlist of bidders for the two deep tube PPP contracts. LINC, Metronet, TubeRail and NewMetro would be invited to tender for Infraco BCV. LINC, Metronet, TubeRail and TubeLines Group would be invited to tender for Infraco JNP.[3] At the time of their bids, the consortia were composed of the following companies:

- **LINC**: Bombardier, Prorail, John Mowlem, Fluor Daniel, Alcatel Telecom, Anglian Water
- **NewMetro**: Siemens, Taylor Woodrow Construction, Innisfree, Gibb, Mott Macdonald
- **Metronet**: Adtranz, WS Atkins, Balfour Beatty, Seeboard, Thames Water
- **TubeLines Group**: Bechtel/Halcrow, Amey, Hyder Investments, Jarvis
- **TubeRail**: Brown & Root, Alstom Transportation, Projects, Almex, Carillion

On 2 May 2001 Tube Lines was announced as the preferred bidder for Infraco JNP (the Jubilee, Northern and Piccadilly Lines) and Metronet the preferred bidder for Infraco BCV (the Bakerloo, Circle and District Lines).[4] Finally, on 19 September Metronet was announced as the preferred bidder for the Underground sub-surface lines.[5]

The Government estimated that, under the PPP, Metronet and Tube Lines would realise over £16 billion of investment in the Underground over the following 15 years and the PPP would save an estimated £4 billion over the same period.[6]

The final bids were submitted to LUL on 4 January 2002; the procedure for agreeing them was as follows:

- LUL and its advisors, PricewaterhouseCoopers (PwC), made recommendations to the Board of London Transport once a final analysis of the value for money of the bids had been completed;

[3] London Underground press notice, 7 October 1999

[4] London Underground press notice, "Key milestone in Tube fit for the future: Preferred bidders named in Public Private Partnership" 2 May 2001

[5] London Transport press notice, "Preferred bidder for Underground Sub-Surface Lines contract named today", 19 September 2001

[6] HHC Deb 7 February 2002, cc1128-1130

- the Board of London Transport then took a decision on each of the three contracts at a Board meeting on 7 February 2002;
- this was followed by a three-week consultation period with the Mayor and Transport for London (TfL) during which time the Government took independent advice on the value for money of the bids from its advisor, Ernst and Young;
- following the consultation the Board of London Transport made a final decision on the contracts, which was then sent to the Secretary of State for approval; and
- the Health and Safety Executive concluded that the PPP was safe (the safety test) and the Secretary of State made his final decision based on the submission of London Transport and the advice of Ernst and Young (the value for money test).

In late 2002 it was reported that Metronet, the preferred bidder for the SSL and BCV infracos, was unable to raise sufficient financing until January 2003 and that the PPP would therefore take place in two stages. It was also reported that Tube Lines had been requesting a staggered closure of the PPP deal.[7] On 31 December 2002 Tube Lines announced that it had reached final close on the contract to upgrade the Jubilee, Northern and Piccadilly lines and responsibility for the JNP infraco was transferred.[8] The final stage of the PPP was completed on 4 April 2003 when Metronet signed the 30-year contract with LUL for the upgrade of the Bakerloo, Central, Victoria and Waterloo & City lines (BCV) and the Sub Surface Lines (SSL).[9]

1.2 The City Hall angle

The PPP was taken forward as part of wider reform of the governance of London.[10] The *Greater London Authority Act 1999* provided for the Greater London Authority (GLA), the elected Mayor of London and the London Assembly. Part IV of the Act concerns transport and road traffic in and around Greater London. The Mayor has a duty to produce an integrated transport strategy for London and can fund new services, make investments and introduce new ticket systems. Transport for London (TfL) is his executive arm and directly accountable to him. It implements the Mayor's transport strategy and oversees transport services on a day-to-day basis.

The former Labour Member of Parliament Ken Livingstone, running as an independent, was elected as the first Mayor of London on 4 May 2000 and TfL was officially established on 3 July 2000. On 9 October 2000 TfL announced the appointment of Bob Kiley, the former Chief Executive and Chairman of New York's Metropolitan Transport Authority, as the first Commissioner of Transport for London. Mayor Livingstone opposed the PPP plan for London Underground on the grounds that it would fragment the unified management and operational structure of the Underground. He campaigned for the infrastructure modernisation to be funded by the issue of bonds.

On July 30 2001 Mr Justice Sullivan dismissed the application by TfL for judicial review of the decision by London Underground (LUL) and London Regional Transport (LRT) to enter into a PPP for renewal of the Underground. TfL had submitted that the PPP contracts, under which

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7 "Tube set to be finalised in two stages", *The Times,* 12 November 2002

8 Tube Lines press notice, "New future for tube starts here: Tube Lines reach financial close on PPP contract", 31 December 2002

9 London Underground press notice, "Tube PPP investment plans finalised", 4 April 2003

10 further information on the governance changes in London and how it affected London transport is available in HC Library Research Paper HRP 08/36

it would be bound for 30 years, would make it impossible to implement the transport strategy formulated by the Mayor under the *Greater London Authority Act 1999*. The Judge found that the Government, through LUL and LRT, was entitled to enter into 30-year PPP agreements even if this conflicted with the Mayor's transport strategy.[11]

The Secretary of State said that the LRT would consult the Mayor of London and TfL under the terms of the *Greater London Authority Act 1999*, and the final decision on whether to proceed with the PPP would be taken in the light of that consultation.[12] On 21 March TfL issued its interim consultation response to LUL in which Mr Kiley claimed that the documentation had been incomplete and the co-operation from LUL and its advisers sparse. The response also labelled the contracts "by far the most complex contractual arrangements ever attempted to be applied to an urban mass transport system" and that they were "difficult to decipher even for experienced transport lawyers and financial experts". TfL concluded that "the final PPP is nothing less than a scandal".[13]

On 23 July 2002 Mayor Livingstone and TfL applied for a Judicial Review on the Government's proposed PPP on the following grounds:

- that the procurement was unlawful because it breached public procurement rules;
- because the contracts had not been properly procured the best deal had not been obtained from the private sector and the contracts therefore could not satisfy the Government's own value for money test; and
- based on the then current funding promises from Government, London simply could not afford PPP.

In a statement to the court on 26 July, however, Lord Lester stated that the Mayor and TfL had been advised that they had no standing to complain to the High Court and were withdrawing their application for judicial review.[14]

2 How did the PPPs perform?

TfL published annual performance reviews of the PPP from 2003-04 to 2009-10, when TfL took over Tube Lines and the PPP effectively ceased. The report for 2007-08 stated that, over the first five years of the PPP, the performance of the Underground had improved. For example, since the start of the PPP, total Lost Customer Hours (LCH) – i.e. the aggregate cost of delays due to asset failures in terms of customers' time – had reduced by approximately 20 per cent; the volume of train services had increased by nearly 2.8 million km, and in 2007/08 almost 125 million more journeys were made on the tube than in 2003/04.[15] The 2008/09 report was published after Metronet went into administration. It offered the following comparisons between the base year 2003/04 and 2008/09:

11 "Government Underground power precedes Mayor's", *Times Law Report,* 2 August 2001
12 "Transport secretary ignored Tube sale warning", *Financial Times,* 7 March 2002
13 TfL, *Interim Consultation Response to London Transport*, 21 March 2002, p2 and p112
14 see, for example, "Livingstone's £4m Tube humiliation", *The Scotsman*, 27 July 2002 and "Taxpayers face £4m bill as Tube case is dropped", *The Times*, 27 June 2002; the decision to take the matter to review was criticised by opposition politicians and also by the QC for Tube Lines
15 TfL, H*London Underground PPP report 2007/08*H, section 3.1

Tube Lines (JNP Contract)

Overall Availability on the JNP lines in 2008/09 was 32% better than benchmark and 20% better than bid. Performance improved by 21% on the previous year, restoring the overall positive trend following the slight decline in 2007/08. A direct comparison of 2008/09 with 2003/04 (the first year of the PPP) also shows a 49% improvement in Availability since Transfer.

Table 1. **Percentage Variance Lost Customer Hours (LCH) against Benchmark**

	03/04 PPP Start	08/09
JUBILEE	-33%	-9%
NORTHERN	-79%	31%
PICCADILLY	8%	54%

[...] **LU Nominee BCV Ltd (BCV Contract)**

In 2008/09, the last eleven months of which the BCV was under LU stewardship, overall Availability was 27% better than benchmark, with a 30% reduction in the total number of Lost Customer Hours (LCH) compared to 2007/08, reversing three years of continual decline under Metronet. Further evidence of the turnaround in BCV performance since the administration is the 21% decline in the average number of LCH per period.

Table 2: **Percentage Variance Lost Customer Hours (LCH) against Benchmark**

	03/04 PPP Start	06/07 Pre-MR Admin	08/09 Post MR-Admin
BAKERLOO	15%	10%	34%
CENTRAL	-16%	13%	33%
VICTORIA	-16%	-27%	23%
WATERLOO & CITY	-58%	-29%	-219%*

**Low Availability score is due to the decision to increase Capability by utilising the whole fleet (see next page).*

[…] **LU Nominee SSL Ltd (SSL Contract)**

Overall Availability in 2008/09 on the SSL was 35% better than benchmark and 36% better than in 2003/04. Under LU's stewardship the SSL has continued the positive trend that started in 2006/07 with a 16% reduction in LCH since 2007/08. The average number of Lost Customer Hours per period was also 18% fewer post-administration.[16]

Table 3: **Percentage Variance Lost Customer Hours (LCH) against Benchmark**

	03/04 PPP Start	06/07 Pre-MR Admin	08/09 Post MR-Admin
DISTRICT	44%	-19%	14%
MCH*	21%	37%	48%

**The MCH grouping includes the Metropolitan, Circle and Hammersmith & City lines.*

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16 TfL, H*PPP and performance report 2008-2009*H, sections 3.1-3.3

The 2009-10 report states that "despite its failure to deliver the biggest projects, the PPP has nevertheless delivered the renewal and upgrade of many other assets — including track, stations, lifts and escalators", as demonstrated in the graphic below:[17]

Renewing assets under the PPP — progress check

		2009/10	Cumulative total since 2003
Kilometres of track replaced	BCV	4	58.5
	JNP	1.2	56.4
	SSL	21.3	82.4
	Total	**26.6**	**197.2**
Escalator refurbishments and replacements	BCV	13	55
	JNP	11	83
	SSL	1	23
	Total	**25**	**161**
Lift refurbishments and replacements	BCV	0	10*
	JNP	2	6
	SSL	0	6
	Total	**2**	**22**
Stations refurbished or modernised	BCV	2	31
	JNP	20	85
	SSL	1	30
	Total	**23**	**146**

*includes two Mobility Impaired Person (MIP) lifts

In his close-out report published in November 2010, the PPP Arbiter, Chris Bolt summarised the lessons to be learned from the PPP. He said that although the first review period (i.e. the first 7.5 years) "saw funding at a level beyond that routinely experienced for decades", major upgrades were not due to be completed until the end of the second review period (i.e. 2017/18). Financially, he thought that, while "it was underpinned by comfort letters and a ten year financial settlement for central government grant to TfL, the long term stability of funding always appeared to be in question". It now falls to London Underground to complete the bulk of the upgrade programme "in a period of extreme funding uncertainty which is already

17 TfL, H*PPP and performance report 2009-2010*H, pp19-20

affecting delivery".[18] However, he did think that the PPP did offer something of a success story, in terms of day-to-day performance:

> A major success of the contract has however been the day to day performance regime. Although initially criticised for its complexity, it has in fact operated effectively throughout the last seven years. On the key routine measure of Availability performance has improved with delays reducing by around half since Transfer.
>
> Tube Lines in particular has also had some significant success in reducing costs. Its progress towards the benchmark range is marked and consistent, and in contrast to the performance of BCV and SSL. For both of these Infracos there has been a steady but significant decline in cost performance since they were taken back under public ownership.[19]

The Arbiter criticised the lack of long term planning and incentives and the relationship between the infracos and TfL. He stated that deficiencies in these areas would mean that TfL would now have to bear the 'cost consequences' of the infracos failing to adopt new ways of working, including increased mechanisation.[20]

3 The collapse of Metronet, 2007-08

3.1 Background

Sections 220-224 and Schedules 14 and 15 of the 1999 Act set out the rules for PPP administration. The Explanatory Notes to the Act explain:

> *Sections 220 to 224* and *Schedules 14 and 15* provide for a special PPP administration order regime. Such an order may be made by the High Court in relation to a PPP company which is on the point of insolvency or winding-up. It may direct a person appointed by the court to take over the running of the PPP company with a view to achieving the purposes of the PPP administration order in a manner which also protects the respective interests of the members and creditors of the PPP company. The purpose of the PPP administration order regime is to ensure that the duty of the administrator principally to protect the interests of members and creditors of a company is balanced against ensuring that activities under the PPP agreement are carried on, thus securing continuity of services for passengers.

In 2004 the Transport Committee looked at the performance to date of the PPP and made the following observation on the possibility of administration:

> A particular problem would arise if one of the consortia's member companies went into administration. We were told that a buyer would be sought and "it is not possible suddenly to find buyers for … equity that are unacceptable to London Underground" and that if an entire company was taken over, there would be a new owner for the shareholding in the consortium. But when we discussed the possible transfer of Jarvis's stake in Tube Lines with Mr O'Toole he was certainly concerned to ensure "that the entire structure is not made more fragile as a result in the change of ownership". London Underground might well have less scope to ensure stability if the company being sold was in administration at the time. If a consortium as a whole went bust London Underground would gain its assets, but would also assume responsibility for a high proportion of its debt. The impact of either situation on London Underground and on the taxpaying passenger would be potentially extremely serious. **The PPP was**

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18 PPP Arbiter, H*OPPPA close out report*H, November 2010, paras 3.21-3.23
19 ibid., paras 3.25-3.26
20 Ibid., paras 3.27-3.30

drawn up in the expectation that shareholders in the infracos might change during the 30 year life of the partnership. When it was in difficulties, Jarvis was able to use its share in Tube Lines as a source of funds. On this occasion, London Underground Ltd was able to ensure that the change was acceptable, but we agree with them that the PPP contract is susceptible to the changes in the commitment of the members of the consortia to the London Underground. Future transfers might not have such a satisfactory outcome. Members of the consortia can sell their share in the Underground relatively freely; the taxpayer is committed to continued funding of the PPP whatever changes in ownership occur.[21]

Metronet operated the BCV and SSL infracos and its performance came in for heavy criticism. In January 2007, for example, the London Assembly Transport Committee concluded that:

> The PPP was designed to bring market discipline to a major public infrastructure project. The management of the preferred supplier contracting arrangements employed by Metronet has failed to impose this discipline. A clear line of responsibility and accountability needs to be established between the work being done on the ground and those charged with overseeing this work.[22]

In May 2007 Metronet admitted that it was expecting to overspend by more than £1 billion – higher than the £750 million anticipated by the PPP Arbiter in November 2006.[23] Metronet argued that the overspend was partly due to London Underground's "wasteful job specification":

> Metronet, the embattled company behind a pounds 17bn upgrade of London Underground, was asked by Tube officials to paint Lancaster Gate station three times in different shades of grey until they were happy with the colour. Andrew Lezala, Metronet's chief executive, said this was just one example of London Underground's wasteful approach to job specification on the project, which has left the contractor with projected cost overruns now thought to top pounds 1bn … Mr Lezala said: "There are lots of examples of waste, where we are spending twice as much as we planned on things that take twice as much time." (…)
>
> Mr Lezala said London Underground managers had a "misconception that this was a fixed price contract", adding: "They have a genuine interest to get as good a job done as they can. They see it as an opportunity to get this railway into a world-class position. The trouble is they want someone else to pay for it." Asked why Metronet continued to do work it was not being paid for, he said that under the public-private partnership contract, "we are required to do what London Underground wants. If we didn't we could be in default".[24]

TfL responded that Metronet was several years late on the basic refurbishment of 28 stations and that while Metronet would say the cost overruns were down to TfL's over-specification, "we would say it's their inability to manage the contracts".[25]

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21 Transport Committee, H*The performance of London Underground*H (sixth report of session 2004-05), HC 94, 18 March 2005, para 32 [emphasis in original]

22 London Assembly Transport Committee, H*A tale of two infracos*H, January 2007, p4

23 "Tube contractor pins hopes on review as overshoot hits £1bn", *The Guardian*, 23 May 2007

24 "HTube row shrouded in shades of greyH", *The Daily Telegraph*, 24 May 2007

25 ibid.

3.2 Administration and the financial fall-out

In early June 2007 it was reported that Metronet had been refused access to its loan facilities by the banks.[26] On 28 June Metronet made a reference to the PPP Arbiter, triggering an Extraordinary Review of the BCV PPP. As part of that reference, it sought a direction on the interim level of Infrastructure Service Charge (ISC) to be paid by London Underground while the Extraordinary Review was being completed. It asked for this direction to be given within a period of four weeks from the date of the reference. Metronet initially sought an increase in ISC of £400.2 million over the twelve month period from the date of the reference. On 12 July, it made a supplemental submission which increased this figure to £551.1 million. On 16 July the PPP Arbiter, Chris Bolt, provisionally concluded that the interim level of ISC in the twelve months from 29 June 2007 to 28 June 2008 should be an increase of £121 million (at nominal prices).[27]

It was widely predicted that if Metronet could not secure the full amount of funding it requested that it would be forced into PPP Administration.[28] On 18 July this is exactly what happened. The statement on the company's website read:

> Metronet Rail BCV Limited ("BCV") and Metronet Rail SSL Limited ("SSL"), the companies responsible for the maintenance and renewal of the Bakerloo, Central, Victoria, and Waterloo & City lines (BCV) and Circle, District, Metropolitan, Hammersmith & City and East London lines (SSL), today entered PPP Administration.
>
> Under the PPP contracts and the Greater London Authority Act 1999, Alan Bloom, Maggie Mills, Roy Bailey and Stephen Harris, partners and directors of Ernst & Young LLP, have been appointed PPP Administrators. The purpose of the Administration is to ensure the continuation of both BCV and SSL's maintenance and renewal activities pending the transfer of the companies' activities to a new operating company with the intention that there should be no noticeable impact on the Tube network or passenger services.
>
> The Directors of BCV and SSL will continue in office and will work with the PPP Administrators. The PPP Administrators have obtained an order from the Court ensuring that all day to day responsibilities within Metronet rest with the existing management team.
>
> Metronet directors and staff are working closely with the PPP Administrator and their staff and with London Underground to ensure that the infrastructure it is responsible for is safely maintained, and to ensure the continued safe and reliable operation of London Underground services.
>
> Staff should continue to undertake all their responsibilities and will be paid in the normal course of business.
>
> Direct third party creditors will be paid their arrears of approved invoices for work done or goods delivered that are outstanding as at the date of appointment, in the normal payment terms. The PPP Administrators will be having separate conversations with the shareholder companies and their subsidiaries / affiliates in relation to their arrangements.

[26] lead by the European Investment Bank, see: "HMetronet in cash pleaH", *The Sunday Times*, 3 June 2007
[27] PPP Arbiter, H*Reference for Directions from Metronet Rail NCV Ltd: draft directions*H, 16 July 2007
[28] e.g. "Metronet braced for ruling on £2 billion overspend", *Financial Times*, 16 July 2007

> Going forward, suppliers will be paid for approved invoices at their usual rates and on existing terms and conditions agreed with Metronet for work carried out (or goods delivered) during the PPP Administration.
>
> Passengers should be assured that all essential maintenance and safety work will continue to be undertaken.[29]

On 30 July the Arbiter announced that he had deferred indefinitely his final directions on Metronet BCV's request for an interim increase in stage payments of ISC.[30] On 10 September it was announced that the Administrators of Metronet had indicated to the Arbiter that they wished to engage with him to clarify issues raised by Metronet's initial submission regarding the extraordinary review; with that in mind the Arbiter announced that he would begin work on a timetable to proceed with the Review.[31] On 21 September the Arbiter published his initial thoughts on the Metronet Extraordinary review:

> Metronet BCV claimed for additional ISC to cover recoverable cost increases (and loss of performance revenue) of £992 million over the first 7½ years of the contract. The Arbiter's current view is that the appropriate figure for an efficient company would be in the range £140 - £470 million. This compares with a figure of £121 million for the period to June 2008 reflected in the draft direction on Interim ISC published on 16 July (…)
>
> He has also reviewed the financial model for Metronet SSL, which shows an underlying increase in costs of some £1.1 billion. He considers that if similar factors apply the potential scale of the increase in efficient and economic costs recoverable by Metronet SSL is likely to be in the range £230-£600 million.[32]

Press reports indicated that TfL was unhappy with the decision which could mean that they owe Metronet anything between £370 million and £1.07 billion.[33]

On 6 February 2008 the Secretary of State for Transport, Ruth Kelly, made a written statement to the House announcing that the Government would pay TfL £1.7 billion to cover the 95 per cent public sector guarantee to the company's creditors and a further £300 million to cover its administration costs.[34] *The Times* gave the views of opposition politicians to the decision:

> Theresa Villiers, the Shadow Transport Secretary, said: "The taxpayer is picking up a £2 billion tab for Gordon Brown's incompetence when he set up the Metronet PPP. But the total cost of this shambles is still unclear."
>
> Norman Baker, the Liberal Democrat transport spokesman, said: "Just like Northern Rock, the private sector takes the profit when they can, and the public sector bails them out when matters go pear-shaped. This is an appalling waste of public money".[35]

In a letter to the paper published a few days later the Secretary of State rebutted:

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29 Metronet press notice, "HMetronet BCV & SSL of into PPP administrationH", 18 July 2007

30 PPP Arbiter press notice, "HArbiter sets out next steps on Metronet Extraordinary ReviewH", 30 July 2007

31 PPP Arbiter press notice, "HArbiter confirms resumption of Metronet BCV Extraordinary ReviewH", 10 September 2007

32 PPP Arbiter press notice, "HArbiter publishes initial thoughts on Metronet Extraordinary ReviewH", 21 September 2007

33 "Arbiter sides with Metronet", *Financial Times*, 23 September 2007

34 HHC Deb 6 February 2008, cc74-76W

35 "H£2bn of public money goes down the Tube as Brown counts cost of failed dealH", *The Times*, 7 February 2008

> This is not a bail-out. This money would have been paid back to the lenders over the course of the PPP contracts had Metronet stayed in business. It will also have limited net impact on public finances as Metronet's borrowing was already part of the Government's balance sheet and now we have made provision for this to appear on TfL accounts rather than directly on the Exchequer's.[36]

3.3 Finding a buyer for the contracts

Among other things the PPP Administrators were responsible for finding buyers for both of Metronet's PPP contracts; the Prime Minister confirmed that another company would be found to take Metronet's place.[37] It was intially not clear whether section 210(5) of the 1999 Act effectively forbids the public sector from operating an infraco:

> (5) If a party who undertakes to carry out or secure the carrying out of any or all of the work mentioned in subsection (3) above (a "PPP company") is a public sector operator at the time when the contract is made, that party must no longer be a public sector operator on the day following the expiration of the period of six weeks beginning with the day on which the condition in subsection (6) below is satisfied.

It was reported in *The Guardian* on 27 July 2007 that TfL was in talks with the Government to transfer Metronet's responsibilities to a company managed by TfL – this would be similar to what happened when Railtrack went into administration and Network Rail took over its assets and responsibilities.[38] It was also reported that TfL would seek to rewrite the BCV and SSL contracts, whoever took over.[39]

In August 2007 TfL announced that it had lodged a formal Expression of Interest with the Arbiter to take over the two Metronet companies on a temporary basis.[40] Before a session of the London Assembly Transport Committee in September 2007 the Administrator, Alan Bloom, stated that he had approached several possible private buyers to gauge their interest in the Metronet contracts but that a sale to the private sector would depend on whether the value of the remaining contracts was greater than the company's main £1.6 billion secured debt.[41] At the same hearing Tim O'Toole, Managing Director of London Underground (LU), indicated that if TfL took over the contracts that they would be broken up and that, for example, station upgrades would be put out to one company and track upgrades to another.[42]

In October 2007 it reported that TfL was facing pressure from the Government to increase private sector involvement in its bid for the Metronet contracts.[43] A few days later TfL lodged a formal bid to take over the Metronet contracts.[44] When the Secretary of State appeared before the Transport Select Committee in November 2007 TfL was the only official bidder for the contracts but the Secretary of State did not rule out setting up another PPP, involving the private sector, to operate the contracts.[45] It was later reported that TfL had withdrawn the

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36 "Don't blame the PPP", *The Times*, 9 February 2008

37 "HTaxpayers face bill of hundreds of millions for Metronet debacleH", *The Independent*, 19 July 2007

38 "HLondon Mayor's transport team in talks to take charge of failed tube contractorH", *The Guardian*, 27 July 2007

39 "Tube chief wants to rewrite contracts", *Financial Times*, 17 July 2007

40 TfL press notice, "HTransport for London seeks Metronet exit from Administration as soon as possibleH", 24 August 2007

41 "Private buyers sought for failed Metronet", *Financial Times*, 12 September 2007

42 "HUnderground mulls Metronet break upH", *The Independent*, 12 September 2007

43 "TfL faces pressure on bid to take over Metronet", *Financial Times*, 22 October 2007

44 "TfL set to take over Tube contract", *Financial Times*, 26 October 2007

45 "Tube deal primed for private sector", *Financial Times*, 8 November 2007

'letter of comfort' to underwrite 95 per cent of Metronet's borrowings; this would discourage any potential private sector investors such as Bechtel, Ferrovial, Carillion, Serco or Tube Lines.[46]

In December TfL acknowledged that it would miss its own deadline of 18 January 2008 to take over Metronet, claiming that the delay was due to issues out of its control such as obtaining approval from the European Commission under the state aid rules.[47] In January 2008 there were reports of further delays due to a dispute between TfL and Bombardier Transportation about aspects of its contracts with Metronet including train maintenance and contracts for new signals.[48] All that aside, a Memorandum of Understanding between the Department for Transport and TfL was published in January on the assumption that London Underground would be successful in its bid for the Metronet contracts.[49]

The Shadow Transport Secretary, Theresa Villiers, stated in August 2007 that the Opposition had no objections to TfL taking control of the Metronet contracts as long as the bidding process was fair and services would be improved. She said: "I don't believe that taking this contract back in-house will necessarily solve the problems of the [PPP] but, having said that, we should look objectively at the quality of the TfL bid in terms of value for money and quality of services".[50] In an August 2007 letter to Ms Villiers the head of the National Audit Office indicated an interest in conducting an inquiry into the PPP;[51] the NAO announced its inquiry in February 2008 and published its report in June 2009.[52]

The Liberal Democrat candidate for Mayor of London in 2008, Brian Paddick, stated that a concession model might be the best way forward for the Underground, much like the Docklands Light Railway operates. He did not, however, support TfL taking over Metronet's contracts: "the inevitable conclusion I have come to is that London Underground and TfL are part of the problem, not part of the solution. The thought of LU taking over where Metronet failed is a recipe for even more disaster".[53]

3.4 TfL assumes control of Metronet

On 2 April 2008 one of the major obstacles to Metronet leaving administration was overcome when a deal was reached over the Bombardier-Invensys resignaling contract:

> The dispute between Metronet and Bombardier Transportation, the world's largest trainmaker, has been the largest issue preventing Transport for London, the London Mayor's transport organisation, from completing a takeover of Metronet.
>
> Under the deal, Bombardier will pay the Westinghouse Rail Systems subsidiary of Invensys, the engineering group, Pounds 95m to withdraw from a project subcontracted from Bombardier to resignal all of the underground's shallow, sub-surface lines - the Metropolitan, District, Circle and Hammersmith &City. Westinghouse

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46 "HTfL removes letter of comfort to shut out interest in MetronetH", *The Times*, 9 November 2007
47 "HTfL will miss own Metronet takeover deadlineH", *Financial Times*, 18 December 2007
48 "Dispute delays Metronet takeover", *Financial Times*, 10 January 2008
49 *Memorandum of Understanding between Department for Transport and Transport for London*, 4 February 2008 (DEP 2008-0360), copies available from the House of Commons Library
50 quoted in: "HTories give cautious backing to TfL Tube contractsH", *Financial Times*, 27 August 2007
51 "Watchdog has Tube partnership in sights", *Financial Times*, 30 August 2007
52 NAO, H*The Department for Transport: The failure of Metronet*H (session 2008-09), HC 512, 5 June 2009
53 Brian Paddick press notice, "Londoners are paying the price for Metronet failure", 25 January 2008

will continue with a similar contract to resignal the deep-level Victoria Line, which is under way.[54]

Consequently, on 23 May 2008 TfL announced that Metronet would leave administration and transfer to TfL on 27 May 2008:

> Metronet's exit from Administration and transfer to TfL neared completion today, as the High Court set the date for the transfer of the people, assets and contracts of the Metronet business to two TfL-owned nominee companies.
>
> This will take place at 00:01 on 27 May 2008.
>
> All Metronet Rail staff will be transferring to the nominee companies under their existing terms and conditions and in accordance with TUPE regulations.[55]

On 7 December 2008 all Metronet Rail employees TUPE transferrred to London Underground. To enable the newly single organisation to function effectively, the top level of London Underground and Metronet Rail were integrated by creating a new London Underground Executive. An agreement was created to enable London Underground to provide staff resource to Metronet Rail to enable Metronet Rail to continue to discharge its obligations under the PPP contracts and related contracts.

The sixth annual review of the PPP, published in December 2009, had the following to say about the 'legacy of Metronet':

> The legacy left by Metronet's former shareholders was one of poor programme management and system integration, ineffective cost control, a lack of forward planning and inefficient fiscal management. During the period of Administration, LU worked initially with the Administrators, and then with former Metronet staff, to develop and drive an improved programme within the budgetary confines of TfL affordability. Significant levels of efficiency have been identified and incorporated into the BCV & SSL plans and these are explained below.
>
> A number of key improvements to London Underground's (LU) own processes have been developed through the integration with Metronet. These have been included in the Tube Lines Restated Terms, with the intention of providing the opportunity to Tube Lines to benefit from efficiencies in areas such as the more innovative use of access and streamlining of the assurance regime.
>
> Initial estimates from the National Audit Office's report into the collapse of Metronet put the loss to the taxpayer of Metronet's failure between £170m and £410m. This result however does not take into account work left undone by Metronet and which still needs to be completed by LU in the future and so does not give a full picture of the financial legacy of Metronet.
>
> As a direct result of significant failures in Metronet's planning and delivery of the programmes of work required under the PPP contracts for both BCV and SS L, a significant, £2.5bn funding gap was identified. In working with the Administrators prior to the Transfer to TfL in May 2008, and through rigorous review during the past year, the £2.5bn of cost escalation was contained through the following actions:
>
> - A detailed programme review and cost saving exercise was undertaken across the entire asset portfolio. The removal of the need for contractual ceremony,

54 "Metronet resolves contract dispute", *Financial Times*, 2 April 2008
55 TfL press notice, "HCourt sets date for Metronet's transfer to TfLH", 23 May 2008

right sizing of programmes and teams, and elimination of duplication between LU and Metronet that was inherent in the PPP structure, enabled a number of programme costs to be saved.

- Significant cost savings were unlocked through attaining full integration of back office and support functions activities across LU and Metronet. Along with this, significant savings have been made through procurement and maintenance efficiencies, namely the re-procurement of maintenance outsourcing which allows for more aligned and consolidated packages of work to be carried out (e.g. in areas such as track and stations cleaning).

- During Administration it became evident that Metronet's station programme was in such a poor state, that it would not be capable of delivering the enhancement to every station as required by the PPP contract ... As a result a revised stations programme was established.

- This has resulted in the following cost reductions:

- The review and revision of supply chain contracts with the previous shareholders prior to exit from Administration, led to an estimated saving of £0.5bn;

- More robust estimates developed for each of the programmes led to both the discovery of programmes that had not been fully developed and for which additional costs were required, and also opportunities to reduce the cost of the programmes through cost containment exercises. The net result was a decrease of £0.2bn;

- Efficiencies in back office and programme support, procurement and maintenance productivities will enable a reduction of £1bn;

- The development of a more robust plan for delivering stations, including the rescheduling of this programme which had collapsed with the demise of Metronet's contracting arm (Trans4M), along with the development of a programme for the Bakerloo Line which sees delivery of the trains in 2020 and the signalling in 2022, enabled a further £0.8bn to be reduced from the original Metronet plan.

The most recent Annual Asset Management Plan (AAMP) shows continued significant investment with a focus on the Line Upgrades.[56]

4 TfL takeover of Tube Lines, 2009-10

Following the collapse of Metronet questions were raised about the future prospects for Tube Lines in the context of the upcoming periodic review and the amount of money that Tube Lines would need to raise over the review period. For example, *The Sunday Telegraph* reported:

> Senior figures in TfL say that if the arbiter requires Tube Lines to raise some of that money itself, it is unlikely to be able to do so given the current state of the bond markets, and could fall into administration. Alternatively, in these circumstances the arbiter can order a so-called "special mandatory sale" of Tube Lines to TfL.

[56] op cit., H*London Underground PPP report 2008/2009*H, pp24-26

> [...] Another option is TfL taking over Tube Lines by buying out its equity. This would only proceed if it could provide a saving to taxpayers greater than the cost of buying out the shareholders.[57]

In December 2009, the PPP Arbiter, Chris Bolt, announced that as part of the Tube Lines periodic review, for the next 7.5 years, he was proposing costs of £4.4 billion, as opposed to Tube Lines' bid for £5.75 billion.[58] This was a draft direction and, after representations from LU and Tube Lines, he made his final ruling in March 2010 raising the final cost to £4.46 billion.[59] Following the Arbiter's draft announcement in December 2009 the Mayor of London, Boris Johnson, was quoted as calling the whole PPP "a complete shambles" and speculation increased about whether the PPP might come to an end:

> Bolt's figure is bad news for both sides, because London Underground estimated that the work would cost just £4bn - leaving LU with the choice of finding £400m worth of savings, or cutting £400m of upgrades out of the programme.
>
> [...] Insiders said the announcement posed serious questions about Tube Lines' viability. It is co-owned by the US project management firm Bechtel and the UK company Amey, a subsidiary of Spain's Ferrovial, the majority shareholder in airport owner BAA. David Begg, chairman of Tube Lines, said LU management was openly trying to close down the PPP. "This is an arranged marriage where one partner does not want to be in it," he said.[60]

Finally, in May 2010 TfL announced its intention to buy out Bechtel and Amey's shares in Tube Lines for £310 million, effectively taking over the company and bringing the whole Underground back into public ownership.[61] The acquisition was completed on 27 June 2010 and was followed in September by a consultation on how to restructure the company now that it was owned by TfL.[62] Between August and October 2011 TfL acquired £1.3 billion of Tube Lines' £1.6 billion debt. TfL stated that because of its AA+ credit rating, this will allow it to "achieve more competitive borrowing rates than those secured by Tube Lines, delivering significant savings over the long-term".[63]

5 Upgrading the London Underground under TfL, 2010-

The TfL LU investment programme 2010 sets out in detail what it expects to deliver in terms of upgrades on the Underground to 2018. This includes new depots, station improvements, signalling and line upgrades. The full list of schemes to be completed over this period is given on the following page:

[57] "Boris fury threatens future of Tube Lines", *The Sunday Telegraph*, 13 December 2009

[58] PPP Arbiter press notice, "HPPP Arbiter announces draft decisions on Tube Lines Periodic ReviewH", 17 December 2009; Hfull draft decisionH available on the Arbiter's website

[59] PPP Arbiter press notice, "HPPP Arbiter sets final costs for Tube Lines and confirms funding gap for London UndergroundH", 10 March 2010; the Hfull decisionH is available on the Arbiter's website

[60] "HLondon Underground's PPP overhaul deal edges nearer collapse after funding verdictH", *The Guardian*, 18 December 2009

[61] TfL press notice, "HTransport for London to acquire the shares of Tube LinesH", 7 May 2010

[62] TfL press notices, "HNew era for the Tube as Transport for London completes acquisition of Tube LinesH", 27 June 2010; and "HConsultation commences to re-shape Tube Lines for the futureH", 15 September 2010

[63] TfL press notice, "HTransport for London acquires Tube Lines' bondsH" 19 October 2011

LU-PF35	Step-free access
LU-PJ03	Seven-car train project
LU-PJ06	Customer information improvements
LU-PJ110	King's Cross congestion relief (CTRL)
LU-PJ111	Victoria station upgrade
LU-PJ154	LU track – BCV
LU-PJ155	LU track – PPP JNP
LU-PJ156	LU track – SSR
LU-PJ157	LU structures – BCV
LU-PJ158	LU structures – PPP JNP
LU-PJ159	LU structures – SSR
LU-PJ160	LU rolling stock – BCV
LU-PJ161	LU rolling stock – PPP JNP
LU-PJ162	LU rolling stock – SSR
LU-PJ163	LU depots – BCV
LU-PJ164	LU depots – PPP JNP
LU-PJ165	LU depots – SSR
LU-PJ166	LU signals – BCV
LU-PJ167	LU signals – PPP JNP
LU-PJ168	LU signals – SSR
LU-PJ169	LU line upgrades – BCV
LU-PJ170	LU line upgrades – PPP JNP
LU-PJ171	LU line upgrades – SSR
LU-PJ180	BCV Station Programme
LU-PJ181	JNP Station Programme
LU-PJ182	SSR Station Programme
LU-PJ219	Green Park station step-free access
LU-PJ231	LU-managed Connect communications
LU-PJ24	Bank station congestion relief
LU-PJ25	Bond Street station congestion relief
LU-PJ251	Wide-aisle gates
LU-PJ273	Train location information
LU-PJ299	Stratford station upgrade
LU-PJ300	Cooling the Tube programme
LU-PJ31	Paddington station congestion relief
LU-PJ32	Tottenham Court Road station
LU-PJ33	Vauxhall station congestion relief
LU-PJ336	Southfields station step-free access
LU-PJ339	Victoria line power optimisation
LU-PJ369	Piccadilly service control
LU-PJ371	Operational accommodation
LU-PJ38	Thameslink programme
LU-PJ391	Northern Line Upgrade 2
LU-PJ43	Rayners Lane track capacity
LU-PJ56	Major power works
LU-PJ92	Finsbury Park station upgrade

BCV = Bakerloo, Central, Victoria lines
JNP = Jubilee, Northern, Piccadilly lines
SSR = Circle, District, Hammersmith & City, Metropolitan lines

The business plan for 2011/12 to 2014/15 states that "line upgrades are at the heart of the Underground's transformation":

> The Jubilee line will be completed in 2011. Next to be completed in 2012 will be the Victoria line. This will be followed in later years by the Northern and sub-surface lines (Circle, District, Hammersmith & City and Metropolitan lines). Across the network new trains and signalling systems will allow more frequent services and quicker, more comfortable journeys. Work has also begun on designing the next generation of low-energy, high-capacity Tube trains for the Piccadilly, Bakerloo and Central lines.
>
> Together the line upgrades will provide the transformation of the Underground, increasing capacity by 30 per cent. This represents the greatest investment in LU in its history, and provides as much additional space as building three more Jubilee lines.
>
> The scale of the task to upgrade the Tube unfortunately means some disruption to services, often at weekends. TfL's acquisition of Tube Lines in 2010 allows greater flexibility in how the works are carried out, which should lead to significantly reduced levelsof passenger disruption.
>
> In addition, TfL will consider other options such as 'extended closures', involving part of a line being closed for a period of weeks to accelerate works and allow it to be undertaken more efficiently. In such cases, TfL will always seek to ensure that alternative travel arrangements are available.[64]

The GLA budget update for the 2011/12-2014/15 business plan set out the finances for LU and Tube Lines (which is being maintained as a separate company) in two tables, as follows:[65]

London Underground and Tube Lines income, operating and capital expenditure plan

(£m)	2011/12 Forecast	2012/13	2013/14	2014/15	Total 2011/12 - 2014/15
Income					
Traffic revenue	1,956	2,106	2,287	2,488	8,837
Secondary revenue	164	178	192	205	740
Total income	**2,121**	**2,284**	**2,479**	**2,694**	**9,578**
Operating expenditure (incl. third-party contributions)					
Operating expenditure	(1,862)	(1,909)	(1,943)	(1,986)	(7,700)
Tube Lines operating expenditure	(353)	(376)	(424)	(423)	(1,576)
Total operating expenditure	**(2,215)**	**(2,285)**	**(2,367)**	**(2,409)**	**(9,276)**
Net operating (expenditure)/income	**(94)**	**(1)**	**113**	**284**	**302**
Capital expenditure (incl. third-party contributions)					
Capital expenditure	(1,030)	(1,187)	(1,275)	(1,199)	(4,691)
Tube Lines capital expenditure	(202)	(259)	(265)	(263)	(989)
Net capital expenditure	**(1,232)**	**(1,446)**	**(1,540)**	**(1,462)**	**(5,680)**
Net expenditure	**(1,326)**	**(1,447)**	**(1,428)**	**(1,177)**	**(5,378)**

64 TfL, H*Business Plan 2011/12-2014/15*H, p33
65 TfL, H*Business Plan - GLA Budget Update 2011/12 – 2014/15*H, pp10-11

Capital projects directly managed by London Underground and Tube Lines

(£m)	2011/12 Forecast	2012/13	2013/14	2014/15	Total 2011/12 -2014/15
Stations	(208)	(335)	(385)	(384)	(1,312)
Power	(103)	(126)	(107)	(91)	(427)
Track	(142)	(179)	(216)	(203)	(740)
Civils	(11)	(35)	(14)	(13)	(73)
Lifts and escalators	(14)	(17)	(31)	(29)	(91)
Sub-surface railway line upgrade	(501)	(545)	(572)	(532)	(2,150)
JNP line upgrades	(124)	(149)	(145)	(156)	(574)
BCV line upgrades	(119)	(49)	(62)	(31)	(260)
Infrastructure management	(23)	(9)	(7)	(3)	(42)
Other (including over-programming)	11	(2)	(1)	(20)	(12)
Total capital expenditure	**(1,232)**	**(1,446)**	**(1,540)**	**(1,462)**	**(5,680)**