House of Commons
Transport Committee

Update on the London Underground and the public-private (PPP) partnership agreements

Seventh Report of Session 2009–10

Report, together with formal minutes, oral and written evidence

Ordered by the House of Commons
to be printed 17 March 2010
The Transport Committee

The Transport Committee is appointed by the House of Commons to examine the expenditure, administration and policy of the Department for Transport and its associated public bodies.

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Mr David Clelland MP (Labour, Tyne Bridge)
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The following was also a member of the Committee during the period covered by this report:

Sammy Wilson MP (Democratic Unionist, East Antrim)

Powers

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The Reports and evidence of the Committee are published by The Stationery Office by Order of the House. All publications of the Committee (including press notices) are on the Internet at www.parliament.uk/transcom.

Committee staff

The current staff of the Committee are Annette Toft (Clerk), Adrian Jenner (Second Clerk), David Davies (Committee Specialist), Marek Kubala (Inquiry Manager), Alison Mara (Senior Committee Assistant), Jacqueline Cooksey (Committee Assistant), Stewart McIlvenna (Committee Support Assistant) and Hannah Pearce (Media Officer).

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1 Introduction

1. The Transport Committee and our predecessor committees followed closely the process which led to the London Underground Public Private Partnership (PPP) agreements in 2003. Over the last seven years we have continued to monitor the performance of the PPP and we have, on a number of occasions, placed on record our judgement that the PPP is flawed. In 2005, we concluded that “on the evidence we received, improvements in facilities and performance are not in proportion to the huge sums of money flowing through the PPP.” We stand by that judgement which was reinforced in July 2007 when Metronet, one of the two infrastructure companies (infracos) in a PPP agreement with Transport for London (TfL), went into administration with significant debts and having failed to meet its obligations for network improvements. Our 2008 Report, The London Underground and the Public-Private Partnership Agreements, recommended that, “If it is not possible in reality to transfer a significant proportion of the risk away from the public purse, a simpler—and potentially cheaper—public sector management model should seriously be considered.”

2. Our previous reports have described the PPP agreements in detail and what we consider to be their failings; it is not our intention to reiterate our full analysis here. The purpose of this short report is to provide an update on the remaining PPP agreement between TfL and Tube Lines. We consider whether the remaining PPP agreement has been working in the interests of taxpayers and passengers since the failure of Metronet. We also consider the performance of London Underground (LU) since May 2008 when it took over responsibility for the Underground lines formerly managed by Metronet. Finally, we provide an update on the first periodic review which will establish the context for the PPP until 2017.

3. We are grateful to the organisations and individuals who submitted written evidence and to the nine witnesses from whom we took oral evidence in December 2009 and January 2010. In connection with this inquiry, we visited London Underground in December 2009. The visit provided us with an insight into the work being undertaken by LU in introducing new trains, replacing signalling and renovating stations on the Victoria line. We are grateful to those who helped arrange our visit.

The demise of Metronet

4. LU entered into three separate PPP Agreements—with Tube Lines in December 2002 and with Metronet (two separate Agreements) in April 2003. Under the agreements, which were due to run for 30 years, the infracos would maintain, renew and upgrade parts of LU’s infrastructure in return for a set price agreed between TfL and the infraco. Any additional work carried out would be for an amount agreed by both parties. LU remained responsible

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3 HC (2007–08) 45
4 For a detailed explanation of the principles of the PPP see HC (2007–08) 45 and HC (2004–05) 94.
for delivering services to customers. The Government predicted that the PPP agreements would realise over £16 billion of investment in the Underground and £4 billion of savings through efficiency gains whilst utilising the expertise of the private sector.  

5. It soon became clear, however, that the PPP agreements were not delivering many of the improvements to the network that the Government had hoped. In 2005, we concluded that:

Availability is the most important factor for Tube travellers. All the infracos needed to do to meet their availability benchmarks was to perform only a little worse than in the past. On most lines, they did not even manage that. We hope that they will be able to meet the more demanding targets for availability expected in future; we have no confidence that will be the case.  

6. In addition, the claim that the PPP would result in value for money for the taxpayer was undermined when Metronet went into administration in July 2007. Metronet had overspent its budget for renovations and refurbishment, and was refused additional loans by its creditors. In our detailed analysis of Metronet’s failure, The London Underground and the Public-Private Partnership Agreements, we concluded that “the PPP model was flawed” and that the failings of Metronet’s management had led to its downfall. Our report, and the July 2009 report by the National Audit Office (NAO), The failure of Metronet, ascribed the infraco’s failure to:

a) Metronet’s poor corporate governance and leadership;

b) Metronet’s shareholders also acting as suppliers in a tied supply chain with management structures which gave power to the suppliers, rather than the management of the business;

c) London Underground’s limited ability to manage the contract in a way that prevented costs from escalating, and

d) the inability of the PPP Arbiter to initiate an Extraordinary Review of the PPP Agreement with Metronet when it was clear that the infraco was experiencing difficulties, but before it entered Administration (under the terms of the PPP, the Arbiter could intervene only if invited to do so by one of the parties involved). 

7. Although Metronet’s failure was largely of its own making, the terms of the PPP agreements meant that it was taxpayers who footed most of the bill for its demise. According to the NAO, the total cost of Metronet’s collapse was £1.75 billion. Of that figure, Metronet’s parent companies—Atkins, Balfour Beatty, Bombardier, EDF Energy,
and Thames Water—were liable only for £70 million each. The taxpayer was liable for approximately £1.7 billion, equivalent to 95% of Metronet’s debt obligations. However, the NAO concluded that the overall direct loss to the taxpayer was in the range of £170 million–£410 million. The remaining loss was “an unanticipated upfront cost to the taxpayer and equivalent to paying off a mortgage early”—an obligation on the taxpayer through a grant from the DfT to TfL which would have fallen due at a later date in any case.\textsuperscript{10}

8. The Mayor of London, Boris Johnson, argued that the cost to TfL of Metronet’s demise was in fact £550 million because, he argued, the NAO estimate did not take into account work left undone by Metronet, which LU has addressed subsequently, or work outstanding which needs to be completed by LU in the future.\textsuperscript{11} TfL’s submission to this inquiry stated that “LU has also had to deal with the financial legacy of Metronet’s collapse—the result of poor programme management and system integration, ineffective cost control, a lack of forward planning and inefficient fiscal management”.\textsuperscript{12}

9. All witnesses to our inquiry accepted that Metronet’s failure cost the taxpayer millions of pounds and that the structure of the PPP left the taxpayer to bear a large financial risk. The Mayor, Boris Johnson, described Metronet’s PPP agreements as “a system that was not operating in the interest of taxpayer value, that ballooned until the point of explosion”.\textsuperscript{13}

10. As we stated two years ago, the failure of Metronet demonstrates the flawed nature of the PPP agreements which placed an unacceptable burden of risk on the taxpayer. Metronet’s demise, which cost the taxpayer at least £170 million, has cast a long shadow of doubt over the remaining PPP agreement with Tube Lines.

2 The performance of Tube Lines and the London Underground

11. Following Metronet’s demise, responsibility for improvement and maintenance work on the Underground is as follows:

<p>| Table 1: Responsibility for improvements to the Underground network, March 2010 |</p>
<table>
<thead>
<tr>
<th>Tube Lines</th>
<th>TfL (formerly Metronet BCV)</th>
<th>TfL (formerly Metronet SSL)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Jubilee</td>
<td>Bakerloo</td>
<td>Circle</td>
</tr>
<tr>
<td>Northern</td>
<td>Central</td>
<td>District</td>
</tr>
<tr>
<td>Piccadilly</td>
<td>Victoria</td>
<td>Hammersmith &amp; City</td>
</tr>
<tr>
<td></td>
<td>Waterloo &amp; City</td>
<td>Metropolitan</td>
</tr>
</tbody>
</table>

Source: Department for Transport

\textsuperscript{10} The National Audit Office, The failure of Metronet, HC 512, 5 June 2009
\textsuperscript{11} Q 18
\textsuperscript{12} Ev 46
\textsuperscript{13} Q 2
Tube Lines (in collaboration with its parent companies Bechtel, and Amey, a subsidiary of Ferrovial) has been responsible for the upgrade and maintenance of the Jubilee, Northern and Piccadilly lines since 2002. The two former Metronet companies were transferred to TfL ownership in May 2008. London Underground, a subsidiary of TfL, is currently responsible for the day-to-day running and upkeep of the lines previously managed by Metronet on behalf of TfL.

12. The day-to-day performance of Tube Lines, and now London Underground, is judged on three outcomes: availability (assessed in lost customer hours, weighted according to the type of service disruption), the ambience of the network (the quality of the passenger experience) and the speed and quality of fault rectification.14

13. As we have noted in previous Reports, the ambience of travelling on the Tube has improved under the PPP. During this inquiry, Tube Lines told us that, since 2002, it has completed the upgrade and refurbishment of 72 of the 96 stations along the Jubilee, Northern and Piccadilly lines. In addition, improvement work was in progress on 13 stations, with work on the remaining 11 due to begin shortly. Tube Lines has also completed 76 lift and escalator refurbishments across the three lines.15

14. The improvements made to station infrastructures are welcome. However, as we noted in our 2005 report:

...ambience is the easiest of the three performance measures to improve, and although it is important to customers, it is less important than a speedy, reliable service.16

Tube passengers are most concerned about whether trains are available and reliable and it is against this measure that the performance of Tube Lines, and now London Underground, is judged.

**Tube Lines**

15. The Department for Transport (DfT) measures reliability against “the availability indicator”. The measure records “Lost Customer Hours”, resulting from delays and service interruptions, against a benchmark figure set out in the PPP agreements. The performance of Tube Lines between 2003 and 2009 is shown in Table 2 below.

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14 See www.tfl.gov.uk/pppreport for monthly performance figures.
15 Ev 35
Table 2: Lost customer hours against benchmark on the lines managed by Tube Lines

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</thead>
<tbody>
<tr>
<td>Jubilee</td>
<td>33% worse</td>
<td>1% better</td>
<td>8% better</td>
<td>20% better</td>
<td>0%</td>
<td>9% worse</td>
</tr>
<tr>
<td>Northern</td>
<td>32% worse</td>
<td>95% worse</td>
<td>62% worse</td>
<td>23% worse</td>
<td>25% worse</td>
<td>31% better</td>
</tr>
<tr>
<td>Piccadilly</td>
<td>8% better</td>
<td>52% better</td>
<td>63% better</td>
<td>51% better</td>
<td>49% better</td>
<td>54% better</td>
</tr>
</tbody>
</table>

Source: London Underground PPP & Performance Report 2008–09

16. In every year since 2003–04, Tube Lines has performed consistently better than its benchmark target on the Piccadilly line. On the Northern line, the infraco’s performance has bettered the benchmark only once, in 2008–09. This is because Tube Lines took over the Northern line when its infrastructure was in a particularly parlous state. Having completed a number of track and infrastructure improvements, Dean Finch, the former Chief Executive of Tube Lines, told us that the Northern line was now “one of the best performing metro lines [...] anywhere in the world”.18 Taken together, the performance of Tube Lines on the two lines, compares favourably with the record of Metronet—a point recognised by TfL which noted that Tube Lines had “showed more consistency in day-to-day maintenance performance”.19

The Jubilee line upgrade

17. Tube Lines’ recent performance on the Jubilee line, has been less satisfactory.20 Until 2008–2009, the performance on the line was deemed satisfactory, but since then, it has been judged to fall short of the “acceptable level” of performance. The cause of Tube Lines’ underperformance on the Jubilee line over the past 18 months is the overrun of the upgrade to the signalling system which has resulted in serious disruption to passengers. The upgrade to the line, when completed, will provide a third more capacity. It was scheduled to have been completed by 31 December 2009, but will now not be finished before October 2010.

18. To enable the work to take place, Tube Lines initially asked London Underground for permission to close the line wholly or partially for up to 52 weekend days. However, the line was eventually closed either wholly or partially for 120 weekend days from April 2007 through December 2009. As the deadline for completion of the project approached, the line closed with greater frequency, sometimes with little notice—between September and November 2009, there was a full or partial closure of the Jubilee line on one or both days of every weekend.21 Over the Christmas holidays in 2009, the line was closed for four days, causing disruption at a particularly busy time of the year.

18 Q 50  
19 Ev 46  
20 The Jubilee line runs from Stanmore in North West London to Stratford in East London.  
21 London Assembly Transport Committee, Too close for comfort, Passengers’ experiences of the London Underground, December 2009
19. The disruption caused to the lives of residents and commuters who rely on the Jubilee line for work or leisure has been considerable. Tim Bellenger, Director of Research and Development, London TravelWatch, told us about the experience of a member of the public who relied on the Jubilee line to move around London:

She cannot plan her life properly now because she does not know whether or not the Jubilee line is going to be available, whether she is going to have to use a replacement bus for all or part of her journey. Essentially she is more dissatisfied now, because she does not know what is going to happen on the weekend.22

20. In addition to providing a vital link for commuters, the Jubilee line serves the entertainment venues of Wembley Stadium in North West London and the O2 Arena in South East London, and the ExCel exhibition centre in East London. In December 2009, The London Assembly Transport Committee reported the impact that the Jubilee line weekend closures had on those venues and their customers:

ExCel estimated that over one million visitors have been affected by disruption to public transport over the last two years and that it has lost 25% of its turnover due to the closures. It had paid some £500,000 a year in compensation to clients and measures to reduce the impact on visitors. The O2 had paid £400,000 in the last year for additional replacement transport for its customers when the Jubilee line was closed.23

21. Dean Finch, the then Chief Executive of Tube Lines, acknowledged that Tube Lines had underestimated the complexity and scale of the project on the Jubilee line and that this had contributed to the project running severely late. To his credit, Dean Finch apologised for the disruption to services on the Jubilee line and for the inconvenience experienced by passengers.24 However, he also acknowledged that the disruption would continue until October 2010 and that Tube Lines had requested further line closures over the Easter holidays. As a consequence of its failure to meet the deadline, Tube Lines will be fined £10 million per month from January 2010 until completion of the works.25

22. We are concerned that, despite over 100 weekend closures of the Jubilee line, including complete closures of the line during seasonal holidays, Tube Lines has failed to complete the upgrade on time. The ongoing disruption caused to people who rely on the Jubilee line to go about their daily lives, and the cost to businesses, is unacceptable.

23. We welcome Tube Lines’ apology and recognise that, in accordance with its PPP agreement, the company has been fined for its poor performance. However, that alone is not enough. Tube Lines must learn the lessons from its poor performance on the Jubilee line upgrade so that, in any future upgrades it undertakes, missed deadlines and disruptions for passengers are minimised. We call on Tube Lines to publish its plans for avoiding similar overruns to its projects in the future.

22 Q 86
23 London Assembly Transport Committee, Too close for comfort, Passengers’ experiences of the London Underground, December 2009
24 Q 35
25 Q 184
Changes to the scope of the project

24. Tube Lines placed much of the blame for the overrun of the signalling upgrade on LU. Both Tube Lines and TfL acknowledged that the upgrade is a complex project involving the introduction of signalling technology that has not been implemented in any other metro system in the world. According to Tube Lines, LU had, on a number of occasions, changed its requirements for the project quite significantly beyond the scope of the original agreement. It claimed that these changes had added significant costs and delayed the project further. The task was, according to Tube Lines, made harder because London Underground had:

Constantly sought to depart from the contractual structure established under the PPP Agreement […] by repeatedly seeking changes to the scope and/or manner in which works are carried out.

Tube Lines claimed that LU’s behaviour had resulted in the project costing the company an additional £327 million beyond the agreed price for the work. In an attempt to reclaim these costs and, in the face of opposition from TfL, Tube Lines appealed to the PPP Adjudicator, Alex Charlton QC. However, on 22 January 2010, the PPP Adjudicator ruled that:

Tube Lines case is dismissed in its entirety […] LU has not breached the PPP Contract as alleged [by Tube Lines] and is not liable for the amounts claimed (or any amount) in respect of the alleged breaches.

Track access

25. Any requests by Tube Lines for line closures over and above those set out in its PPP agreement have to be agreed by LU. There is only recourse of appeal to an independent body—the PPP Arbiter—if both parties agree to a referral. Dean Finch, the then Chief Executive of Tube Lines, argued that LU had contributed to the delay to the Jubilee line project by not granting his company sufficient track access to move heavy machinery into place and to turn off the power to the system:

London Underground is quite right in saying that it has granted a substantial volume of closures to Tube Lines. However, the important point is: has it granted those closures in the pattern, both in terms of duration and geography, that Tube Lines requested? In terms of the match request, they have only matched Tube Lines’ request to the extent of something just over 50%. The consequence of that is that Tube Lines has needed more access. If Tube Lines has requested a 52 hour closure

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26 Ev 35
27 Ev 43
28 Under the 1999 Act, if TfL and the infraco are unable to agree on a dispute then upon the request of the party who referred the dispute or difference to adjudication, a person is chosen by London Court of International Arbitration to act as adjudicator.
29 www.Tfl.gov.uk
and is granted two 27 hour closures, they do not amount to 52 hours of work because you have to power down and power up the railway.30

26. Tube Lines commissioned a review of its work on the Jubilee line from Phil Gaffney Consulting Ltd which concluded that Tube Lines and TfL were both to blame for delays. According to the report, Tube Lines had “significantly underestimated” the scope and complexity of the project and its management was slow to respond to problems when they occurred. On the other hand, the report concluded that TfL had allowed only a “limited amount of track access” to carry out the upgrade and that, while it had agreed to closures on 52 occasions, it was either for less time than requested or for a shorter section of the line, meaning Tube Lines could not make as much progress as it had planned.31

27. TfL responded that, rather than hampering the work of Tube Lines, it had tried to meet all “reasonable” requests for line closures. Its prime concern had been to restrict disruption to passengers as much as possible in the face of Tube Lines’ requests for ever more closures. TfL told us they had faced repeated requests for additional closures: “we were assured that granting a further 12, then a further six, closures was all that was needed”.32

28. The terms of the PPP agreement give TfL power to allow or to refuse requests for line closures over and above those stated in the agreement. There is clearly an inherent conflict between Tube Lines’ need to gain adequate access to the track and signalling system so that it can finish its work on time and TfL’s wish to minimise disruption to passengers. While there is insufficient evidence to conclude that TfL has behaved unreasonably in this instance, there is some evidence that it could have responded to Tube Lines’ requests for whole closures of the line more readily. We recommend that to avoid such squabbles in the future, the neutral PPP Arbiter should be responsible for making decisions on requests for additional line closures. The Department should make the necessary amendments to the PPP agreement to put this change into effect.

The use of secondments

29. We have noted previously that a prime cause of Metronet’s demise was its tied supply chain whereby Metronet intended to award some 60% of its projected capital projects in the first seven and a half year period to its parent companies. In our 2008 Report, we concluded that:

    The fact that such a management structure was judged to be capable of efficient and economic delivery seems extraordinary now that Metronet has collapsed but the ultimate recipients of the money which was paid to the company have walked away with limited losses. The Government must not allow this blurring between the roles of shareholder and supplier in future bids to carry out work by the private sector.33

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30 Q 48  
32 Ev 49  
30. Some witnesses argued that Tube Lines was in danger of replicating Metronet’s tied supply chain through its use of seconding work to its parent companies. However, Tube Lines told us that it seconded companies to carry out work on its behalf only after a competitive tendering exercise. The company argued that, unlike Metronet, it had not experienced any of the inherent conflicts of interests associated with operating a tied supply chain.

31. The PPP Arbiter accepted that Tube Lines’ use of secondments had generally avoided the problems experienced by Metronet. However, the Arbiter argued that in relation to the signalling upgrade:

   I think there is an issue, and maybe this is part of the experience with the Jubilee line, that a signalling project is actually an IT software project rather than a civil engineering one. I think there are questions about whether reliance on the Bechtel secondment arrangements in that case has enabled Tube Lines to manage that project as effectively as it might have done.\textsuperscript{34}

32. \textit{We remain convinced that Metronet’s tied supply chain was a major cause of its demise. Although we note similarities between Tube Lines’ practice of seconding work to its parent companies, we also note that, unlike Metronet, Tube Lines awards contracts only after a process of competitive tendering. We are concerned, however, that there may be a temptation for Tube Lines to award projects to its parent companies for which they do not possess the required expertise. Such practices may have contributed to delays on the upgrade.}

\textbf{London Underground}

33. It is widely accepted that LU inherited from Metronet some of the worst performing lines on the network. Starting from a low base, in the one full reporting year since then (2008–09), the company’s performance on lost customer hours has been better than the benchmark target on all lines apart from the Waterloo and City line, which is a remarkable 219\% below the benchmark.
Table 3: Lost customer hours against benchmark on the lines formerly managed by Metronet, now managed by London Underground

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<tbody>
<tr>
<td>Metropolitan, Circle, Hammersmith &amp; City</td>
<td>21% better</td>
<td>50% better</td>
<td>39% better</td>
<td>37% better</td>
<td>44% better</td>
<td>48% better</td>
</tr>
<tr>
<td>District</td>
<td>43% better</td>
<td>35% better</td>
<td>16% better</td>
<td>19% worse</td>
<td>53% worse</td>
<td>14% better</td>
</tr>
<tr>
<td>East London</td>
<td>4% better</td>
<td>2% better</td>
<td>34% better</td>
<td>29% better</td>
<td>20% better</td>
<td>Line closed</td>
</tr>
<tr>
<td>Bakerloo</td>
<td>15% better</td>
<td>34% better</td>
<td>13% better</td>
<td>10.7% worse</td>
<td>3% better</td>
<td>34% better</td>
</tr>
<tr>
<td>Central</td>
<td>16% worse</td>
<td>2% better</td>
<td>14% better</td>
<td>24% better</td>
<td>33% worse</td>
<td>33% better</td>
</tr>
<tr>
<td>Victoria</td>
<td>16% worse</td>
<td>9% worse</td>
<td>11% worse</td>
<td>26.7% worse</td>
<td>40% worse</td>
<td>23% better</td>
</tr>
<tr>
<td>Waterloo &amp; City</td>
<td>58% worse</td>
<td>12% worse</td>
<td>66% worse</td>
<td>29.2% worse</td>
<td>66% worse</td>
<td>219% worse</td>
</tr>
</tbody>
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34. Richard Parry, Interim Chief Executive at London Underground, told us that LU’s first aim had been to eliminate Metronet’s inefficient practices. As a consequence, a number of central support functions across LU were removed and duplications eliminated with the loss of around 1,000 jobs. In addition, LU had renegotiated Metronet’s key contracts and taken measures that it estimated would “save Londoners and taxpayers an estimated £2.5bn, now and in future”.

35. LU also maintained that, since 2008, it had carried out work on the former Metronet lines very efficiently. This claim was disputed by Tube Lines which further argued that it compared very favourably to LU in terms of value for money. The Tube Lines Chief Executive told us that Tube Lines’ delivered improvements to its three lines, at a cost approximately one-third cheaper than similar work carried out by LU on its lines.

36. Making comparisons on costs under the PPP is difficult. We have previously noted that the lack of comparable performance data is a significant failing of the PPP, a point also emphasised by the PPP Arbiter, Chris Bolt. The Arbiter went on to say that although he would value more information with which to make a direct comparison, the available information suggests that Tube Lines’ maintenance costs are lower on average than those of LU.

37. We were pleased to hear from the Arbiter that better information about both costs and the quality of the work undertaken by Tube Lines and LU is forthcoming. Chris Bolt told us that:

35 Ev 46
36 Q 47
37 Q 158
It is currently difficult to make a full assessment of the upgrade projects, given that most are still under way, and because of changes in reporting arrangements for Metronet following administration. The Arbiter is working with London Underground to develop information that would permit him to monitor the Metronet upgrades and use data gathered in this way as a benchmark for Tube Lines.38

38. It is clear that London Underground inherited from Metronet a number of lines that were under performing. Early indications are that London Underground has succeeded in cutting costs and improving performance on the lines it inherited. That is welcome.

39. We are, however, concerned by indications that London Underground’s work is up to one third more expensive than similar work undertaken by Tube Lines. It is important that reliable data about costs and the quality of work undertaken on all Underground lines is collated. We therefore welcome the Arbiter’s work with London Underground on developing information that will enable him to set performance benchmarks for the former Metronet lines. We look forward to these benchmarks being made public as soon as practicable.

Relations between Tube Lines and TfL

40. For the remaining PPP agreement to function effectively there must be good working relations between TfL and Tube Lines. Unfortunately, due to the disagreements over the Jubilee line upgrade, including a series of claims and counter-claims made by the two parties in public, relations between TfL and Tube Lines have deteriorated. The Mayor, Boris Johnson, told us about an acrimonious exchange he had in September 2009 with Riley Bechtel, one of Tube Lines’ parent companies.39 The Mayor has also written a number of letters to Tube Lines that are highly critical of its performance and which subsequently appeared in the press. Tube Lines described TfL as having adopted an “unco-operative approach” to Tube Lines since the PPP started in 2003.40

41. The lack of co-operation between the parties has had a detrimental effect on the programme to renovate the underground network and on the experience of passengers. The PPP Arbiter argued that “Tube Lines, operating in effective partnership with London Underground, could have delivered the Jubilee line upgrade on time and to budget, and could now be progressing well with the Northern line upgrade”.41 Laying blame on both sides, the Arbiter described how “it is absolutely clear that that concept of partnership has not always operated.42 The relationship between the two organisations was the poorest he had come across both in his current role and during his time as Chairman of the Office of Rail Regulation.43
42. We are deeply concerned at the increasingly antagonistic relationship, stoked by the Mayor, between TfL and London Underground on one side, and Tube Lines on the other. Relations between the parties have deteriorated further over the past year. They are the poorest that the PPP Arbiter has ever witnessed and both TfL and Tube Lines must bear responsibility for this sorry state of affairs. The PPP Agreement between Tube Lines and TfL will only succeed if all parties work in co-operation and in a spirit of goodwill on all sides.

3 The role of the PPP Arbiter

43. We have commented in previous reports that the PPP Arbiter should be given more power to collect rigorous and comparable data about the PPP. It remains our view that the gathering and publication of information by the PPP Arbiter will generally tend to benefit all interested parties: London Underground as client, the infracos as suppliers and the public as users. The Government should also find such information useful for monitoring the benefits and costs of the agreement. Any reporting process must be seen as neutral and be designed to provide the information that both the infracos and London Underground require to address performance issues and to prepare for periodic review. In 2008 we asked the Government to make the necessary changes to the PPP.44

44. In its Response to our Report the Government argued that changes to the PPP Arbiter’s powers were not necessary and, in the two years following Metronet’s demise, the Government has taken no action in this area. During this inquiry, the Minister, Rt Hon Sadiq Khan MP, told us that if the role of the Arbiter was to change, Parliament would have to amend the 1999 Greater London Authority Act. The Minister did not believe any such change was necessary in the short term:

> I am confident that Tube Lines are transparent with the Arbiter, with ourselves and with TfL….I am confident that the regime set up with the Mayor, elected by Londoners, to have independent scrutiny will lead to greater transparency and more information being passed to us, to give us the reassurance that you rightly say we need to have.45

TfL and London Underground are similarly reluctant to see the Arbiter’s powers increased. They regard the new monitoring arrangements, which have been introduced with the co-operation of the Department, as adequate.

45. In contrast, Tube Lines told us that it wishes to see the Arbiter’s role extended to monitoring the work of TfL on the former Metronet lines. Tube Lines argues that if the PPP Agreement’s objectives are to be met, then all those involved in the work must follow clear, accurate, transparent, and relevant reporting procedures.
46. As we said two years ago, the Arbiter should be able to carry out an annual review of all PPP contracts including those transferred to London Underground. This would help companies address performance problems and prepare for periodic reviews. We are disappointed that the Government has not implemented our recommendation to bring greater transparency and accountability to all of the work being carried out on the Underground network. We call on the Government to reconsider its stance.

4 The 2010 periodic review

47. The poor relationship between Tube Lines on the one hand, and TfL and LU on the other has continued into the periodic review exercise. Under the PPP Agreement, LU and Tube Lines are required to set out a programme of work for 2010–17 along with estimated costs. Some tension in the process is inevitable because the parties have conflicting objectives: Tube Lines wants to deliver the work as cost-effectively as possible so that it can provide dividends for its shareholders; TfL is seeking to maximise the work done whilst minimising cost.

48. TfL and Tube Lines began planning for the periodic review in 2009. Following informal discussions between the two parties, it became apparent that the two organisations’ estimates of the work that needed to be done during 2010–17 diverged very significantly. As negotiations between the two parties stalled, both parties submitted to the PPP Arbiter their estimates of the cost of an upgrade and maintenance programme from 2010–17, including an extensive upgrade of the Piccadilly line. The second set of projections were submitted by each party to the Arbiter, as required, on 17 November 2009. The main difference between the two submissions was “updating” to reflect the agreement reached between Tube Lines and TfL on the scope of the work programme and to take into account inflation. In total, Tube Lines’ 17 November submission proposed costs of £5.75 billion. London Underground considered that the appropriate level of costs was £4 billion.

49. On 17 December, the Arbiter published his “draft directions on costs and related matters” for the period 2010–17. The Arbiter judged that the cost of works on the Jubilee, Northern and Piccadilly lines over the seven and a half years from 1 July 2010 should be set at £4.4bn. According to Chris Bolt:

I have reviewed carefully the submissions from Tube Lines and London Underground, and taken expert advice. On the basis of my analysis, I consider that a company operating in an overall efficient and economic manner and in accordance with Good Industry Practice—the test in the PPP Agreement—could deliver its obligations at a substantially lower cost than projected by Tube Lines, though not as cheaply as suggested by London Underground.

50. The Arbiter reached his initial judgement by comparing Tube Lines’ estimated costs with similar projects undertaken on other metro systems, a process he referred to as international benchmarking. He found Tube Lines’ estimated unit costs to be significantly higher. In addition, the Arbiter explained that part of the £1.35 billion difference between his estimate and that of Tube Lines was a consequence of Tube Lines’ poor performance on the Jubilee line:
My assessment is that the notional infraco, which is the standard I have to use for pricing, would have delivered or could have delivered the Jubilee line on time and that as a consequence about three-quarters of the work on the Northern line would be completed in the first review period.\textsuperscript{46}

Therefore, some of the costs that Tube Lines expects to accrue in the second review period, should, according to the Arbiter, have been borne by the company during the first period. The Arbiter’s judgement encouraged TfL and Tube Lines to make further representations to his office before he published his final guidance in “early March 2010”.

51. The PPP Arbiter’s final directions and guidance, published on 10 March 2010, increased his initial estimate of the cost of the work to be carried out by Tube Lines during 2010–17 by £65 million to £4.465 billion.\textsuperscript{47} Alongside this guidance, the Arbiter recommended that London Underground should either: finance the £465 million shortfall between its estimate and the Arbiter’s final directions, or scale back the work that it required Tube Lines to carry out during 2010–17.\textsuperscript{48} TfL’s initial reaction to the Arbiter’s guidance was that the Arbiter had exceeded his powers by making directions on finance and that TfL would keep its options open.\textsuperscript{49}

**Implications for the future of the PPP**

52. The Arbiter’s guidance for 2010–17 has led some commentators to question whether Tube Lines and with it, in all likelihood, the PPP itself has a viable future. If Tube Lines is to deliver what it has agreed to, it will have to make up the funding gap of £1.5 billion between its own cost estimate and what TfL will pay. Tube Lines’ shareholders (Bechtel and Amey) must decide if they can afford to make up the difference or seek to raise additional funds for Tube Lines’ 2010–17 programme in a very difficult financial environment. Alternatively, if the management board of Tube Lines decides that neither option is feasible, then the company’s future involvement in the PPP will be in doubt. The former Chief Executive, Dean Finch, told us that Tube Lines would not follow Metronet into administration and that no conclusion about the company’s viability should be drawn from his decision to leave his position as Chief Executive of Tube Lines.\textsuperscript{50}

53. The Arbiter’s initial guidance also has implications for TfL which will have to find an additional £400 million to finance the work planned for 2010–17. If it cannot provide the additional funding through further increases or additional grants from the Government, it will need to review the scope of its requirements for the next seven and a half years. In all likelihood, this could result in fewer station refurbishments or less ambitious track renewals.

\textsuperscript{46} Q 153  
\textsuperscript{47} www.ppparbiter.org.uk/output/Page1.asp  
\textsuperscript{48} Tube Lines will be required to deliver the refurbishment of stations and the completion of upgrades to the Northern and Piccadilly lines.  
\textsuperscript{49} TfL Press Release, Mayor and TfL: Arbiter’s Directions show PPP is “not delivering for Londoners and taxpayers” 10 March 2010  
\textsuperscript{50} Q 44
54. The fall out from the PPP Arbiter’s ruling on the costs for the second review period may take a while to become apparent. In the meantime, the process leading up to the Arbiter’s final ruling in March 2010 has subjected Tube Lines, responsible for three Underground lines, to a great degree of scrutiny. The level of transparency given to Tube Lines’ project planning and cost estimates is welcome; however, this degree of scrutiny is currently not applied to London Underground, itself responsible for managing improvements to seven Underground lines. As stated previously, this situation is one that this Committee recommended should be improved by granting the Arbiter more power to monitor the performance of TfL.

5 Conclusion

55. During our inquiry both the Mayor of London and the Minister of State for Transport argued that they were not ideologues with regard to the PPP. Both agreed with the position made by representatives from the trade unions, that passengers do not care who is responsible for improving the underground as long as the work is done effectively and within budget.

56. We reiterate once again our judgement that the PPP scheme is flawed. Some 20 months following the demise of Metronet, the Government is no nearer to being able to demonstrate that the PPP provides value for money for the taxpayer. The performance of Tube Lines has, in some cases, been exemplary. However, the sorry tale of the upgrade to the Jubilee line has marred its overall record badly. In the light of this project which, on current estimates, will be delivered 10 months late, the PPP has so far failed to prove that it is capable of delivering consistent value for money.

57. On the other hand, there is not sufficient evidence available to demonstrate whether London Underground is providing value for money in its work on the former Metronet lines. We reiterate our previous recommendations that the Government should prioritise transparency and accountability to taxpayers and passengers by extending the PPP Arbiter’s powers for the collection of data across the entire underground network—LU managed lines as well as those managed by Tube Lines.
Conclusions and recommendations

Introduction

1. As we stated two years ago, the failure of Metronet demonstrates the flawed nature of the PPP agreements which placed an unacceptable burden of risk on the taxpayer. Metronet’s demise, which cost the taxpayer at least £170 million, has cast a long shadow of doubt over the remaining PPP agreement with Tube Lines. (Paragraph 10)

The performance of Tube Lines and the London Underground

2. We are concerned that, despite over 100 weekend closures of the Jubilee line, including complete closures of the line during seasonal holidays, Tube Lines has failed to complete the upgrade on time. The ongoing disruption caused to people who rely on the Jubilee line to go about their daily lives, and the cost to businesses, is unacceptable. (Paragraph 22)

3. We welcome Tube Lines’ apology and recognise that, in accordance with its PPP agreement, the company has been fined for its poor performance. However, that alone is not enough. Tube Lines must learn the lessons from its poor performance on the Jubilee line upgrade so that, in any future upgrades it undertakes, missed deadlines and disruptions for passengers are minimised. We call on Tube Lines to publish its plans for avoiding similar overruns to its projects in the future. (Paragraph 23)

4. The terms of the PPP agreement give TfL power to allow or to refuse requests for line closures over and above those stated in the agreement. There is clearly an inherent conflict between Tube Lines’ need to gain adequate access to the track and signalling system so that it can finish its work on time and TfL’s wish to minimise disruption to passengers. While there is insufficient evidence to conclude that TfL has behaved unreasonably in this instance, there is some evidence that it could have responded to Tube Lines’ requests for whole closures of the line more readily. We recommend that to avoid such squabbles in the future, the neutral PPP Arbiter should be responsible for making decisions on requests for additional line closures. The Department should make the necessary amendments to the PPP agreement to put this change into effect. (Paragraph 28)

5. We remain convinced that Metronet’s tied supply chain was a major cause of its demise. Although we note similarities between Tube Lines’ practice of seconding work to its parent companies, we also note that, unlike Metronet, Tube Lines awards contracts only after a process of competitive tendering. We are concerned, however, that there may be a temptation for Tube Lines to award projects to its parent companies for which they do not possess the required expertise. Such practices may have contributed to delays on the upgrade. (Paragraph 32)

6. It is clear that London Underground inherited from Metronet a number of lines that were under performing. Early indications are that London Underground has
succeeded in cutting costs and improving performance on the lines it inherited. That is welcome. (Paragraph 38)

7. We are, however, concerned by indications that London Underground’s work is up to one third more expensive than similar work undertaken by Tube Lines. It is important that reliable data about costs and the quality of work undertaken on all Underground lines is collated. We therefore welcome the Arbiter’s work with London Underground on developing information that will enable him to set performance benchmarks for the former Metronet lines. We look forward to these benchmarks being made public as soon as practicable (Paragraph 39)

8. We are deeply concerned at the increasingly antagonistic relationship, stoked by the Mayor, between TfL and London Underground on one side, and Tube Lines on the other. Relations between the parties have deteriorated further over the past year. They are the poorest that the PPP Arbiter has ever witnessed and both TfL and Tube Lines must bear responsibility for this sorry state of affairs. The PPP Agreement between Tube Lines and TfL will only succeed if all parties work in co-operation and in a spirit of goodwill on all sides. (Paragraph 42)

The role of the PPP Arbiter

9. As we said two years ago, the Arbiter should be able to carry out an annual review of all PPP contracts including those transferred to London Underground. This would help companies address performance problems and prepare for periodic reviews. We are disappointed that the Government has not implemented our recommendation to bring greater transparency and accountability to all of the work being carried out on the Underground network. We call on the Government to reconsider its stance. (Paragraph 46)

Conclusion

10. We reiterate once again our judgement that the PPP scheme is flawed. Some 20 months following the demise of Metronet, the Government is no nearer to being able to demonstrate that the PPP provides value for money for the taxpayer. The performance of Tube Lines has, in some cases, been exemplary. However, the sorry tale of the upgrade to the Jubilee line has marred its overall record badly. In the light of this project which, on current estimates, will be delivered 10 months late, the PPP has so far failed to prove that it is capable of delivering consistent value for money. (Paragraph 56)

11. On the other hand, there is not sufficient evidence available to demonstrate whether London Underground is providing value for money in its work on the former Metronet lines. We reiterate our previous recommendations that the Government should prioritise transparency and accountability to taxpayers and passengers by extending the PPP Arbiter’s powers for the collection of data across the entire underground network—LU managed lines as well as those managed by Tube Lines. (Paragraph 57)
Formal Minutes

Wednesday 17 March 2010

Members present:
Mrs Louise Ellman, in the Chair

Mr David Clelland
Mr Phillip Hollobone
Mr John Leech

Mr Eric Martlew
Ms Angela C. Smith
Graham Stringer

Draft Report (Update on the London Underground and the public-private partnership (PPP) agreements), proposed by the Chair, brought up and read.

Ordered, That the draft Report be read a second time, paragraph by paragraph.

Paragraphs 1 to 57 read and agreed to.

Resolved, That the Report be the Seventh Report of the Committee to the House.

Ordered, That the Chair make the Report to the House.

Ordered, That embargoed copies of the Report be made available, in accordance with the provisions of Standing Order No. 134.

Written evidence was ordered to be reported to the House for printing with the Report.

[Adjourned till Wednesday 24 March at 2.30 pm]
Witnesses

Wednesday 9 December 2009

Mr Boris Johnson, Mayor of London, and Mr Richard Parry, Interim Managing Director, London Underground at Transport for London  Ev 1

Mr Dean Finch, Chief Executive, Tube Lines  Ev 6

Mr Steve Grant, District Organiser for London Underground, ASLEF; Mr Bob Crow, General Secretary, RMT (National Union of Rail Maritime and Transport Workers); and Mr Tim Bellenger, London TravelWatch  Ev 9

Rt Hon Sadiq Khan MP, Minister of State for Transport, and Ms Bronwyn Hill, Director General, City and Regional Networks, Department for Transport  Ev 14

Wednesday 6 January 2010

Mr Chris Bolt CB, PPP Arbiter  Ev 20

List of written evidence

1 ASLEF  Ev 27
2 The PPP Arbiter  Ev 28
3 London TravelWatch  Ev 32
4 Tube Lines  Ev 35
5 National Union of Rail, Maritime and Transport Workers (RMT)  Ev 43
6 Transport for London (TfL)  Ev 46, 49
7 Department for Transport (DfT)  Ev 51, 56
8 Martin Blaiklock  Ev 58
List of Reports from the Committee during the current Parliament

The reference number of the Government’s response to each Report is printed in brackets after the HC printing number.

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First Report The future of aviation HC 125–I and –II (HC 388)
Second Report Work of the Committee in 2008–09 HC 262
Third Report Priorities for investment in the railways HC 38
Fourth Report The performance of the Department for Transport HC 76
Fifth Report The proposal for a National Policy Statement on Ports HC 217
Sixth Report The new European motorcycle test HC 442
Seventh Report Update on the London Underground and the public-private (PPP) partnership agreements HC 100

Session 2008–09
First Report Work of the Committee in 2007–08 HC 211
Second Report School Travel HC 351 (HC 561)
Third Report Appointment of the Chair of the Office of Rail Regulation HC 433
Fourth Report The effects of adverse weather conditions on transport HC 328 (HC 957)
Fifth Report The use of airspace HC 163 (HC 996)
Sixth Report Taxes and charges on road users HC 103 (HC 995)
Seventh Report The enforcement activities of the Vehicle and Operator Services Agency (VOSA) HC 39 (HC 1057)
Eighth Report Rail fares and franchises HC 233 (HC 1004)

Session 2007–08
First Report Galileo: Recent Developments HC 53 (HC 283)
Second Report The London Underground and the Public-Private Partnership Agreements HC 45 (HC 461)
Third Report Work of the Committee in 2007 HC 248
Fourth Report The future of BAA HC 119 (HC 569)
Fifth Report Ticketing and Concessionary Travel on Public Transport HC 84 (HC 708)
Sixth Report The Blue Badge Scheme HC 475 (HC 1106)
Seventh Report Department for Transport Annual Report 2007 HC 313 (HC 1102)
Eighth Report Freight Transport HC 249 (HC 1103)
Ninth Report The Draft Marine Navigation Bill HC 709 (HC 1104)
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Oral evidence

Taken before the Transport Committee
on Wednesday 9 December 2009

Members present:
Mrs Louise Ellman, in the Chair
Mr Jeffrey Donaldson
Mr Philip Hollobone
Mr John Leech
Mr Eric Martlew
Ms Angela C Smith
Sir Peter Soulsby
Graham Stringer


Chairman: Good afternoon, gentlemen. Welcome to the select committee. Do Members have any interests to declare?
Ms Smith: I am a member of GMB and Unison.
Graham Stringer: I am a member of Unite.
Mr Martlew: I am a member of Unite and GMB.
Sir Peter Soulsby: I am a member of Unite.

Q1 Chairman: Louise Ellman, member of Unite. Could I ask our witnesses, please, to introduce themselves for our records?
Mr Johnson: I am Boris Johnson. I am the Mayor of London.
Mr Parry: I am Richard Parry, the acting managing director of London Underground.

Q2 Chairman: Thank you very much. Mayor, you have had to take over from the consequences of the collapse of Metronet. What would you say you have learned from that on how you are handling Tube Lines?
Mr Johnson: May I begin by saying, Mrs Ellman, what a joy it is to be back before you and your Committee and, just for the avoidance of doubt or any suggestion of any possible misconception of my motives at the end, I must leave unfortunately at 3.15 to go and do something else, but also because I do not want to hold up your timetable, as I know you have Tube Lines waiting in the wings. I do not want TfL to be in any way responsible for a Tube Lines delay, which is very much the issue in hand. What we have learned from the collapse of Metronet has been I think several things, or at least a couple of things. The first is that I think the Metronet structure was wrong. It did not serve the interests of the taxpayer well. It did not serve the London travelling public well and I think, going forward, what we need is a system that protects the taxpayer, that protects taxpayer value, and above all that enables London Underground to have proper oversight of the contracts that are essential for the delivery of a good service to London Underground passengers.

Q3 Chairman: Have you concluded that the public-private partnerships are wrong in principle?
Mr Johnson: No. I am not an ideologue who wants to take back the track or renationalise every aspect of London Underground; nor do I defend every particular of the public-private partnership because patently it has not worked to the advantage of the taxpayer and it has not worked to the advantage of the London travelling public. All I would really say is that I think what we need is a sensible system going forward. The key thing it has to deliver is taxpayer value and it can only really deliver that, in my view, if London Underground is given the ability to see what is really going on. I think part of the problem that we had with Metronet and certainly the problem that we have at the moment with Tube Lines has been just a lack of transparency. That is a key difficulty for us in London Underground. Obviously, the consequences for the London travelling public are pretty dire.

Q4 Mr Hollobone: Mayor, can we just get some of these time lines sorted out? Can you remind the Committee when you were elected Mayor of London?
Mr Johnson: I can. Thank you. I was elected in May 2008.

Q5 Mr Hollobone: When was Metronet taken into TFL ownership?
Mr Parry: That was shortly after that.

Q6 Mr Hollobone: In your mayoralty, one of the first problems you have encountered is the legacy of this system.
Mr Johnson: Yes. Patently, I think it was a poorly conceived system. I think if you were to get Shriti Vadera before your Committee to go through her thinking now about the PPP, I do not think that you would find her defending it very vigorously. I do not think anybody now thinks, even in the Treasury, that it was the right model, the right way to transfer risk to the private sector, which is what after all was intended by that PPP model, to try to liberate the energy and competitiveness of the private sector without greatly exposing the public purse to unnecessary risk. That was the idea. I do not think it did achieve that. It has been a substantial drain on TfL finances to have to deal with the ensuing catastrophe.

Q7 Mr Hollobone: You have inherited the problems caused by Metronet but under your mayoralty I suppose the big question is: is Tube Lines going the same way as Metronet? Surely on that question the same answer applies. Surely the big question is: is Tube Lines going to be cheaper than the PPP. I do not think that would be right. Richard may want to amplify this but my feeling is that the arbiter is going to produce his view on 17 December about the equitable price for the second review period. I think we should see what happens. What Londoners want is a convincing account from Tube Lines about how they are going to deliver these upgrades.

Q8 Mr Martlew: Is it not a fact that Tube Lines are doing the work 30% cheaper than London Underground? I think there was a freedom of information request from The Guardian that says that. Is that not correct?
Mr Johnson: No, it is not.

Q9 Mr Martlew: Mr Parry, what is your view?
Mr Parry: We do not think that is correct.

Q10 Mr Martlew: Can I be less specific then and take the 30% out? Is it not correct that Tube Lines are doing the work cheaper than London Underground?
Mr Parry: There are exercises under way to benchmark the work that Tube Lines or over the PPP. I do not think that would be right. Richard may want to amplify this but my feeling is that the arbiter is going to produce his view on 17 December about the equitable price for the second review period. I think we should see what happens. What Londoners want is a convincing account from Tube Lines about how they are going to deliver these upgrades.

Q11 Mr Martlew: Let us just talk about Tube Lines. Mr Parry: When you examine those costs, there are various different ways of comparing costs. You have very different railways. You have very different arrangements that apply. There are some legacy arrangements and when you look at that you can find different ways of cutting that, some that will show you Tube Lines is cheaper, some that will show that London Underground is cheaper and some that will show that they are broadly the same. The key thing that we have tried to work with Tube Lines and the arbiter on is to understand how there is scope for improvement and for delivering greater economic efficiency in the way that we manage the Underground. It is not true that there is a simple comparison that just says they are 30% cheaper.

Q12 Mr Martlew: Therefore it is not true for the Mayor to say, “No, they are not” either, is it, by definition, which he has just said. You have the Jubilee Line which is a signalling issue. I think I was reading something in the paper about the number of weekends that it needs to be off operation recently. I think it was about 28, if I recall. How much of that will be for driver training on the Jubilee Line? It is a new signalling system. I understand you have not negotiated with the trade unions about this at all yet. Is that the case?
Mr Parry: No, that is not true.

Q13 Mr Martlew: How much of it will be for driver training?
Mr Parry: Any major project of this sort delivering new signalling includes within its programme a last stage which is about bringing the railway into operational readiness for use in revenue service. That has always been the case for the Jubilee Line upgrade, as it has been for every other upgrade. That will require a short amount of access at the back end of the plan. We are still discussing with Tube Lines the full scope of the additional closure that they need in 2010, having used significant access as we all know through 2009 and the years prior. We expect that Tube Lines will use of the order of 28 closures, as I said earlier this week. The exact detail of that is being worked out. They will not all be full line closures. They will not all be full weekends, but there will be some closure activity most weekends through first six to eight months of 2010. At the very back end of that, some of that time will be used with our drivers using the system prior to going into revenue service.

Q14 Mr Martlew: That is something we can take up with ASLEF when they come before us later. The Jubilee Line is being upgraded by Tube Lines. The Victoria Line is being upgraded by yourselves. When is that likely to be completed? Is there going to be any overrun on costs?
Mr Parry: On the Victoria Line, it was a former Metronet project to deliver. Their contract date was 2013. They always had a target date that was ahead of that. Since the collapse of Metronet and us picking up that work with Bombardier and Invensys as the contractors, we have sustained the programme. We are delivering the programme as expected. We are seeing the first new train running in passenger service on the line today. The new signalling system is also in place and is working when we are testing that system. That will run and we expect to deliver on schedule by something like the early part of 2012, which will actually be about a year ahead of the original date that Metronet were working to.

Q15 Mr Martlew: And the costs?
Mr Parry: We are confident that the costs are within the budget we are working to. A lot of the contractual arrangements were inherited from
Metronet, but we have picked up those contracts and we are delivering that project on time and on budget as we stand today.

Q16 Chairman: And the Jubilee Line?
Mr Johnson: The Jubilee Line is being upgraded by Tube Lines, as Mr Martlew correctly indicated. That frankly is not going well. Mr Martlew referred to the number of closings he had read about in the newspaper. Indeed, there has been a very significant number of closings since last year. As he says, another 25 seem to be demanded by Tube Lines. The situation is really very unsatisfactory and I do think that it goes to the heart of what is wrong with the structure, because you fundamentally have a system in which Bechtel, a leading engineering firm as you know, has to manage a software programme which is basically being delivered by a bunch of Canadian software programmers in Toronto. With the best will in the world, I could not, hand on heart, now say that programme of managing the software delivery for the Jubilee Line upgrade has been effectively done. I am going off piste here, but that is the fundamental problem.

Q17 Chairman: It is a management problem?
Mr Johnson: I would say it is a management problem. The difficulty that the Tube Lines/PPP structure creates is that, because Bechtel is not only a shareholder but also a contractor, there is no very clear way of making sure that Bechtel has a very strong incentive to get it done in a timely way and to deliver taxpayer value. Getting back to what Mr Martlew was saying about the relative costs of Tube Lines versus London Underground in doing the upgrades, I happen to think that Richard is right and that the statistics that you have seen are misleading. If Tube Lines can do this very cheaply and if they can do it in a timely, effective way, that is what we want to see. I want to be totally pragmatic about this. If they can do it cheaply and in a transparent way and get a grip on the upgrades, then I think that would be ideal for all concerned.

Q18 Ms Smith: In the memorandum of evidence from Transport for London, it does say that the National Audit Report put the losses to the taxpayer of Metronet’s failure at something between £170 million and £410 million. Is that accurate?
Mr Johnson: I will ask Richard, if I may, to elaborate. We think that when you take various other costs into account the bill rises to about £550 million.

Q19 Ms Smith: We are talking at the top end of that initial estimate and more?
Mr Johnson: That is correct.
Mr Parry: We understand how the NAO made their calculation but it was limited to an historical calculation but it was limited to an historical calculation so it did not really look at the additional cost being incurred by Transport for London in getting hold of the programmes of work that were left, in some cases as we saw on the stations, in a very poor state. We have had to spend additional money to complete work that in effect Metronet had been paid for doing so you have to add that amount on top of the amount identified by the NAO. The other thing that is also worth saying of course is that the collapse of Metronet brought forward a lot of costs that would otherwise have been paid but would have been paid over the 30 years. For example, the costs of the debt that had to be paid. The costs incurred with the new trains, the new signalling that were proposed to be paid over the 30 year term are now going to be paid for in 2009/10 going forward. That has changed the profile of the costs as well as the total cost.

Q20 Ms Smith: You mentioned the refurbishment of stations. You will have seen the media speculation today about the possible closure of 142 and the intention to ensure that smaller stations will only have staff issuing tickets during peak hours. Is this true?
Mr Parry: We are firmly committed to providing staff at all stations across the London Underground throughout the day. That is fundamental to our service proposition. We know it is what customers value. We are looking at options, as every public service is doing right now in the current economic climate, as to how we can ensure that our overall service operation is efficient, effective and delivers the service that customers value. That piece of work is ongoing. It is part of the overall change we are bringing about on the Underground which will bring forward the new trains, the new signalling. We have changed the focus within the Underground to make sure that we have the business that we need going forward.

Q21 Ms Smith: Mr Johnson, your manifesto commitment was to ensure that there was a manned ticket office at every station.
Mr Johnson: I prefer to use the phrase “staffed”.
Ms Smith: I am using what I thought was your phrase.
Chairman: I am glad to hear you have the up to date words.

Q22 Ms Smith: Are you now saying that that will only be during the day time?
Mr Johnson: No, but you are right to raise it. There is no question that in very tough economic times you have to look at what savings you can make in a pragmatic way. I have not seen the leaked document that I think forms the basis of your question but Richard is absolutely right to stress that it is our job to make sure that the London travelling public have all the safety and reassurance that they deserve and that goes with having a fully staffed station at all times. Whether or not you have a person behind glass in a ticket office at all times is another matter. I understand that people want this and I understand that a lot of people believe that this is absolutely essential to the safe operation of stations. I am going to have to look at the evidence and decide whether or not we can deliver that kind of safety and that kind of reassurance by staffing all stations at all times and not staffing ticket offices at all times. That is the issue for us. I fully understand where you are...
Q23 Mr Leech: You mentioned about the involvement of Bechtel as a parent company and as a contractor. This was part of the disastrous collapse of Metronet, the involvement of the parent companies as contractors. My understanding is that while Terry Morgan was the CEO they tended to be able to keep the parent companies out of it and they were going out to the market for best value. Why has that changed?

Mr Johnson: I am afraid I cannot give you any guidance in the dispensation under Terry Morgan or anyone else. All I can say is that it is my impression, as you say, that with the structure of the PPP in which you have shareholder companies being asked to deliver taxpayer value you have an inherent conflict, because their duty is at once to their shareholders and to the taxpayer. Those two duties conflict.

Mr Parry: The Tube Lines model is different to Metronet’s. The work is procured independently of the supply chain. The point that the Mayor is making is that Bechtel’s role within the Tube Lines organisation is to second people in who will then run the project side of that business. Whist that has been successful in delivering some of the stations’ programmes over the early years, it is the first really significant test for the Tube Lines organisation that is delivering a line upgrade. We have put on record our very grave concerns about how that has been managed. It is undeniably very, very significantly late. We cannot give you an answer. Tube Lines are on later to talk about this. We do not have an answer for why it is late and what has happened but our observation is you have people from within the Bechtel organisation sitting in key roles who are, it seems, not capable of delivering this upgrade. We have put on record our concern about that and our need for getting from Tube Lines a firm and credible plan for the delivery of this upgrade so that we can then make our own plans and we can then communicate to London to tell them what they are going to expect in the year or so ahead in terms of the disruption that will be caused on the Jubilee Line.

Mr Leech: What discussions have you had with Tube Lines and Bechtel about warning them about the potential consequences of going down this model road, because if two people are stood in front of a cliff and one jumps off most people, if they were the second person, would probably think that it is a bad idea to go down that same route. Have you had any discussions with Tube Lines and Bechtel about this?

Q24 Chairman: What can you tell us about what is happening? Could you tell us briefly where you have got to on it?

Mr Johnson: Where we are at the moment is that we have of course had a series of discussions both with Tube Lines and with Bechtel themselves. It would be fair to say I had a meeting with Riley Bechtel himself in my office in about September. It was what they call a frank, full and free exchange of views about this issue of transparency. It seemed to me at the time that there was no clarity for London about the speed at which we could expect these upgrades to be delivered and the number of times we were going to be asked to close sections of the Jubilee Line, greatly inconveniencing Londoners. Yes, I did have a fairly acrimonious exchange with Bechtel back in September and those points were put across, I hope, in a vivid way, but in the end what we want is to get to a stage, after the arbiter’s ruling, where as Richard says Tube Lines are able to put forward a clear and convincing account of how they are going to get the upgrades done.

Q25 Mr Donaldson: You mentioned earlier about Metronet and how Metronet is effectively in-house again. What is happening with their former obligations?

Mr Johnson: Their former obligations are being very largely fulfilled now by London Underground though clearly there has been scope to make substantial savings in the way that we go about it. After all, if you think about the Metronet structure, it involved in a large number of cases a great deal of man marking and the pointless duplication of officials. We have been able to winnow out quite a few layers of management to save £2.5 billion. Otherwise, as we were saying to Mr Martlew, the upgrades that Metronet was carrying out are broadly continuing. What we have been unable to persist with at the rate I would have liked is for instance the introduction of step free access to some stations in London, simply because of the straightened financial circumstances that we find ourselves in. There is no doubt that there is a crunch in the budget, very largely caused by a 6% fall in ridership on the London Underground. That has cost us between £700 million and £900 million. That is a huge abstraction of resources for TfL and we have had to compensate for that by making some reductions in the scope of the upgrades, but the principle has been at all times to deliver those Metronet upgrades that maximise the capacity of the Underground and get people moving from A to B as fast as possible and to reflect the fact that we think, notwithstanding the current fall in ridership, the demand for London Underground services is going to increase.

Q26 Graham Stringer: You said at the start that you did not think the government would come up with the idea of a PPP again for the tube. Rather surprisingly in their written evidence they are still wedded to the idea and they still think it is a jolly good thing. What would you put in its place?

Mr Johnson: Mr Stringer, I am not going to be tempted into reading the last rites over the PPP or announcing the death knell for Tube Lines. I do not think that would be right. Whatever model you come up with has to deliver taxpayer value and it has to allow London Underground some understanding of what is going on. That was the real flaw.
Q27 Graham Stringer: Do you think that is possible within the PPP structure? I understand the principles but is it possible within the PPP structure?
Mr Johnson: It has not proved possible so far. Richard, you may want to come up with a brilliant third way here.
Mr Parry: The answer for us, being pragmatic, is that we have had to recover the work undertaken by Metronet and put in new arrangements, often with supply contracts that it was necessary to take forward because we needed to maintain the work on the Underground. By having a much more straightforward, conventional, direct relationship with suppliers and a much more collaborative approach often in the way that we are delivering the major projects, we have seen significant benefits from working in that way. We always recognise that the delivery of these major enhancements to the Underground will be a private sector delivery model. What we have been able to establish is a much clearer, stronger, publicly owned applied function that is able to work very closely through direct contractual relationships to get things to happen, rather than to have the complexities of the PPP stand, as they are currently standing on the Jubilee Line, in the way of some of the progress that we needed to make. We are seeing, in the way that we have put in place arrangements following the demise of Metronet, a simple, more effective way of delivering these upgrades on the Underground.

Q28 Graham Stringer: The government justify their support for the PPP in saying that—
Mr Johnson: Do they still?

Q29 Graham Stringer: Yes. There is some written evidence that we have before us. They say that previously London Underground, when they were building the Jubilee Line, were 30% overspent and when you add the 1.7 billion for the debt and the half a billion it is still only 10%. Do you think that is a fair justification for the PPP?
Mr Johnson: I just think you have to take ideology out of it and look at what the system—

Q30 Graham Stringer: I am looking at the figures; it is not ideology.
Mr Johnson: In terms of the Jubilee Line upgrades?

Q31 Graham Stringer: No. In terms of comparing the old system. The government is saying that the PPP, with all its failings, is better than the old system. It is not a fair comparison. The question I am asking is: is there a better system still?
Mr Johnson: I think that what you want is a system where you do not have this conflict of interest inherent in the structure and you have a strong measure of accountability to London Underground of the people who provide the service for passengers in London of what is going on in the upgrades. The difficulty with the current system has been that it is just not transparent. If from all that you could argue that I am in favour of a more conventional model of the kind that is currently operating on, say, the Victoria Line, then yes, that seems to be working better. That seems to me to be delivering better value for Londoners.
Chairman: That sounds to me a bit more like the principle. You said it was not about principle at the beginning.

Q32 Sir Peter Soulsby: I just wanted to take you back briefly to the role of the PPP arbiter. The original arrangement with Metronet, as I understand it, was that the arbiter would report annually on their performance, efficiency and economy. In fact, the Committee recommended that that should be extended in future to all of the Infracos. Indeed, I think that has been supported by the National Audit Office. I understand you have resisted that. Would you like to explain why?
Mr Parry: I do not think it is a question of resisting it. I think we have an existing contract with Tube Lines so we are not able to say how we want to do things differently. There needs to be an arrangement agreed between us. We see the role of the arbiter as being effective in terms of what it needs to do right now. The arbiter has a role at this point in determining what the cost is going forward for Tube Lines. We have invited him to make that determination and we believe he has adequate powers in the role that he has today to do that. I do not think we believe that an annual review would have resolved the Metronet situation at that time, given the status of what was going on with Metronet at that time. We are reasonably comfortable with the position that the arbiter has with regard to the Tube Lines contract today but actually it is not something that is in our gift to change right now.

Q33 Sir Peter Soulsby: Is that something for Mr Bolt himself? A proposal has been made and has been rejected. It is something that this Committee has supported, the National Audit Office has supported and surely would be in the interests of greater transparency?
Mr Johnson: It would be but it just does not seem to have worked like that. I think Richard is right to say that the arbiter, whatever his function, was not able to stop the bill ballooning in the way that it did under Metronet. He was not able to prevent the system from collapsing. Obviously anybody who can exercise a downward pressure on the costs of this system is to be welcomed by me.
Chairman: Thank you, gentlemen.
Witness: Mr Dean Finch, Chief Executive, Tube Lines, gave evidence.

Q34 Chairman: Good afternoon. Would you like to identify yourself for our records, please?
Mr Finch: I am Dean Finch. I am chief executive of Tube Lines.

Q35 Chairman: We have just had evidence, as you may have heard, from Transport for London and the Mayor and it seems that you are very much at loggerheads with Transport for London in how you are developing the project, particularly in relation to the Jubilee Line. Would you say you had an unduly adversarial relationship?
Mr Finch: First of all, thank you for inviting me here to give evidence this afternoon. With regard to the Jubilee Line, can I say that on behalf of Tube Lines I apologise for it being late. We are sorry it is late and I am sure we will come on to the reasons why we think it is in a moment. Our relationship with London Underground ranges from extremely collaborative to quite adversarial, depending on which part of the business we are looking at. Fundamentally, I think having heard some of the evidence today with regard to the contract, my view is you can make any contract work. It requires effective partnership from both sides.

Q36 Chairman: Would you say there is real partnership in the very adversarial aspects of your relationship?
Mr Finch: I think that our relationship is improving. I can understand the frustration of the Mayor and of London Underground with Tube Lines for the delay of the Jubilee Line. Since joining, one of the steps I have taken is I now chair a weekly meeting between London Underground, ourselves and our contractor, Thales, where each week we discuss progress on the Jubilee Line and that has been going on now for some 12 weeks. I think that has helped improve transparency between us and London Underground and I think it is beginning to restore London Underground’s confidence that there is a credible programme which we are discussing, which will see an end date for the Jubilee Line project.

Q37 Chairman: What progress have you actually made? Can you give us some examples?
Mr Finch: As of this week on Tuesday for example one of the objects clearly of this weekly programme has been at weekly meetings to produce a programme which we can all believe in. Certainly, in terms of the director of line upgrades, he told me directly on Tuesday that he is happy with the programme that he is now discussing with London Underground, which will see the Jubilee Line finished next year.

Q38 Chairman: When next year?
Mr Finch: What we will see is, by May 2010, Tube Lines will have delivered the contractual obligation that it was supposed to have delivered by the end of this calendar year and the Jubilee Line will be into service by the autumn of 2010.

Q39 Mr Hollobone: When did you take over your current post at Tube Lines?
Mr Finch: I joined Tube Lines in May and became chief executive in June.

Q40 Mr Hollobone: Will you be getting a bonus this year?
Mr Finch: I expect not.

Q41 Mr Hollobone: If you were offered one, would you turn it down?
Mr Finch: Probably in relation to where Tube Lines performance is, I think overall the company is not going to be in a position to have earned a bonus this year, so I just do not think the question of that will arise.

Q42 Chairman: You do not expect to have the choice?
Mr Finch: I do not expect to have the choice.

Q43 Mr Hollobone: Is there any truth in the press reports that you have been approached to become the new chief executive of National Express?
Mr Finch: National Express have approached me, yes.

Q44 Mr Hollobone: That would be quite a handy lifeboat, wouldn’t it not, if Tube Lines is going the same way as Metronet?
Mr Finch: I do not believe Tube Lines is going the same way as Metronet. In specific relation to that question, clearly this is not something I have sought. It clearly is a substantial proposition which I have to discuss but you will appreciate that is something I have to discuss with my shareholders.

Q45 Mr Hollobone: The Mayor has kindly shared with the Committee a copy of his letter to you of 4 December in which he described the situation on the Jubilee Line as “unacceptable” and asking you for an urgent report on progress. Have you responded to that letter yet?
Mr Finch: I have.

Q46 Mr Hollobone: Would you be able to make a copy of that reply available to the Committee?
Mr Finch: Yes, absolutely.

Q47 Mr Martlew: You were obviously sitting at the back and you heard the comments both from the chief executive of London Underground and the Mayor. Is there anything in those comments that you disagree with?
Mr Finch: Yes, there is a number of things. In relation to Tube Lines, is it in the interest of the taxpayer, yes, I fundamentally believe it is. Its record is that since it took over it is 20 times safer for its employees; it has cut delays by half and its operating costs with regard to 2008/9 are a third cheaper than London Underground's. These are not data that we have invented. They are data that have been compiled by the arbiter. Indeed, I note in his submission to you he notes that in 07/8 Tube Lines' costs were cheaper than Metronet's costs and that in 08/9 Metronet's costs have gone up. In terms of a direct comparator between the average of the three...
lines that Tube Lines is responsible for and the five that were with the former Metronet companies, we are a third cheaper.

Q48 Mr Martlew: One of the excuses and reasons that you use for the delay is the fact that London Underground have not given you access to the line. Can you expand on that?

Mr Finch: There are a number of reasons why Tube Lines is late on the Jubilee Line. First and foremost, I think it is a huge leap in technology. As you may imagine, I have looked at this in some considerable detail and we have taken advice from others. Madrid did not attempt what is being attempted here in one leap. It tried to do it in at least two. I think Tube Lines and its contractor Thales failed to appreciate the extent of that leap. It is not as simple as to say that London Underground has not granted closures. London Underground is quite right in saying that it has granted a substantial volume of closures to Tube Lines. However, the important point is: has it granted those closures in the pattern, both in terms of duration and geography, that Tube Lines requested? In terms of the match request, they have only matched Tube Lines’ request to the extent of something just over 50%. The consequence of that is that Tube Lines has needed more access. If Tube Lines has requested a 52 hour closure and is granted two 27 hour closures, they do not amount to 52 hours of work because you have to power down and power up the railway.

Q49 Chairman: How many times has that happened?

Mr Finch: Just under 50% of match requests have not been met.

Q50 Mr Martlew: There has been no reference to the Northern Line which I understand you did work on. Is that correct? Is it not correct that if I look at London Underground’s website they boast about how well that is working?

Mr Finch: The Northern Line is one of the best performing metro lines I think probably anywhere in the world at the moment. I think that is a great example of where the partnership between London Underground and Tube Lines has worked very well indeed.

Q51 Mr Leech: You were here for my question to the Mayor about the involvement of the parent companies being at least partly responsible for the demise of Metronet and my suggestion that Bechtel were being too involved with Tube Lines. Was that a fair point that I made?

Mr Finch: I think Richard answered the question accurately. Bechtel are not a contractor of Tube Lines. They supply secondees. Those secondees fit into the management structure that reports to me and they are fully accountable to me for their performance.

Q52 Mr Leech: Their involvement does not have any adverse impacts on Tube Lines at all?

Mr Finch: I see Bechtel’s incentive as perfectly aligned with Tube Lines because fundamentally if Tube Lines runs out of cash there is a first call on Bechtel. To say there is no incentive on Tube Lines to deliver the Jubilee Line I fundamentally disagree with. There is a huge incentive on tube Lines to deliver the Jubilee Line on time, both in terms of reputational damage and in terms of financial cost.

Q53 Mr Leech: Changing the subject slightly, how responsible do you think London Underground are for the delays in the upgrade of the Jubilee Line in relation to their change in specification for the signalling system?

Mr Finch: You are asking me to go back into the distant past which I was not around for, so I really cannot apportion blame. What I would say is that I think it is vital that the two parties can work together effectively, because the important thing is that London gets its upgrade as soon as possible. I see much better working between London Underground and Tube Lines than was the case in the summer and I hope we continue to improve that trend so we can deliver the Jubilee Line as quickly as possible as well as the Northern Line as quickly as possible.

Q54 Mr Leech: What lessons have Tube Lines learned about the demise of Metronet and what are you doing differently to make sure that Tube Lines does not go the same way?

Mr Finch: Tube Lines has a different governance structure. Its shareholders are not its contractors. Everything is competitively tendered on a third party basis and clearly my responsibility as CEO to the company and to my customers on London Underground is to make sure that we deliver as efficiently and as effectively as possible. I believe that is the best way of ensuring that it will not go bust.

Q55 Mr Leech: After their demise though, did Tube Lines do anything differently to avoid the possibility of going down the same route?

Mr Finch: I believe Tube Lines started with a different operating model and that operating model has not changed.

Q56 Ms Smith: In the written evidence submitted there were references to the lessons to be learned by London Underground. Some of these relate to the initial contracting process, if you like, the structure of the PPP, the scope of the work to be carried out and so on and arguments over additional work required at a later date. A specific example given was work to improve mobility access at tube stations. Do you believe that there are lessons to be learned in terms of the contracting process for public-private partnerships as a result of that experience?

Mr Finch: As I said at the outset, I suppose my philosophy to some extent is that any contracting model can be made to work, provided you have effective and sensible and mature parties on both sides. I am sure there are lessons to be learned, but the most important lesson to be learned for me, for Tube Lines, is that if it fundamentally disagrees with
an approach that London Underground is taking it should raise that urgently with London Underground at the earliest convenience.

Q57 Ms Smith: I have been involved in PFI and local government and I have been through some of the traumas of the relationship at that level. It always appears to me that it is the quality of the initial written and legal agreements that does to some extent determine the nature of the partnership that follows.

Mr Finch: I suppose my counter would be if the contract is flawed both parties should sit in a room and sort it out.

Q58 Ms Smith: At the bottom line you often find with private contractors that, when the public sector provider wants to explore additional capacity or additional work through a contract, the private partner will always fall back on the legal agreement and is very unwilling to cooperate. You are saying that Tube Lines never took that stance?

Mr Finch: I am saying that if London Underground was not satisfied with some work that Tube Lines did, it could competitively tender. If there was variation work outwith the contract, you are quite right; the contract is set, but if there is variation work that London Underground wants over and above that contract then it is entitled to go and tender it as far as I understand it. Indeed, I see that in the case of ongoing works.

Q59 Ms Smith: You are saying in effect that there was nothing particularly wrong in the legal agreements and in fact it was at London Underground’s insistence that work be carried out within the contract that had not been specified?

Mr Finch: I would not represent for one moment that I think the contract is perfect. If we were starting again, maybe there would be aspects that would be changed, but fundamentally I suppose I take the pragmatic view that an agreement can be reached as to what will be the best way forward.

Q60 Chairman: You do seem to be blaming London Underground’s attitude for a lot of the problems in your written evidence. You give some pretty striking examples of that.

Mr Finch: I think there have been lessons learned along the way. Some of those examples are listed out there but what I really, fundamentally believe is that Tube Lines and London Underground have just got to sit down and resolve those things.

Q61 Chairman: One of the examples you give in your written evidence is that Tube Lines have difficulty gaining access to a car park and that the station manager only allowed you to have access if you agreed to put air conditioning and blinds in his office.

Mr Finch: I think there have been examples like that in the relationship between Tube Lines and London Underground over the years. I know of none at the moment. I believe that the organisations have moved on from that.

Q62 Ms Smith: The work on mobility is a much more significant example. The one about the air conditioning unit is frankly worrying on another level but the mobility work is quite serious. Are you saying that you would have preferred to have sat down with London Underground and negotiated an additional price to deliver that work? What you seem to imply in the document is that London Underground were insisting that they could deliver within the terms of the contract.

Mr Finch: Tube Lines and London Underground have got to agree on what the base scope is, because that is the price that Tube Lines has costed for and did cost for in its original price.

Q63 Ms Smith: Nobody is blaming you for that.

Mr Finch: What Tube Lines clearly has to do is to vigorously defend itself in that respect. I do not think Metronet did and I think that is one of the reasons why Metronet collapsed, but if London Underground want a variation they have a choice. They either can pay for it, choose to do it another way or not have it.

Q64 Ms Smith: They are saying that they wanted to have it and not pay for it?

Mr Finch: Yes.

Ms Smith: That is what I wanted to get out of you.

Q65 Chairman: Is that still the situation?

Mr Finch: I know of no examples of that.

Q66 Chairman: It has changed now, has it?

Mr Finch: Yes.

Q67 Chairman: What is the position now? That they are prepared to pay for what they want?

Mr Finch: I think there is a fair degree of respect between the two organisations certainly on a commercial basis in terms of understanding what the base scope is. That is vigorously discussed and that results in agreement.

Q68 Sir Peter Soulsby: You have argued that if the PPP’s objectives are to be met there need to be clear, accurate, transparent and relevant reporting procedures. You will have heard my earlier questions about the role of the PPP arbiter. How do you respond to the answers that we had earlier from London Underground and the Mayor on the role of the arbiter? Do you think that the arbiter has a role in ensuring that reporting procedures are as you describe them and as they ought to be?

Mr Finch: I fundamentally believe that the arbiter should have a strong role. We would be perfectly happy to see him have an extended role across both Tube Lines and across all Metronet companies.

Q69 Sir Peter Soulsby: Have you given any thought as to what would be necessary in order to strengthen that role?

Mr Finch: There is a range of different models and ultimately one could look at the rail regulator as a model.
Q70 Chairman: Why do you think that there is such a big variation on the estimates of the work that needs to be done in the next period, on what you think and what London Underground thinks?

Mr Finch: Rather than go into the detail of that, the arbiter is about to determine where he thinks the price should be on 17 December. I do not think it serves any of us to second guess that but from a taxpayer’s point of view his direction will probably drive exactly the kind of behaviour you would expect from a private sector company providing services to the public sector.

Q71 Chairman: Is London Underground more efficient than Metronet?

Mr Finch: I see no evidence of that.

Q72 Chairman: You see no evidence of that. You do not see any advantage in London Underground doing the work rather than Metronet?

Mr Finch: I can only compare Tube Lines’ costs with London Underground’s costs. The only data I have as a reference point are the data that the arbiter has compiled, which is 08/9 and 07/8. On that basis, Tube Lines is significantly cheaper than London Underground.

Q73 Graham Stringer: Are London Underground worse than Metronet?

Mr Finch: Again, I can only rely on the arbiter’s data and his evidence to you. His evidence to you is that costs went up between 07/8 and 08/9.

Q74 Graham Stringer: From your knowledge of the industry, you think they are less efficient than Metronet?

Mr Finch: Again, I am not in a position to judge because I do not have access to the data. I am relying on the arbiter’s data and I was not in the underground industry at that point in time to understand what changed between 07/8 and 08/9.

Q75 Ms Smith: London Travel Watch in their evidence to the Committee drew attention to the costs of consultancy fees and advisory fees generally for this kind of project. Can you give us a ballpark figure for the consultancy fees paid out by Tube Lines so far in connection with the overall management of your part of the Underground network?

Mr Finch: We virtually have no consultancy fees on an ongoing basis. We do that work ourselves.

Q76 Ms Smith: It is part of your overall cost, is it not?

Mr Finch: I believe there were substantial fees when the PPP was first set up, but those costs are sunk costs and they are not ongoing.

Q77 Ms Smith: Could you give us an indication of those initial fees, which is what I was talking about?

Mr Finch: I will happily supply you with those.

Q78 Ms Smith: Could you give us those on a written basis?

Mr Finch: Yes.

Chairman: Thank you very much.

Witnesses: Mr Steve Grant, District Organiser for London Underground, ASLEF. Mr Bob Crow, General Secretary, RMT (National Union of Rail Maritime and Transport Workers), and Mr Tim Bellenger, London Travel Watch, gave evidence.

Q79 Chairman: Good afternoon. Would you please identify yourselves for our records.

Mr Crow: Bob Crow, General Secretary of the RMT.

Mr Grant: Steve Grant, District Organiser, ASLEF.

Mr Bellenger: Tim Bellenger. I am Director, Research and Development, at London Travel Watch, the statutory consumer body representing the interests of customers in London.

Q80 Chairman: Thank you. Would you say that safety is being compromised by London Underground and Transport for London in an effort to reduce costs?

Mr Crow: If you look overall, the makeup of the industry leads to the same situation we had, basically, under Railtrack and before Network Rail brought the infrastructure companies back in-house. What you have is a multitude of contractors. Even though there is only one company now which is in the private sector doing work for the Jubilee, Northern and Piccadilly Line, there are a number of subcontractors and agencies that live off those contractors doing work. When you have basically more cooks in the kitchen than you need, then in our opinion it is going to lead to a different kind of layout for safety and certainly we believe that safety is being compromised. What you need to run the railways is a bit like a ship really: the captain is in charge and when he makes a decision it is filtered through straightaway to the shop floor. Under the old London Underground regime, the managing director would say change a light bulb at Rickmansworth Station and the person would change the light bulb. Now he has to ring a contractor up, who rings a subcontractor up, who rings an agency up, which then rings a handyman up out of the Yellow Pages to go and put in a light bulb.

Q81 Chairman: What has happened to safety levels on the network since we last looked at this in 2008? What is the record of what has happened?

Mr Crow: On staff being injured?

Q82 Chairman: Yes, staff or members of the public.

Mr Crow: I think it has been constant, to be honest with you. To be truthful, I could provide figures of recorded instances where they have taken place. What is quite clear is that when you have a number...
of processes in place—because what you have is one overall policy from London Underground who get their policies overall arching from Transport for London, and then you have policies for Tube Lines and then you have policies for all the stream of contractors who you have got out there as well—you have a number of catalogues, basically, for staff working for different employers, all doing the same job at the end of the day and supposed to be delivering a service for London Underground.

Q83 Chairman: Does any other panellist want to comment on safety levels for either passengers or people working in the system?

Mr Grant: Since the privatisation seven years ago, immediately after there were a number of derailments. My members, predominantly train operators, deal with the interface between wheel and rail and these contractors my colleague Mr Crow has talked about. Even as recently as a few weeks ago, with the Jubilee Line upgrades, the communications between the managers of London Underground and the managers of the contractors, subcontractors, et cetera, broke down to a point whereby, on a recent weekend where upgrade work was being done, there was no passenger service—again major disruption to customers—and there were lives being put at risk because of the breakdown in that communication. A lot of the issues arising that my union gets are dealing with those issues.

Q84 Chairman: Mr Bellenger, do you have any observations?

Mr Bellenger: We do not have any particular evidence that safety of passengers has declined since the introduction of the PPP, but then you have to realise that all sorts of other things are going along in parallel to the PPP which may mean that safety is staying constant or may in fact have reduced.

Q85 Chairman: What would you say about the passengers’ experience since PPP started? Has it become a better or a worse experience?

Mr Bellenger: In one sense the “Passenger has Paid the Price” for the PPP—as a different acronym. Passengers are certainly experiencing a better quality of service in some respects because the investment programme is going in—and that is something we have always argued for—but it is not necessarily easy to distinguish whether the PPP is responsible for that because there are other things that are being paid for as part of the investment programme which are outside of the PPP. That means that you cannot necessarily attribute wholly any improvement to the PPP or not. Certainly passengers are paying the price at the moment in terms of the additional costs that the PPP is currently experiencing. Because of that passengers are likely to have to pay lot more money in their fares in the New Year to bridge the gap between the amount of money that Transport for London needs to pay out on the PPP and the amount of money they have coming in, and they are also paying the price in terms of disruption to the network, particularly on the Jubilee Line, where the numbers of closures has got to some unacceptable levels. We certainly believe that there are other and better ways that such disruption could be planned and also communicated to customers.

Q86 Chairman: What are those better ways?

Mr Bellenger: To give you an example, one of my correspondents was a regular user of the East London Line. When the East London Line was proposed for a blockade, she complained about the blockade but she knew about it six months in advance and was able to plan her life around that blockade. She has again contacted me now that we have the extensive Jubilee Line closures—because she lives in that sort of Canada Water area and she uses the Jubilee Line at weekends. The thing is that she cannot plan her life properly now because she does not know whether or not the Jubilee Line is going to be available, whether she is going to have to use a replacement bus for all or part of her journey. Essentially she is more dissatisfied now, because she does not know what is going to come to happen on the weekend. At least when she had a blockade, she knew that for four years the East London Line was going to close and she could plan around it. We have urged in our evidence to you and to the London Assembly on their previous inquiry on this that Tube Lines and London Underground look at long-term blockades perhaps as quicker way of delivering the upgrade, so that at least passengers know, if they cannot travel between Kings Cross and Hyde Park Corner, that they cannot do that, but they have a set amount of time in which that work is going to be completed.

Q87 Mr Hollobone: Mr Crow, if we were to ask you how many people did it take to change a light bulb on an underground before and now, what would your answers be?

Mr Crow: One person, the same as it was before.

Q88 Mr Hollobone: But you were indicating that there are certain steps you have to go through now in order to do that.

Mr Crow: Absolutely. I do not suppose that the light bulb causes the big problems out there, but certainly changing high levels of track components and refurbishments of stations certainly do cause problems. With most of the companies now concerned the first thing they do is run to see what their contract says, more than what they used to, say, when the managing directors was making an instruction do it.

Q89 Mr Hollobone: In its evidence to this Committee the Department for Transport has justified the PPP programme by saying that the costs that have been incurred have been less than the costs incurred on the Jubilee Line extension or the Central Line upgrade. They quote figures saying that with regard to the Central Line upgrade cost overruns were up 30% and significantly behind schedule—six years in the case of the Central Line—whereas with Metronet, even though the costs were, as we have heard, in the
hundreds of millions, the costs were in the range of 4% to 10% against the total value of the investment.

**Mr Crow:** If Metronet did so well, how come they are not around any more? It must have been some good business if they went out of business. The reality is that the Metronet situation, when they talked about upgrades, was that they were concentrating on station modernisation. That is where they concentrated their efforts. I have to say station modernisation is fantastic, it is nice to sit on a station and look at it all day and say how nice and pretty a station looks, but the majority of passengers that I speak to every day when I travel on the tube want the train to come on time and they want to have a seat to sit on on the train.

Q90 **Mr Hollobone:** In this dispute between TFL and Tube Lines, where does the balance of responsibility lie in your view?

**Mr Crow:** It is quite clear that Tube Lines, for example, are the ones who have not carried out the work they said they had done and which they should not have said they had done. The reality is they are supposed to have finished all the upgrades by the end of this year, and now we are talking about upgrades to 2010 and in certain parts of the spring the Jubilee Line being shut down for perhaps three or four days. I am not a cynic but it is strange why the Chief Executive has left the company if it is doing so well.

Q91 **Mr Hollobone:** If you had to split the responsibility in percentage terms between the two—

**Mr Crow:** I am sorry?

Q92 **Mr Martlew:** The Chief Executive is behind you.

**Mr Crow:** I thought you were a heckler.

Q93 **Chairman:** Can we keep to the questions. **Mr Crow:** I am being distracted, I am sorry. **Chairman.**

Q94 **Mr Hollobone:** If you had to split the responsibility in percentage terms between Tube Lines and TFL, would it be 100% Tube Lines and nothing TFL or would there be a balance?

**Mr Crow:** The whole lot needs to go to TFL. It is one system. We want a joined up system. If you have Jubilee, Northern and Piccadilly Line, it sounds nice—it is three deep level tubes that they broke away for one contract, and then they split the other two contracts up, which was the sub-service lines, and then the other lines in three separate contracts, and Metronet got the two contracts put together—but they all have interfaces. The Jubilee, Northern Line and Piccadilly Line, everywhere you go along that route, will meet somewhere with the other contracts. The railways can only be run on the basis of being joined up. It is one operation. You cannot have a ship and then turn around and say that the engine room is being run by someone else and the navigator is being run by someone else and the people doing the food are someone else. It is all on board together. That is why the railways have to be joined up. They should be run democratically by Transport for London and the people who run Transport for London should have a clear, constant direction of line of running the system at the end of the day by the Chief Executive of Transport for London. He or she should be responsible for running that network.

Q95 **Mr Hollobone:** Do you think Tube Lines is going the same way as Metronet?

**Mr Crow:** Absolutely, and the quicker the better, to be honest with you. The sooner Tube Lines are back in London Underground and we all have one London Underground system together, then the passengers will have a better railway.

Q96 **Mr Hollobone:** How long do you give it?

**Mr Crow:** It is not for me to say. They have never shown us the contracts. That was left to all these whiz kids who said they had it all right, but it looks like they have got it all wrong.

Q97 **Mr Hollobone:** Do I take it Mr Finch is not on your Christmas card list?

**Mr Crow:** I have nothing against Mr Finch. He is a nice personable bloke, but obviously he has found his place better in National Express than he has with Tube Lines.

Q98 **Mr Martlew:** Obviously the Jubilee Line has a very advanced signalling system and it will increase the capacity. Has the agreement been reached between the Trade Unions and London Underground on the operation of this and has the work been done on the training of the staff? Has the decision been taken or not how the training is going to be done?

**Mr Grant:** We have major issues with London Underground on the training of staff. These trains will eventually be totally automatic, like Victoria, but with the upgraded system, as you say. The comparison was made earlier between Central Line. When I was a driver I went through all that. It was an off-the-peg system; it was not started from scratch as this system is. Obviously any new system will have its problems and we do have concerns over the length of training and the quality of training. London Underground has had some good training over the years in safety, which has kept down the numbers of incidents, lost time injuries, deaths and accidents amongst staff and customers. To answer your question, no, we are not happy with it and there is major disagreement.

Q99 **Mr Martlew:** We have had evidence from the Mayor and the Chief Executive that this was not a problem, that it had all been sorted out. That is not the case, is it?

**Mr Grant:** From my point of view, dealing with the train operators who are the trainers and the managers who are the trainers and the staff who are being trained specifically on the Jubilee Line, I could send this Committee a whole year’s worth of emails, complaints and concerns over the training quality and the content of that training.
Mr Martlew: This will be to London Underground.
Mr Grant: We work for London Underground, yes, sir.

Mr Martlew: When you do have the training on the line, does it mean that the line for some of the time will have to be closed to the public?

Mr Grant: Tube Lines in this particular case provide the trains and the signalling systems, and London Underground provide the shutdown, or blockade as my colleague here calls it. That training is then done for hands-on training by drivers, but we are arguing over the way that is being done. Just to slightly digress, on the comment about overruns, whether it is for weekends or for six months does not matter; the most annoying thing for the person concerned of Croydon, or whoever the person was, is when come Monday morning the Jubilee Line is not back up and running because of the overrun of the engineering work. That causes even more major disruption to hundreds of thousands of Londoners. It is my belief that it is easier for the companies to pay the fine of the overrun and get the work completed and of course the people of London are not compensated for that delay.

Mr Martlew: Mr Grant, you have been very helpful. Do you think that the training will be completed for the drivers in time for when Tube Lines say that the job will be completed?

Mr Grant: In my view, no, sir, because the argument is over the provision of the shutting of the line to enable drivers to be trained in the signalling system that they wish to run.

Mr Martlew: Basically you are going to have to close the line to train the drivers.

Mr Grant: Yes. In the majority respect of physically driving, yes.

Mr Leech: Is the performance of Tube Lines any better than Metronet from a passenger perspective?

Mr Crow: On what basis? Passenger demands?

Mr Leech: No, the whole passenger experience.

Mr Crow: The passenger does not see Tube Lines as such. If the passenger gets on the train in the morning or in the evening and there is a delay, it is London Underground that announces that there is a delay because of a signal failure here or because of a track defect there, but the average passenger just wants to make sure that there are no delays. Tube Lines do not make that announcement. I am not saying they should make that announcement, because London Underground is responsible for the operation of the railway, but London Underground have no say whatsoever over that signal failure or track component that goes wrong on the Jubilee, Northern and Piccadilly Line. It has on the Metropolitan Line. It now has the responsibility to say what is wrong. Richard Parry was here earlier on. If there is a problem now on all the lines except the Jubilee, Northern and Piccadilly Line, the Chief Executive can just turn around and say what has gone wrong. Now he has to ask his counterpart in Tube Lines, who has to go through the entire programme down to the bottom to find out what went wrong on that piece of track. I would say that people are feeling very, very annoyed. Especially at this time of year when people are Christmas shopping, the only day they probably have off is a Saturday or a Sunday and they are faced then with delays. Those people going to Wembley or to the O2: are faced with delays for the concerts and circuses and things they have on at weekends. It is causing massive disruption. You only have to be around the East End of London, around Stratford way, to see the absolute chaos that takes place with people trying to shop on a Saturday and Sunday now when there is engineering works.

Chairman: Mr Bellenger, is there anything you would like to add on this topic of the passengers’ experience?

Mr Bellenger: For a start, the lines are obviously different, and that has an effect on the ability to compare like for like.

Mr Leech: Are you not able to compare like for like when there are no works going on or when there are works going on and comparing different lines, so comparing one line which is run by Tube Lines where there is work going on and one line when there was work going on when Metronet were running that particular line? Have you done no work on that?

Mr Bellenger: We, as such, have not done any work on that, but I think the thing to note is that if you close one part of the system there will be an effect on other parts of the system which may be run by the other contractor; for example, if there is a closure on a Tube Lines part of the network, then it may well have a knock-on effect on something to do with that run under the old Metronet system. It may be quite difficult to parcel up the blame between the two.

Mr Leech: If there is more than one company running lines on the Underground it is very difficult to recognise whether or not one is doing a better job than another.

Mr Bellenger: No. Because they are different lines, there will be different specifications there depending on the type of services provided.

Mr Grant: To be fair to Tube Lines——the question is: “Is Tube Lines better than Metronet?”——there are two examples I could give you in the affirmative. The axle boxes on a Piccadilly Line train that kept going up in flames have been replaced. The 7th Car Project on the Jubilee Line has been delivered before target. There are two examples, but you would have to look at the progress of Metronet, a collapsed company, and the present Tube Lines trying to deliver the upgrade work and closures.

Mr Leech: If there is more than one company running different lines on the Underground, it is difficult to assess whether or not that company is
Mr Crow: The Arbiter at the end of the day is a person who, in my opinion on this PPP, has to decide if the contract is being carried out to the specification, as laid down and given to London Underground before the PPP came in? If you remember what happened was that the Mayor, who is now responsible—not the individual, but the Mayor who is now responsible—was handed the contracts and never had a chance to see them. That is what the specifications are on. Now, as the time evolves and we are into seven years, 14 years, 21 years, 28 years and 30 years, those contracts will start coming to an end and new specifications will go in there, so the Arbiter is going to have to decide if the laid down specification is being carried out correctly by the contractor concerned, and if he is not carrying out that contract then who pays for the lost time. Either Tube Lines is going to pay for it or Transport for London is going to pay for it. Really basically he is just the Arbiter who is sitting there and weighing up whether the contract is in favour of the one employer or Tube Lines who carry out the work for them. There is quite clearly a massive difference now in the amount of money that is owed between Tube Lines and TfL.

Mr Crow: Money-wise he has. There will be different kinds of specification regarding safety and one thing and another. Quite clearly the Arbiter has the power, and really the death knell for Metronet is when the Arbiter says that Metronet has to pay the money back. That is when they have to liquidate.

Mr Grant: You asked if they have a role in transparency. At the present time they are having a role in negotiating between the difference between London Underground and Tube Lines over the costs. Previously, in the last tranche, London Underground and Tube Lines and Metronet, as was, used to manage to resolve or work out their differences at many levels of strata of the business between them. Now, whether it is because there is more pressure from TfL on London Underground or whether it is the demise of Metronet—and I am not a lawyer or accountant or whatever—or whether London Underground has got more hardnosed about the contacts, Mr Finch gave evidence earlier that they are asking for variations to that contract and Tube Lines are trying to renegotiate those contracts. Yes, he does have a role at the moment. Whether that will continue, only time will tell. I am not a foreseer either, but I do believe he has a present role in trying to resolve differences. As Mr Crow said, the longer they take for someone to bang their heads together and deliver the services for the customers, as usual it will be them who keep paying.

Mr Bellenger: Yes, there is a role for the Arbiter. The Arbiter also takes account of the needs of passengers. In all the big arguments that surround the PPP, it is the passenger who is often forgotten. Certainly, yes, we want to see the Arbiter given more power if he can do that for the benefit of passengers.
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Q114 Sir Peter Soulsby: Mr Finch earlier suggested the model might be something like the Rail Regulator. Do you think that is what is needed in this context?
Mr Bellenger: That might be a way in which you could possibly look at that. The current PPP Arbiter was in fact the previous Rail Regulator, and I believe he developed the post in the same way that he did the Rail Regulator post, so I think there is some scope there, yes.

Q115 Chairman: You have all been very critical about the Public Private Partnerships. Is there anything positive you have to say about them? Has anything good been delivered? Do you welcome the investment that has come in?
Mr Crow: It is without doubt that money has gone into the industry. There is no doubt about that. You cannot hide the fact that there is new money in the industry. The trouble is that it has not gone into delivering better services; it has gone into those contractors that make up the consortium that runs Tube Lines and Metronet. Basically they were more concerned with station modernisation rather than more trains and better quality. We are now seeing a situation where, as I see it, there is a complete rundown now of Tube Lines.
Mr Grant: I would like to see someone like an Arbiter deciding that, after you and your colleagues in this House decide how much money is going to be given to railways, and leave them alone for a period of time because railways cannot exist on short-term needs. They need to plan the advance stock, they need to do maintenance. As I say, it is consistency that the railways require. The only good thing about the privatisation was the length of time the contracts were done: there was guaranteed money put in without interference, albeit there is pressure now on cutting costs, et cetera. But I have seen so many times in 35 years of working in the railway industry, this House promising something, like Crossrail, and a new government or another government or party getting in and changing that and not giving that consistency to the industry.
Mr Bellenger: The investment programme certainly has delivered an amount of benefits. I have to take issue with that about stations. Stations are vitally important, not only as the place where people travel to and get into the system but, also, because London is a world city, if we have stations which are run down and poorly maintained they give a very poor image of our city. Certainly the investment in stations has been welcome and long overdue and I certainly would not want to go back to a situation as happened tragically at Kings Cross, where so many people died simply because of poor systems and poor maintenance and all those other things that contributed to that tragedy.
Mr Crow: On that last point, I was not at all saying that stations should not be modernised to the same effect they should be. I am saying that the money that should be used should be used more on providing better train services than putting the new colour tiles up on stations. Regarding the fire at Kings Cross, it had nothing to do about the state of the station; it was the running down of the escalators and the non-cleaning of the escalators that caused that fire there. There is plenty of these stations that are turning into shopping malls now rather than stations. There is enough shopping cities around Britain for people to go shopping. Let us have railways as a railway system and let us have shops as shops.
Mr Grant: And those stations staffed too.

Q116 Chairman: Mr Crow, can you tell us if any progress has been made on averting a strike on the Underground?
Mr Crow: Pardon?
Q117 Chairman: Has any progress been made on averting a strike?
Mr Crow: Which strike is that?
Q118 Chairman: There is no strike.
Mr Crow: There are a number of issues but not with London Underground at the moment. There is a ballot going on with London Underground but there is no result back for that. There is a dispute with one of the subsidiaries, EDF, the French nationalised power company that now runs the power for London Underground, to extract a profit out to give back to its own station national company in France, which is an odd one to understand. We do have a dispute with them. We do have a dispute with Alstom, another company, which subcontracts work from Tube Lines on the maintenance of the trains on the Northern Line. There are two disputes there coming up, but we hope to resolve them very quickly.
Chairman: We are not in dispute with London Underground or Tube Lines.

Witnesses: Rt Hon Sadiq Khan MP, Minister of State for Transport, and Ms Bronwyn Hill, Director General, City and Regional Networks, Department for Transport, gave evidence.

Q119 Chairman: Good afternoon. Would you identify yourself for the record, please.
Mr Khan: My name is Sadiq Khan. I am Minister of State for Transport.
Ms Hill: Bronwyn Hill, Director General, City and Regional Networks.

Q120 Chairman: Minister, are you of the view that the PPPs are good value?

Mr Khan: If you look at the investment over the last 13 years and the progress we have made since PPP began a few years ago, people using the Tube in London have seen huge improvements. If I measure success by the quality of Tube travel that commuters in London receive, then I think the answer is yes.
We have had this evidence failings and I am the last person to say that PPP has generated by PPP, but I am not blind to some of the huge evidence of the fruits of the investment rolling stock that fail or the fewer breakdowns in the now using our tube system, whether it is the fewer whether it is the increased numbers of passengers may not like, whether it is the improvements in the stations, that some of the previous witnesses may or may not like, whether it is the improvements in the escalators, whether it is the increasing number of tube trains now running through our tunnels, whether it is the increased numbers of passengers now using our tube system, whether it is the fewer rolling stock that fail or the fewer breakdowns in the systems in London, whether it is the increased numbers of people coming into London. I have seen huge evidence of the fruits of the investment generated by PPP, but I am not blind to some of the failings and I am the last person to say that PPP has been a utopian perfection. I accept the failings.

Q122 Mr Martlew: We have had this evidence session today and we have a very high profile transport system in the London Underground, probably the most famous in the world. We put this partnership together between private sector and public sector and when things go wrong is it not going to be a great temptation for the politician in charge, the Mayor of London, to say, “It’s not my problem, it is somebody else to blame.” Is that not a fault with the system? With such a high profile Public Private Partnership, the Government should have known that they would have had this sort of problem when they were putting it through, especially as the then government wanted to privatise and just blinded to the concept of PPP and just want to support it in principle without looking at the consequences?

Mr Khan: The reason why I have said that PPP had been a success is the criteria I gave for defining that success. I am not an ideologue. To me it is not the type of finance that matters; what matters is that we get finance into London’s Underground system. I recognise the failings of the Metronet collapse, I recognise the amount of taxpayers’ money that has been lost, I recognise the NAO Report’s findings in relation to the poor corporate governance in Metronet and the lack of leadership, but I also see examples of some of the improvements that my constituents and Londoners have seen since the start of the PPP, whether it is the improvements in the stations, that some of the previous witnesses may or may not like, whether it is the improvements in the escalators, whether it is the increasing number of tube trains now running through our tunnels, whether it is the increased numbers of passengers now using our tube system, whether it is the fewer rolling stock that fail or the fewer breakdowns in the systems in London, whether it is the increased numbers of people coming into London. I have seen huge evidence of the fruits of the investment generated by PPP, but I am not blind to some of the failings and I am the last person to say that PPP has been a utopian perfection. I accept the failings.

Q123 Mr Martlew: Do we accept that that had to be done through the Public Private Partnership? We had not built any new schools in my constituency for 50 years and we are now building three, but that is not being done by PPP; it is because the Government have made more money available that is what they have done with the Underground.

Mr Khan: If you see some of the ways that the private sector has levered in the money, it has been borrowing from the financial lenders. Of course we have been paying contractors with the performance element of the PPP. We have seen a huge leverage of investment from the private sector as well.

Q124 Mr Leech: Mr Martlew asked the question I was going to ask, so I will ask a different one. Do you think that Tube Lines is going down the same route as Metronet?

Mr Khan: It is not for me to defend Tube Lines but the short answer is no. If you compare and contrast what the NAO, the PAC, the Transport Select Committee, the Arbiter have said about Metronet compared and contrasted to Tube Lines, it is comparing apples with pears.

Q125 Mr Leech: Do you think lessons have been learned from the failure of Metronet?

Mr Khan: I hope so. I can give you some examples to illustrate the point. Eric made the point that back in 1997 and onwards PPP was a new, innovative way of trying to lever in monies from the private sector to invest in a Tube system that had been underinvested in for decades. There was some nervousness about the private sector lending monies in, so the security we gave to the commercial lenders may have been overgenerous. One of the lessons learned is to make sure that when the Treasury now gives advice to departments on PFI projects, there are now standardised contracts. We have changed the way we pay contractors. You see the M25 widening project, the A1 major upgrade projects on a different system, so the same sort of losses that were incurred in Metronet hopefully could not occur. You will have heard from the previous witnesses examples of how there will be greater transparency and information being passed between ex-Metronet and TfL, the Mayor, and the Secretary of State than was previously the case, so I hope lessons have been learned.

Q126 Mr Leech: If Tube Lines were to fail—and it sounds as though some people want them to fail—would the Government take a different view on the relative success of PPP?
Mr Khan: I am always ready to accept that PPP has its failings. It is not a perfect system but if you look back to where we were in 1997, 1998, 1999, the GLA Act of 1999 onwards, I can see no evidence of a better form of investing the sums of money that we decided to invest since the start of the PPP.

Q127 Mr Hollobone: Minister, you said you were not an ideologue when it comes to PPP. In the evidence to this Committee from Transport for London they say “Metronet’s failure was largely the result of its own inefficiency rather than a consequence of the PPP structure. However the legacy of Metronet’s collapse has inevitably raised questions about whether an alternative model may offer greater efficiency and value for money. As the one remaining PPP contractor, it is on Tube Lines’ shoulders that the case for the PPP model now rests.” What is your response to that assessment?

Mr Khan: There is a delicious irony in the current Mayor Boris Johnson wanting to nationalise the Tube. As far as the ideologue point is concerned, I make the point that if you look at the NAO Report, a comprehensive report into Metronet’s collapse, they did not point to PPP as the reason for Metronet collapsing and for the losses; they pointed towards poor corporate governance and they pointed towards poor leadership. It was open to them to point the finger at PPP. I have accepted and I recognise that PPP are not perfect, but I do say that if you go back into time there was no other way of investing the sorts of money we invested in London Underground. Accepting John’s point that we do not know what is around the corner with Tube Lines, putting aside the Jubilee Line upgrade issues there are currently, if you look at the last period, on all the objective criteria Tube Lines have performed remarkably well. On the Northern Line I see for myself, as an MP who has three stations along the Northern Line, the improvements on the tracks, in the station, in the numbers of CCTV cameras, in the numbers of help points, and the quality of the trains. Or on the Piccadilly Line and on some of the improvements on the Jubilee Line there have been huge improvements. Some of the transparency Tube Lines have performed extraordinarily well. On the 11 lines are run from the ex-Metronet by LU. The panel was because that was the immediacy, that we could straightaway get more information and that is one of the ways in which we are going through now for period 2 and, if necessary, they have the opportunity to call for an extraordinary review as well. My understanding—and my officials receive regular updates from Tube Lines—is that they do not feel that they need to, as a department, not just to TIL but also to the Arbiter lots of information, and that is one of the ways in which the Arbiter is able to benchmark the performance of Tube Lines versus the performance of ex-Metronet as well. One of the reasons why, for example, when it came to learning the lessons from the collapse of Metronet, we have ensured that the new independent panel is transparent and open in relation to how 8 of the 11 lines are run from the ex-Metronet by LU. You will hopefully have heard from both the Mayor of London and Richard Parry—and I know you are hearing from the Arbiter in January—about how we have learned the lessons to help ex-Metronet to have greater transparency and to make sure there is a passing of information between us, TIL and ex-Metronet.

Q129 Mr Hollobone: If you are not prepared to put your office on amber alert for a potential collapse of Tube Lines, one mechanism which you could introduce, which has been recommended by both this Committee and the National Audit Office and which you have prayed in aid on several occasions in this session already, is that the PPP Arbiter be given powers to initiate a review on his own terms rather than after a reference from one of the interested parties. Is that something that you would consider?

Mr Khan: That is a good question. When Chris Bolt has been asked the question, “Do you think you have enough powers and what sort of powers do you think you could have?” one of the things he has raised, which is interesting, is the issue of having powers himself to go in and look at what has happened rather than being asked to do so. As you know, with Tube Lines there is the periodic review which we are going through now for period 2 and, if necessary, they have the opportunity to call for an extraordinary review as well. My understanding—and my officials receive regular updates from Tube Lines—is that they do not feel that they need to do so. As a department, not just to TIL but also to the Arbiter lots of information, and that is one of the ways in which the Arbiter is able to benchmark the performance of Tube Lines versus the performance of ex-Metronet as well. One of the reasons why, for example, when it came to learning the lessons from the collapse of Metronet, we have ensured that the new independent panel is transparent and open in relation to how 8 of the 11 lines are run from the ex-Metronet by LU. You will hopefully have heard from both the Mayor of London and Richard Parry—and I know you are hearing from the Arbiter in January—about how we have learned the lessons to help ex-Metronet to have greater transparency and to make sure there is a passing of information between us, TIL and ex-Metronet.
the same with Metronet. I am confident that the corporate governance in Tube Lines and the leadership is not the same as with Metronet. I am confident that the regime set up with the Mayor, elected by Londoners, to have independent scrutiny will lead to greater transparency and more information being passed to us, to give us the reassurance that you rightly say we need to have.

Q130 Graham Stringer: You say there have been problems with PPP but it is still the better structure or the best structure. Do you regret giving 95% guarantee for losses to Metronet?

Mr Khan: One of the questions that I ask myself is: Did the fact that the financial lenders had that big guarantee mean they were more lax than they otherwise would have been in relation to the monies they lent? What reassures me in the fact that if you look at the amount of shareholders monies lost: £200 million of loans and a further £340 million of equity and contractual penalties so about £540 million in total and the banks had 5% at risk—it is still a huge sum of money. Yes, on the one hand maybe only 5% that was the reason why they were more lax than they otherwise should have been, but I go back to the point where back in the late 1990s or the early part of the 2000, there was not a queue of people queuing up to lend monies to what was an innovative way to fund a Tube system that had been underfunded for literally decades.

Q131 Graham Stringer: I accept the last part; I do not really accept the figures you have just said, not that they are not true in themselves but if you look more deeply at them there was basically a corrupt relationship between Metronet and the supply companies because they were paying themselves. While the headline losses to Metronet may be, whatever you say, £300 million or £350 million, they had trousered that money themselves, had they not? They had circulated the money to themselves in very inefficient contracts, so in actual fact their incentive was just to funnel the money through to the supply companies/themselves and the losses or the liquidation of Metronet therefore meant less to them. The controls that we look at, the bank said, “Well 5% we can stand that, we are being paid,” and the companies themselves took very little risk because they were paying themselves loads of money, and at the back of that is the taxpayer or the government paying 95%. That cannot have been a sensible contract.

Mr Khan: The Treasury now does not give those sorts of guarantees—one of the lessons that has been learned. Second, if you look at Tube Lines they have similar guarantees of 95%, and you will see shareholders and leadership which is very different from Metronet. Third, the advice back then was that the only way you were going to get financial lenders to lend the sort of monies that we needed to invest in a system that had had underinvestment for decades, would be to borrow from the private sector and you would need guarantees to do so, the comfort letters that we gave to LU, because LU themselves had none of the funding. Last, do not forget, notwithstanding the point that you made—if one penny of taxpayers’ money is lost it is one penny too much and I take your point very seriously—you still see over the last period more than £4 billion worth of investment in those lines run by Metronet and ex-Metronet. One point is this: do not forget that having tied supply chains is not unique to this contract. We had tied supply chains in relation to the high speed rail, the new Channel Tunnel Link, in relation to the widening of the M25 and the A1 upgrade and others as well.

Q132 Graham Stringer: What you seem to be saying is Tube Lines so far have behaved well, but the contracts were open to abuse and there was nothing in the system that stopped it. While you are defending PPP, it was open to abuse. That does not mean to say that Tube Lines or anybody else involved would abuse it. Clearly Metronet did. Does it concern you that those people in the supply chain, that is the original shareholders of Metronet, are still effectively getting public money because they are still working on the Underground?

Mr Khan: You mean those below the—

Graham Stringer: The people doing the work.

Q133 Chairman: When the Select Committee looked at this previously, these were the points that we drew out of what had happened and we expressed our very great concern about the way that the PPP had been constructed in this relationship particularly, on this supply chain.

Mr Khan: You mean why they haven’t been blackballed. Is that the point you are making?

Q134 Graham Stringer: Yes, precisely.

Mr Khan: First, I am not sure if I accept they were corrupt. You have made that point quite forcefully, but I am not sure about that.

Q135 Graham Stringer: I think that if something has a cold nose, a furry coat and wags its tail, it is a dog. If that money is going through the system and people walk away with the money, I think it is corrupt.

Mr Khan: I think having a 95% guarantee may lead to people being less careful about how their money is being invested and not having the right checks and balances as they should do. That is one of the reasons why we changed the guarantees we give in these sorts of arrangements. I accept that point. It is one of the lessons we have learned. I go back to the point that, back when these contracts began, the advice I have is that these were the terms that were required to give comfort to those lending monies.

Graham Stringer: I do not want to turn this into a sort of discussion of history, but it is not completely true that there were not warnings right the way through the setting up of PPP. There were dangers, were there not? This Committee in 2000 asked very unusually for the National Audit Office to get involved and look at PPPs before they were let. The National Audit Office drew attention to the fact of the models being used were suspect and there was a lot of uncertainty in the system, yet the Government ploughed on and went through it.
Chairman: A division has been called. It will be ten minutes if there is one vote, and if there are more we will be back as soon as possible.

The Committee suspended from 4.39 pm to 5.14 pm for divisions in the House.

Chairman: Mr Stringer.

Q136 Graham Stringer: I was trying to say that on warnings from the National Audit Office the Government changed its position a number of times on PPPs, saying there would be no cost to the public purse at the start of it to various different models where there clearly was going to be a charge. When it was implemented, the risk was not transferred and there were problems with Metronet and we now are facing problems with Tube Lines. You say you are not ideological, but it seems to me that there must be a better way of either a public sector way or of really transferring the risk. Why is the Government so wedded to saying it still supports the PPP process?

Mr Khan: If you look at other projects which have needed major investment, we have moved away from a PPP type model. As far as the Tubes are concerned, Tube Lines are in 30 year PPP contract, albeit with four different phases, so what you are talking about are the other 10 or 13 lines that are currently ex-Metronet. Proof that we are not ideologues is the fact that the other ex-Metronet are currently ex-Metronet. Proof that we are not ideological is that we have moved away from that and we will move for a model closer to the management systems used for TfL or other projects that have worked well.

Q137 Chairman: Is your justification of the PPP in the evidence we have from you something defensive about a decision that was taken some time ago without recognising a better way of moving forward?

Mr Khan: There are two issues there. One is how is Tube investment funded and the second is general ways of funding government/private projects. I am not suggesting that PPP is an ideal model for the latter. I am suggesting that we are now in train (if you will forgive the pun), approaching year eight of a 30-year contract with Tube Lines, and so, unless you are suggesting that we terminate Tube Lines, I am not sure what else we can do vis-à-vis the London Underground.

Q138 Chairman: What assurances have you sought from Tube Lines in relation to its work 2010-2017 on the Northern and Piccadilly Lines?

Mr Khan: The good news is that we are currently going through the periodic review for period 1 to period 2, and one of the things that the Arbiter is looking at is all sorts of issues in relation to costs of period 1, costs of period 2, safeguards and levers. One of the things that we have with Tube Lines, which we did not have with Metronet, is information systems, risk management systems, management controls, meaning that information is passed on to the Arbiter who can make the call. I have seen no evidence of the sort of financial crisis or corporate governance problems or other problems that there were in Metronet. The alternative is a case where Tube Lines are bending over backwards to provide information to the Arbiter, TIL, the Mayor and the Department for Transport as well.

Q139 Sir Peter Soulsby: In your earlier answer to Philip Hollobone, you were quite positive about the prospect of an increased role for the Arbiter. As I understand it, you have had, it is not so much Tube Lines that are being resistant to that; it is London Underground and the Mayor, it seems to me, who are resistant to that. As I understand it, it has been left to them to discuss it together. In your earlier responses you said that ultimately it was subject to legislation, but clearly you cannot force it upon them. On the other hand, as it seems unlikely that they are going to agree, and it is also unlikely that we are going to get legislation, are you and the department prepared to put a considerable amount of pressure on them to try to get an improved role for the Arbiter?

Mr Khan: One of the most important and pressing issues of the last period has been what sort of relationship does government have in relation to making sure there is value for money, bearing in mind that ex-Metronet has now been taken over by LU/Mayor/TFL. There is taxpayers’ monies involved as well as obviously London taxpayers’ monies involved. It is balancing the fact that on the one hand we believe in devolution and making sure that the London council have the governance to run the service, but in mind that leadership that we envisaged in the 1999 Act, but also bearing in mind there has been a huge financial loss by the collapse of Metronet. The pragmatic solution is the independent scrutiny panel, whereby not only do we look at the financial investment arrangements of London Underground but also across the rest of TIL, estate, which includes buses and trams. There are currently discussions taking place between us and the Mayor on terms of reference for the independent panel, what sort of people would be on the panel to ensure it does not become co-opted into part of the Mayor’s fiefdom and to have issues of conflict, which is one of the lessons that we have hopefully been trying to improve upon in relation to transparency of information. The point I was making is that I accept the criticism that we need to make sure there is transparency in terms of how general taxpayers’ money is spent. If it is the case that the independent
scrutiny panel does not work and we are not satisfied, then legislation is an option we will have to explore.

Q140 Sir Peter Soulsby: It struck me from the evidence that we had from the Mayor that it was him and Transport for London (influenced by his attitude) who were resistant to interference in their thinking, and that in fact the response we had from Mr Finch was much more positive and it saw the prospect of some order being brought into the relationship if there were a stronger role for an external Arbiter.

Mr Khan: Your analysis is one I would not disagree with. In fact the experience I have had, and I have been in this job since June, is that Tube Lines are having to passing information on. If the discussion is as to whether we have an annual report from the Arbiter, in fact Tube Lines give much more information than in end of year reports. There is an irony that Tube Lines are more than happy for an Arbiter to have more say, because they would say, “We are giving more information now to the Arbiter, to Department for Transport, to TfL than would be required under the legislation.” But I go back to a point I made previously, the one point where I am an ideologue is devolution, having a Mayor of London, even though he or she may be from a different party, having the tools at his or her disposal to run London—with the caveat, bearing in mind that there is general taxpayers’ money, your constituents’ taxpayers’ money and monies from others from outside London being spent, that we need to make sure that there are sufficient safeguards and levers to make sure we are confident that the money is being spent properly. So far I am reassured by the arrangements we have. But if there is a stage where I am not happy, we are not persuaded and we think it is not working, we have to have the option of legislation.

Q141 Chairman: Are you satisfied with the position of the Government or the department in relation to getting access to the information you need?

Mr Khan: From Tube Lines or from ex-Metronet?

Q142 Chairman: From any source, because one of the difficulties with Metronet is that the department lacked access to information at the right time.

Mr Khan: That is a good question. One of the problems with Metronet when it was Metronet was that they themselves were not on top of information, let alone us or TfL. As far as Tube Lines and ex-Metronet are concerned, I am confident we are given the information that we need—in fact, we are given information we have not asked for, which is a good sign. My officials are in regular contact with TfL and Lord Adonis and myself work closely with the Mayor of London, as you would expect us to, bearing in mind the huge sums of money and huge reasons why London Transport needs to work effectively.

Q143 Graham Stringer: Is it possible to say in the period of this Labour Government how much central government money and how much local taxpayers’ money as opposed to fare box money has gone into capital investment in the Tube?

Mr Khan: That answer can be provided.

Q144 Chairman: Could you let the Committee have that information.

Mr Khan: Yes. That will include, in answer to a previous question, where private money has gone. I am happy to provide the Committee with that.

Graham Stringer: That would be very helpful.

Chairman: Thank you very much, Minister.
Wednesday 6 January 2010

Members present:
Mrs Louise Ellman, in the Chair
Mr Eric Martlew
Graham Stringer
Mr David Wilshire

Witness: Mr Chris Bolt CB, PPP Arbiter, gave evidence.

Chairman: Good afternoon and welcome to the Committee. Do members have any interests to declare?
Mr Martlew: Member of GMB and Unite trade unions.
Graham Stringer: Member of Unite.

Q145 Chairman: Louise Ellman, member of Unite. Would our witness identify himself please for our records?
Mr Bolt: I am Chris Bolt, the PPP Arbiter.

Q146 Chairman: I think we would all like to congratulate you, Mr Bolt, on your New Year’s honour.
Mr Bolt: Thank you very much.

Q147 Chairman: When you spoke to us in the past about the London Underground PPP you said that you thought the PPP was essentially sound? Do you still hold that view?
Mr Bolt: I think it is really what is underlying that question. Do I think that private sector involvement in delivering the renewal and upgrade of the Tube is capable of delivering more efficiently than the public sector? Yes, I remain of that view. I think some of the more recent benchmarking information, some of which is reflected in the draft direction I published before Christmas, continues to reflect that. Do I think the PPP as a contract is sound? No, I think it has lots of deficiencies.

Q148 Chairman: Deficiencies that could have been anticipated?
Mr Bolt: I think some of them yes. It is quite a complex legal document and one of the problems I have experienced is actually trying to make sense of provisions which in some cases are unclear; in other cases are actually mutually contradictory. If I took one example of the problems which are reflected in the draft directions I issued before Christmas, we have two parallel regimes within the PPP contract: a process of periodic and extraordinary review, where the Arbiter determines the appropriate costs and revenue payments through the contract, and separately a contractual claims mechanism. If those contractual claims were dealing with small matters that would not be a problem but, as is currently the case where there is over half a billion pounds worth of outstanding claims against London Underground, that creates difficulties in putting those two regimes together. That would be one example where I think really from the beginning that issue ought to have been identified and dealt with more effectively.

Q149 Chairman: Metronet failed spectacularly at great cost to the taxpayer. Do you think the lessons have been learned?
Mr Bolt: Some of them, yes. Clearly, one of the big issues with Metronet was the corporate governance structure, the relationship between the five shareholders as shareholders and as contractors. Clearly Tube Lines has a different structure to that one. For example, they have always competitively tendered the major contracts. Have all the lessons in terms of monitoring and fully assessing value for money as you go along been learned? Possibly not. I think there are still some outstanding questions: for example, picking up recommendations that this Committee has made in the past about the visibility of performance information and independent assessment of that information.

Q150 Chairman: And how do you think that could be improved?
Mr Bolt: On that specific issue for example it is accepted by London Underground that the Arbiter has access to information for the BCV and SSL lines to use as a benchmark for Tube Lines. In practice, in the work I have done, those have not been useful benchmarks because international benchmarks suggest that rather different levels of cost are achievable. I have no ability to go in to look at the BCV and SSL costs and do the equivalent of the periodic review and say London Underground itself could be delivering more efficiently. That could happen if they asked me to do it because I have the powers to go in and carry out that sort of investigation.

Q151 Chairman: One of Metronet’s major failings was its tied supply chain. Do you feel that Tube Lines is replicating that problem with its secondments from its parent companies?
Mr Bolt: As a general point I think no. As I said, Tube Lines has generally gone through competitive tender for its major contracts. I think there is an issue, and maybe this is part of the experience with the Jubilee Line, that a signalling project is actually an IT software project rather than a civil engineering one. I think there are questions about whether reliance on the Bechtel secondment arrangements in that case has enabled Tube Lines to manage that project as effectively as it might have done.
Chairman: The Mayor of London told us that the PPP was not delivering value for money. Do you agree with that judgment?

Mr Bolt: I think, to be honest, in the way the point was put, no, because if the comparison is delivery by London Underground there is certainly no evidence that I have seen that London Underground is delivering through the BCV and SSL more cost effectively than Tube Lines is. In fact to the extent there is evidence it is rather to the contrary.

Chairman: There really is a major difference between Transport for London and Tube Lines in their cost estimates for the period 2010-17. Have you got any proper explanation for why that is? Looking at the list we have let me just take one example—depots—Tube Lines’ submission, £46 million, London Underground’s, £17 million and the Arbiter’s assessment, nil. How can it be nil?

Mr Bolt: I think if you take an item like that, the reason my number is nil is because the equivalent costs are in other lines in the table, so it is probably more helpful to take numbers at the more aggregate level for say the line upgrades or for rolling stock to make sure they are fully comparable. In very headline terms the reason Tube Line’s costs are higher than the ones I have considered appropriate fall into two broad headings. One is unit costs. I believe they can deliver at significantly lower unit costs than they were projecting for the second review period. As I said, I have used international benchmarking information and other things to reach that conclusion. The other is on line upgrades particularly they are starting from the actual position where the Jubilee Line is delayed and therefore a lot of the work on the Northern Line falls into the second review period. My assessment is that the notional infraco, which is the standard I have to use for pricing, would have delivered or could have delivered the Jubilee Line on time and that as a consequence about three-quarters of the work on the Northern Line would be completed in the first review period. That is shifting costs from the second review period into the first period.

Chairman: Given the very wide difference in cost do you think it is inevitable that the proposed upgrades to the Piccadilly Line and the station upgrades are actually going to be cut back?

Mr Bolt: I think that is entirely a question for London Underground, TFL and the Mayor. What I have said is that my assessment of the costs that will fall into the second review period is higher than London Underground’s figure and that creates an affordability question. It is for LU and TFL to decide whether it can meet that difference elsewhere within the TFL budget or not and if it cannot then, yes, it will have to look at the requirements to be funded in the second review period. I have asked them precisely that question: can they afford this figure and, if not, will they tell me how they propose to modify the requirements?

Chairman: What would your best guess be? Are we going to have a reduction in upgrades?

Mr Bolt: The public expenditure environment clearly is extremely challenging. Given that the difference on my numbers is over £400 million and if they then have to meet the costs of some of the claims of Tube Lines on top of that, there is clearly a very challenging position for London Underground and TFL. As I say, it is for them to decide whether they can find those resources elsewhere within their budget or whether they want to scale back the requirements for the second review period.

Mr Bolt: The PPP was not delivering value for money. Do you agree with that judgment?

Mr Bolt: I think what I was trying to say is I see no evidence that says the public sector is delivering more cheaply and such evidence as there is points to Tube Lines being more efficient.

Graham Stringer: If I can take you back to one of your answers to the Chairman, you said that so far as you could tell Transport for London was less efficient than Tube Lines. Do you have complete access to all the information from both TFL and Tube Lines to be able to make that assessment objectively and can you tell us how you have done it?

Mr Bolt: I think the reason we can spell out this is because of the contract for the second review period. This involves a joint benchmarking exercise which takes costs or different aspects of performance reflecting the sorts of asset breakdowns that are in my report and compares the unit cost of maintaining a kilometre of track between each individual line as well as for the infracos. That has been done for five years now so there is five years’ worth of data and the most recent joint benchmarking exercise showed increases in unit costs within BCV and SSL for track extensions particularly, some of which reflects extra work being done but none of which shows the costs below the Tube Line level. So that is looking at the past. Looking for the future, it goes back to the answer I gave the Chairman, what I would like to be able to do is to understand properly the basis on which the BCV and SSL projections for the next seven and a half years have been produced to see whether the same efficiency drive is reflected in those numbers that is clearly reflected in my 4.4 billion number for Tube Lines.

Chairman: You say “challenging”. May we interpret that as a big question mark?

Mr Bolt: There is a clear question mark. Although there are questions about how that gap should be financed, should it be through higher infrastructure service charges paid by LU or by Tube Lines borrowing, even if it was Tube Lines’ borrowing, that is LU using the private sector credit card, it will have to be paid back, so over the life of the contracts there is clearly an affordability question.

Graham Stringer: Can you spell out for us how you do this?

Mr Bolt: Essentially there are two broad elements to this. One is to look at costs as they are actually incurred. There is a joint benchmarking exercise which takes costs or different aspects of performance reflecting the sorts of asset breakdowns that are in my report and compares the unit cost of maintaining a kilometre of track between each individual line as well as for the infracos. That has been done for five years now so there is five years’ worth of data and the most recent joint benchmarking exercise showed increases in unit costs within BCV and SSL for track extensions particularly, some of which reflects extra work being done but none of which shows the costs below the Tube Line level. So that is looking at the past. Looking for the future, it goes back to the answer I gave the Chairman, what I would like to be able to do is to understand properly the basis on which the BCV and SSL projections for the next seven and a half years have been produced to see whether the same efficiency drive is reflected in those numbers that is clearly reflected in my 4.4 billion number for Tube Lines.

Graham Stringer: Have you had meetings with the Secretary of State or other Transport ministers and asked for more powers?

Mr Bolt: I have had discussions with officials in the Department. I think, as the Committee will be aware from the responses from the Minister when you saw
him before Christmas, there is a clear recognition that giving the Arbiter more powers would be one way forward but without LU in a sense embracing that voluntarily it would require legislation. The view they have taken—and it is clearly a matter for ministers—is that legislation is not something they want to pursue at the moment.

Q160 Graham Stringer: That is a very helpful answer.
Mr Bolt: Is the DfT clear that I think it would be useful for me to be doing that work? Yes.

Q161 Graham Stringer: That is a very helpful answer but have you had meetings with ministers?
Mr Bolt: I have not discussed that matter directly with ministers.

Q162 Graham Stringer: That is rather surprising, is it not, because this is a huge wodge of public money that appears to be going pear-shaped. I would expect you to have been inside Andrew Adonis’s office on a number of occasions. Is this any particular reason you have not been there?
Mr Bolt: I think the honest reason is that I have had very constructive discussions with officials and I know that they have been reporting my views to ministers. I think the basis of their decision reflected, as I say, the view that legislation would not be appropriate at the current time and the point the Minister was making when he appeared before you about local accountability, I am sure ministers are well aware of my position on that matter.

Q163 Graham Stringer: The Mayor of London said he was not—and I have not got his quote in front of me—prepared yet to read the last rites over Tube Lines. Do you think Tube Lines is going to go to the wall?
Mr Bolt: It is a personal view; no. Certainly if the Chief Executive was quoted accurately what he was reported as saying in the Guardian yesterday, they made a strong point that what was affecting their performance quite severely was access at weekends in particular but at other times in the Tube. They were given very small periods in which to get the equipment down to do the work. Firstly, do you think that is fair comment and, secondly, is that not a fundamental failure in the system? Dan Milmo’s argument in the Guardian was there may well be a political incentive with the Mayor of London to prove that the PPP does not work and he can do it by stealth, if you like, by not allowing them access. Do you think that is a fair comment? Do you think that is going on?
Mr Bolt: It is not something that I have been asked to look at. It is one of the reasons Tube Lines has a claim against London Underground on the signalling upgrades of over £300 million to include what they regard as additional costs resulting from London Underground’s behaviour. That is going through adjudication and goes back to the point I was making earlier about the claims mechanism, and the adjudicator is due to reach a decision on that by early February. What I am saying in my report is, based on the concept of a notional infraco that Tube Lines could have managed the delivery of the Jubilee Line in a way which delivered it on time and within the original contracted amounts of access if it had gone about it in a different way. With hindsight, the approach that London Underground has adopted or, to be honest, it was the approach Metronet originally developed for the Victoria Line, which was to develop the new signalling as an overlay system so you could run trains with the new signalling system at the same time as other trains on the existing system reduces the requirement for access, compared with the approach that Tube Lines adopted where everything has to be switched over to the new system and switched back again at the end of a weekend’s testing.

Q164 Graham Stringer: Are you going to charge Tube Lines? Are there going to be any financial penalties or any fines on Tube Lines for under-performance?
Mr Bolt: Under the terms of the contract if they do not deliver the performance matrix for availability, ambience and capability then, under the performance regime, payments from London Underground are abated to reflect that under-performance. They clearly are being abated at the moment for late delivery of the Jubilee Line. Those are matters set out in the contract not things that I oversee.

Q165 Graham Stringer: Not that you control. So in effect they are going to be fined?
Mr Bolt: Yes.

Q166 Graham Stringer: I do not want to put words in your mouth but that is almost bound to make them less viable, is it not, and closer to going to the wall?
Mr Bolt: If you are paying financial penalties of that sort on top of the extra costs which they have incurred in delivering the Jubilee Line, yes, clearly those are both costs which the shareholders will have to bear. Does it threaten their viability? That is a matter for the company but that is not the indication they have given so far.

Q167 Graham Stringer: Just a last point, when Tube Lines were here, and it was in Dan Milmo’s article in the Guardian yesterday, they made a strong point that what was affecting their performance quite severely was access at weekends in particular but at other times in the Tube. They were given very small periods in which to get the equipment down to do the work. Firstly, do you think that is fair comment and, secondly, is that not a fundamental failure in the system? Dan Milmo’s argument in the Guardian was there may well be a political incentive with the Mayor of London to prove that the PPP does not work and he can do it by stealth, if you like, by not allowing them access. Do you think that is a fair comment? Do you think that is going on?
Mr Bolt: It is not something that I have been asked to look at. It is one of the reasons Tube Lines has a claim against London Underground on the signalling upgrades of over £300 million to include what they regard as additional costs resulting from London Underground’s behaviour. That is going through adjudication and goes back to the point I was making earlier about the claims mechanism, and the adjudicator is due to reach a decision on that by early February. What I am saying in my report is, based on the concept of a notional infraco that Tube Lines could have managed the delivery of the Jubilee Line in a way which delivered it on time and within the original contracted amounts of access if it had gone about it in a different way. With hindsight, the approach that London Underground has adopted or, to be honest, it was the approach Metronet originally developed for the Victoria Line, which was to develop the new signalling as an overlay system so you could run trains with the new signalling system at the same time as other trains on the existing system reduces the requirement for access, compared with the approach that Tube Lines adopted where everything has to be switched over to the new system and switched back again at the end of a weekend’s testing.

Q168 Graham Stringer: That is a really interesting point but I would repeat the question which is I know you have not been asked to do that but you have made general comments about the structure of the PPP work. Do you think the Mayor/TfL’s control over access is a fundamental flaw in the system?
Mr Bolt: I understand for obvious reasons why London Underground needs to have the final say on that because you cannot have all the lines on the Underground shut at the same time and LU clearly want to avoid clashes with things on at Wembley or O2. That is why there is a process set out in the contract for the infraco to give notice to London Underground and that is the sort of thing where I think the contractual claims mechanism is perfectly sensible if those mechanisms are not working. When the cost consequences of that behaviour have got to the sorts of levels which are in the contractual claims, it makes a nonsense of the whole thing. I genuinely do not know and cannot say whether LU has been exercising that process sensibly but I think it is a fundamentally sensible process to have an access allowance, which is what is there, and for a requirement for the infraco to bid for specific closures on a basis which LU has to approve but should not refuse unreasonably.

Q169 Chairman: How would you describe the relationship between Tube Lines and London Underground?

Mr Bolt: I think it has been at times extremely difficult. Again one of the points which Tube Lines has expressed concern about is that they think that I have done my work on the basis of what they call the notional client—the perfectly behaving London Underground. I have not done that. I have recognised that both the contract itself and the approach that London Underground has adopted do cause some additional cost and some delay. One of the reasons for example I have a much bigger risk provision in my numbers than either Tube Lines or London Underground is to reflect that, but I have not priced in the specific things that are the subject of the claims.

Q170 Mr Wilshire: I want to go back to the point Mr Stringer raised but get there via a general question first, if I may. Do you consider that it in the interests of passengers and the taxpayer that Tube Lines survives or is it in their interests that it finishes?

Mr Bolt: My view very clearly is that it is in the interests of taxpayers and users of the Tube that Tube Lines survives or is it in their interests that it finishes?

Mr Bolt: It is absolutely clear that the financial markets, the lenders and investors in Tube Lines are concerned about the long-term viability of the company. I have had people like the European Investment Bank and some of the rating agencies talking to me to understand the basis of the draft directions for precisely that reason so, yes, there is concern there. What really matters, going back to a previous question, is whether Tube Lines can deliver for this cost, and that is a matter for the company.

Q172 Mr Wilshire: You rather indicated it was predictable that Tube Lines would not be wildly enthusiastic about the decision you took a few weeks ago. Would you accept that that decision in itself could potentially make matters worse, whether or not the decision was right in the end, as being yet another problem for them?

Mr Bolt: Clearly it creates a problem. I emphasise it is a draft direction and both London Underground and Tube Lines will be making further representations so it might change but, yes, the whole structure of the PPP is that this is a long-term contract with sub-periods within it. The pricing for a seven and a half year period is designed to give the company a clear framework within which to plan its work to deliver greater efficiency but the flip side of that is every seven and a half years there will be this sort of process which creates a significant measure of uncertainty.

Q173 Mr Wilshire: You say you think it is in most people’s interests for Tube Lines to continue to survive. You accept that your draft decision might have made life more difficult. Have you had the opportunity and made it your business to watch at all what the effect of that draft decision has been vis-à-vis the viability in the medium and longer term?

Mr Bolt: It has clearly been a concern for me but there is a very clear difference between the framework set out in the PPP contract and for example that which applies to a price regulated utility. Take Network Rail as an example that you and I are familiar with, one of the duties on the Regulator in the Railways Act is not to make it unduly difficult for Network Rail to finance its activities; it is there as a statutory duty. There is no such equivalent on the PPP. I am told to price on the basis of the notional infraco, which is the company from transfer operating in an efficient and economic manner in accordance with good practice. If the actual infraco has not delivered to that standard in the first review period, by definition, it is going to have some catching up to do in the second period. Whether that catching up is achievable or not is precisely the question that Tube Lines is now deliberating about.

Q174 Mr Wilshire: I am not seeking to criticise. I am trying to see with a little bit of hindsight now available to you whether you have reached any sorts of conclusions about what impact that draft decision of yours might have had thus far?
Mr Bolt: Clearly it is forcing Tube Lines to think very carefully about whether it is able to deliver its future obligations on the basis of funding reflecting those costs. The reason for emphasising that distinction between the regimes is that the PPP contract could have said “price on the basis of the notional infraco starting from the start of the second review period”. It did not. It is very clearly saying any inefficiency in the first review period is down to the company. You do not restart the clock. So that issue about viability is inherent in the way the contract was established.

Q175 Mr Wilshire: Just one last question, if I may, off the back of that. You are keen that Tube Lines survives. You can see that what you have done in the draft decision may harm them—I am not saying it will but it may—so in order to help Tube Lines to continue, are there things that you are entitled to do or could do to assist and to help or is that way beyond you?

Mr Bolt: In shifting things up to reflect their actual position rather than the notional infraco, I would be having London Underground, rightly, saying I had not done the job as defined in the contract. The short answer to your question is no there is nothing under the terms of the contract I can do to take account of those sorts of factors.

Q176 Mr Wilshire: Not necessarily take account in changing your mind or taking decisions, I am just interested in in what you see from your independent position and being able to make comparisons, as you said, was a valuable reason why you should have Tube Lines, whether you can then go to Tube Lines and say, “This is what I have seen. These are the things I really do think would help you.”, and to volunteer that rather than wait to be asked?

Mr Bolt: Maybe I misunderstood your question.

Q177 Mr Wilshire: It is as much my fault as yours.

Mr Bolt: One of the things that I have been keen to do is not simply to use international benchmarking as a device for setting costs but to promote understanding about what it is that metros in Madrid or Paris or some of the others we have looked at in detail do that is different so that Tube Lines can learn and London Underground can learn, because it is absolutely clear that in a number of areas, not just the Underground because it applies to the national rail network, costs in the UK are higher than in comparable activities in other European countries. We need to understand why to help drive further efficiencies, so, yes, I do see it as part of my role not simply to hand this to Tube Lines and say get on with it but to help them understand what it is that some of the benchmarks I have used are doing differently.

Q178 Mr Martlew: Mr Bolt, you say things very reasonably, but having listened to some of the things you have said they are quite startling. At one point you indicated that you fined—my word “fined”—or charged London Underground for being unreasonable. Is that the case?

Mr Bolt: The nature of the PPP contract involves a lot of interfaces between London Underground as client and Tube Lines, and I think on previous occasions when this Committee has looked at the PPP, examples have been raised about the number of signatures that were originally required to sign off a station project and things like that, and it was included in the NAO’s report which the Public Accounts Committee looked at recently. Yes, this sort of relationship involves costs. There have been some areas. I have had to exercise judgments in interpreting benchmarks and in two areas—admin costs and risk—I have shaded that upwards because of my view that that relationship does add to costs and that even the most efficient company would incur those sorts of costs.

Q179 Mr Martlew: I am not totally sure what you said there, Mr Bolt. The question I am asking you is you have looked at it and you have increased the amount of money due to Tube Lines because you accept that in certain instances London Underground has been unreasonable. Is that correct?

Mr Bolt: Where I have exercised judgments in some areas I have shaded the judgment up. Can I point to a precise number in here? No. It is in the overall judgments and weighing the balance of arguments between the two parties.

Q180 Chairman: Do you consider you have access to enough information to make those judgments?

Mr Bolt: To be honest, I do not think that is the sort of decision which is one that you can say the cost of London Underground’s behaviour is X. It is a judgment about what you would expect and whether in all cases London Underground has acted as constructively as it can. Within the contracts there is this description of a partnership and it is absolutely clear that that concept of partnership has not always operated.

Q181 Mr Martlew: In some ways you think instead of an arbiter they need a marriage guidance counsellor? At one point you said that the Bechtel model did not appear to be right for this. Could you develop that point?

Mr Bolt: The point I was making quite simply was a signalling project is essentially software and the way you manage software projects is very different from the way you manage a civils projects. Bechtel have a good reputation on managing civils projects. When I appeared in front of this Committee wearing another hat we have talked about the failings that Network Rail had on signalling projects. It is one of these areas where it seems the UK is not very good yet.

Q182 Mr Martlew: You made the point and the present Rail Regulator is making the point that the cost of doing work on rail is probably 25% greater in the UK than it is in comparative countries and that goes for the Tube as well, but can I take it that what you are saying is that none of them, be it Tube Lines or London Underground, are as efficient as they
should be but that Tube Lines are more efficient than London Underground? If that is the case, how do you explain the Mayor denying that when he came before us?

Mr Bolt: I cannot explain what led the Mayor to say what he said.

Q183 Mr Martlew: What are you saying is there is no evidence to back up his view?

Mr Bolt: No, not that I have seen. One point he was making could be a very different point which is that London Underground undoubtedly has managed to drive costs out of the former Metronet infracos but so it should have done because that was starting from a woefully inefficient position.

Q184 Mr Martlew: A final point, and it is a question Mr Stringer asked, is that you are saying there would be a cost to Tube Lines for the delay in completing the Jubilee Line and that would amount to a fine. Have you got any idea about what sort of figure that would be?

Mr Bolt: From memory it is of the order of £10 million a month.

Q185 Mr Martlew: So it is a lot of money?

Mr Bolt: It is a significant sum of money, yes.

Q186 Mr Martlew: How long do you think it is going to be overrunning?

Mr Bolt: I believe Tube Line’s current estimate is they will deliver the full contractual capability by October so ten months late.

Q187 Mr Martlew: So you are talking about a £100 million fine?

Mr Bolt: Against that they have claimed £300 million from London Underground which includes in a sense their view that the primary cause of that delay is London Underground itself.

Q188 Mr Martlew: That is to be decided?

Mr Bolt: That is the matter which the adjudicator is currently considering.

Q189 Mr Martlew: Finally again, going back to the issue of when you were the Rail Regulator, have you ever been in a situation where you have had two so-called partners who have been at loggerheads as much as these two organisations are?

Mr Bolt: I think it is fair to say that relationships between train operators and Network Rail were not always straightforward and the Rail Regulator felt like a marriage guidance counsellor on occasions.

Q190 Mr Martlew: But I am asking is this worse than that?

Mr Bolt: It is worse in the sense that quite often on the national rail network, if you take the West Coast, Virgin had a particular view but the freight operators or London Midland or Cross Country might have had a different view, and it was the job of the Regulator to balance competing views and make sure Network Rail was delivering efficiently. In this case you have just got two so you probably get more extremes in the views coming out.

Q191 Mr Martlew: Do you suspect there could be politics involved in this as well?

Mr Bolt: I do not get involved with politics.

Mr Martlew: I am sure you do not but I thought I would ask you anyway.

Q192 Chairman: A diplomatic answer but we might decide to pursue this further. You referred earlier to this Committee’s earlier representations that you should have increased powers. Which powers do you think it is most important to increase to let you do your job more efficiently?

Mr Bolt: You recommended in your previous report that I should have the power unilaterally to carry out the equivalent of the annual Metronet report without being asked to do it, and for Tube Lines as well as Metronet. I think the ability and in a sense the duty to report for the benefit of taxpayers and users of the Underground on all three infracos—BCV and SSL within London Underground ownership, and Tube Lines in private sector ownership—and to do that independently would be valuable.

Q193 Chairman: Have you been given any indication that there might be any change in that area?

Mr Bolt: As I say, that could be done within the existing statutory framework if London Underground were prepared to make a reference to me. I have received absolutely no indication that they are minded to do that and indeed the answer Mr Parry gave to one of your questions in December suggests that that remains their position.

Q194 Chairman: Why do you think they are so opposed to that?

Mr Bolt: He expressed his position there. I think there is clearly a governance structure within TfL and if the Mayor believes that is delivering the same rigour and transparency as me looking at it then that is his view, but it seems to me that the ability to do the comparison on an equal basis between all three infracos would be extremely valuable and only I could do that because clearly the Mayor is not in a position, nor is the independent advisory group he is setting up, to look at what is going on within the Tube Lines contract.

Q195 Chairman: Do you get enough information from London Underground about its performance?

Mr Bolt: I get information. I get the information I ask for so it is not their willingness to provide it. It is sometimes the understanding of that information. I referred earlier to the asset management plans, the projections for BCV\(^1\) and SSL\(^2\) for the next seven and a half years and I am able to ask the independent reporters that I appoint to look at the basis of those plans and will do so in the new year and their report.

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1 Bakerloo, Central and Victoria lines
2 Sub-surface line
will be published, but that is not the same as carrying out, for example, a periodic review of the BCV and SSL costs for the next seven and a half years.

**Q196 Chairman:** Do you think you should have powers to monitor the performance of all parties?

**Mr Bolt:** Of all the infracos?

**Q197 Chairman:** Yes?

**Mr Bolt:** Yes, and that goes back to the answer I gave earlier. In doing that analysis on a comparable basis for the three infracos and within the infraco comparing different lines is a source of learning—the joint benchmarking I referred to earlier. It is true that both Tube Lines and London Underground have learned from those comparisons—why is it for example on track work that the Piccadilly Line has very much lower unit costs than any other line? They have learned from that. That is one thing. It is just that the knowledge that you are subject to scrutiny keeps you on your toes.

**Q198 Chairman:** You said earlier that the UK was not very good at delivering infrastructure developments economically. Why do you think that is?

**Mr Bolt:** A variety of factors I think. I would emphasise the point, you certainly observe differences in wage rates between London and other cities, and I am not suggesting that London overnight can become a low-wage economy. What I am saying is the way that projects are planned in other areas is different. There are clear lessons for Tube Lines as it moves from the Jubilee Line to the Northern Line to the Piccadilly Line. Quite often—and the Madrid experience has been particularly relevant here—that can be done with relatively few closures if you plan the project properly. Standards are different. They tend to be more reliant on risk-based approaches to maintenance rather than a frequency basis. There is a whole raft of things like that all of which add up to a significant difference in costs.

**Q199 Chairman:** Do you think we are learning any of those lessons?

**Mr Bolt:** I think we are learning. It is all about the pace of learning.

**Q200 Chairman:** Is the pace fast enough?

**Mr Bolt:** Personally I think the pace is not fast enough, which is one of the reasons Network Rail finished up with more challenging efficiency targets than it started off with proposing and why the numbers for Tube Lines also involve lower costs than they proposed.

**Chairman:** Thank you very much.
Written evidence

Memorandum from ASLEF (UPP 01)

1. The Associated Society of Locomotive Engineers and Firemen (ASLEF) is the UK’s largest train driver’s union representing approximately 20,000 members in train operating companies and freight companies as well as London Underground and Overground. With our long experience and extensive knowledge of the UK rail industry, ASLEF is well placed to comment on the current issues and developments in the sector.

2. ASLEF welcomes the opportunity to contribute to the Transport Select Committee’s update on the London Underground and the PPP agreements.

3. ASLEF is opposed to Public-Private Partnerships in principle and believe that the collapse of Metronet gives a clear example of why such agreements are an inefficient and damaging way of developing much needed upgrades on the Underground system.

4. The union believes that the public contracts given to private companies are too often a risk free venture for the contractor who can only make profit from the public purse and have no danger of losses. This is quite clearly demonstrated by the fact that Metronet’s demise cost its five parent companies (Atkins, Balfour Beatty, Bombardier, EDF Energy, and Thames Water) £70 million each. It cost the tax payer £1.7 billion. This means each parent company has lost just 4.1% in comparison to the public purse.

5. In addition to the huge financial drain the failed PPP with Metronet was to the taxpayer, it also meant that much needed work was delayed or not done. The collapse of Metronet had enormous implications for the London Underground system, the workforce and the travelling public. Contracts that were supposed to deliver upgrades to 35 stations over three years in fact only delivered 14 (this is just 40%). Stations that were supposed to cost Metronet £2 million in fact cost £7.5 million, 375% of the original stated price. By November 2006, only 65% of scheduled track renewal had been achieved.

6. The union takes the view that within the flawed PPP system, there were additional errors such as Metronet having a tied supply chain which guaranteed the majority of work to its parent companies but without safeguards. This system also prevented any competitive tendering for the sub-contracted work.

7. ASLEF would point that the return anticipated by Metronet’s shareholders appears to have been out of all proportion to the level of risk associated with the contract. The implication of this was that the Metronet contract was completely ineffective in transferring any risk from the public to the private sector. Therefore the contract has almost no benefits for the taxpayer but gives guaranteed money to the parent companies.

8. The committee previously stated that “it is worrying that the Government’s confidence in such savings appears to stem from a belief that inefficiency is more endemic and irreversible in the public than the private sector.”

9. ASLEF would urge the Government to learn that the private sector is not inherently more efficient than the public sector. This is especially the case when there is such limited risk for a company and there is no competition within the supply chain. In short, the company simply has a licence to take money from the public purse with no concern for the work taking place and no risk of financial loss from mismanagement or inefficiencies.

10. The union believes that lessons have clearly not been learnt as significant failings are now evident in the case of Tube Lines. London Underground has revealed that it has “grave doubts” over Tube Lines ability to deliver the upgrades needed on the Jubilee Line. They have had to extend their weekend closures, creating great inconvenience for the public and still look to be falling behind targets. Tube Lines is now claiming that works that had been priced at £4.1 billion to improve the Jubilee, Northern and Piccadilly Lines will cost £5.5 billion, leaving a gap of £1.4 billion. Other estimates suggest costs could rise to £7.2 billion. ASLEF is deeply concerned at these developments both for its members on London Underground but also the travelling public.

11. It therefore looks like the one remaining PPP company is destined to fail in a similar way to Metronet. Lessons have clearly not been learnt and ASLEF believes this shows the fundamental flaw in PPP and its ability to ensure infrastructure upgrades.

12. It should be clear from the Metronet catastrophe that the optimum means of delivering Underground infrastructure improvements is within an internal, vertically integrated structured. PPP is simply a flawed model and we can only hope this expensive mistake can perhaps have one positive outcome, an end to the presumption that the private sector is good and the public sector is bad.

13. There are clear risks in the PPP Agreement with Tube Lines and as a result of the previous issues with Metronet. The lack of any real risk along with reduced competition means that innovation, competition and efficiency do not occur at any stage of the process with the resulting spiralling costs and taxpayer bailouts.
14. ASLEF believes that the current economic climate will have very grave implications for PPP and PFI schemes. Construction and infrastructure companies are being affected more than most during this recession. If they feel they cannot make money from their public contracts they will simply cut their losses, withdraw from the contracts and leave the taxpayer to pick up the bill and the mess. This is exactly what happened with Metronet and is more likely to happen during periods of economic instability and recession.

15. ASLEF would highlight that the previous Mayor of London opposed PPP but the scheme was pushed through by the Government. The Government’s policy has since been proven wrong. It is therefore essential that the Government learn from this costly mistake and heavily scrutinise all PPP and PFI schemes in the light of the Metronet collapse.

16. To conclude, ASLEF welcomes the revisiting of this vitally important issue by the Transport Select Committee. The union believes that the PPP model as used on the London Underground is utterly discredited, leaving the taxpayer saddled with huge debts while letting the companies involved walk away with minimum liabilities. We hope that lessons are learned by the Government for the future of all public sector infrastructure projects.

October 2009

Memorandum from the PPP Arbiter (UPP 02)

INTRODUCTION

1. The role of statutory Arbiter for the London Underground Public-Private Partnership Agreements was created by the Greater London Authority Act 1999. I was appointed as the first PPP Arbiter in December 2002, and my appointment runs to 30 December 2010. My role is concerned principally with assessing the efficient level of costs and pricing at Periodic Review (and at the Extraordinary Reviews which may take place between Periodic Reviews). Annex 1 summarises my functions and duties.

2. Based on my experience to date, I set out below my views on some of the questions covered by the call for evidence. I do not respond on questions which are outside the scope of my role as PPP Arbiter. Nor do I comment on matters directly related to the Periodic Review of Tube Lines’ PPP Agreement which are the subject of a reference to me from London Underground dated 23 September 2009.

What lessons can be learned from the collapse of the London Underground PPP Agreement with Metronet?

3. My views on the collapse of Metronet were set out in evidence to the Committee in 2007, when it last considered the London Underground PPP.1

4. I consider that the main lessons which are relevant to the management of the PPP Agreements are that their effectiveness depends on:

— an agreed base plan, to enable effective monitoring of both costs and performance;
— a clear understanding between the contract parties about the allocation of risk, with effective monitoring of key risks, in order to incentivise delivery by the infracos;
— effective partnership;
— regular independent reporting on the performance of the infracos; and
— provisions which prevent an Infraco deferring a request for Extraordinary Review once it is clear that increases in costs are likely to exceed the Materiality Threshold.

5. In terms of delivery, there was a general consensus that Metronet’s governance was ineffective and that this, coupled with its supply chain structure, made a major contribution to its failure. Tube Lines competitively tendered its major contracts, for example in respect of the signalling upgrades for its three lines, although secondment agreements with its shareholders, Bechtel and Amey, give those companies a major role in managing major projects and operations respectively. In preparing for a Periodic Review reference, I have sought advice on whether this approach to procurement and project management has delivered an outcome consistent with that of a Notional Infraco.2

6. Although London Underground has claimed savings of £2.5 billion as a result of taking Metronet in-house, this largely reflects reductions in costs from levels which, as part of my uncompleted 2007 Extraordinary Review of Metronet, I had concluded were inefficient. It is too early to make a robust comparison between the costs of public sector and private sector provision of infrastructure services. However, the report on Phase V of the joint benchmarking programme comparing the operating expenditure of Tube Lines with the former Metronet companies, which covers 2008-09, will be available shortly. Initial results from the draft analysis undertaken for this report suggest that the former Metronet companies’

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2 The Notional Infraco is defined in the PPP Agreement as the notional entity with the same contractual terms and financing as Infraco, and which carries out its activities in an “overall efficient and economic manner and in accordance with Good Industry Practice”. The Notional Infraco is the basis of repricing the contract at Periodic Review.
maintenance costs for track, signalling, stations, lifts and escalators have risen in 2008–09 compared with 2007–08 levels. The draft analysis also reinforces previous year’s benchmarking results which have found Tube Lines’ maintenance costs to be lower on average than for the former Metronet companies.

**Are these lessons being applied to the London Underground PPP Agreement with Tube Lines?**

7. As part of the preparation for the Periodic Review, my Office has developed a format for the submission of information about future costs (the “Data Breakdown Structure”—DBS) which both London Underground and Tube Lines have agreed to adopt. This will ensure consistent provision of information, which London Underground is also following for the former Metronet companies. In particular, it will facilitate monitoring of costs and activities against plans, and make it easier to compare performance both between the infracos and with external comparators.

8. Under the terms of the PPP Agreement, an Infraco is protected, through the Extraordinary Review mechanism, against all changes in the efficient cost of delivering its contractual obligations, except for the first £50 million in each 7½ year period. This is only about 1½% of the contract value. An important part of the Periodic Review is therefore establishing an appropriate allowance for risk. If this is too high, London Underground could pay too much for the contract; if it is too low, an early Extraordinary Review could be required, which would impact adversely on incentives to deliver improved efficiency over the whole Review Period.

9. I have also, therefore, discussed with the Parties through the regular tripartite meetings which I chair the linkage between the risk allowance at Periodic Review and the form and conduct of the Extraordinary Review mechanism in the second Review Period. This will now be considered further as part of the Periodic Review reference.

10. Under Metronet’s PPP Agreements, it was envisaged that the Arbiter would report annually on efficiency and economy. In the event, I was only asked to carry out one such annual review, in 2006, before Metronet went into administration. Although the Metronet PPP Agreements remain in place, London Underground has indicated to me that it does not propose to seek annual reports in future. The Committee recommended in its last report on the PPP that a mechanism be put in place to allow the PPP Arbiter to report annually on the performance of all the Infracos, including Tube Lines, whether or not he is called on to do so; the recent report from the National Audit Office made a similar recommendation.

11. Unless the Arbiter’s role is extended in the way the Committee recommended, the future role of the Arbiter would be restricted to Periodic and Extraordinary Reviews of the Tube Lines Agreement alone. With this restricted role, and no regular reporting function, it would be difficult to retain or recruit staff of the current calibre beyond the current Periodic Review. This could seriously prejudice the effectiveness of the Arbiter’s statutory role, for example by losing continuity in the benchmarking work which I have initiated.

12. If the Arbiter was able to prepare and publish regular assessments of Infraco performance, it might not be necessary to make contract changes to prevent an Infraco deferring a request for Extraordinary Review (or giving London Underground the right to trigger such a Review). With that degree of transparency, it is much less likely that lenders would waive the requirement to seek Extraordinary Review than was the case with Metronet.

**How has the upgrade work progressed since the demise of Metronet?**

13. It is currently difficult to make a full assessment of the upgrade projects, given that most are still under way, and because of changes in reporting arrangements for Metronet following administration. The Arbiter is working with London Underground to develop information that would permit him to monitor the Metronet upgrades and use data gathered in this way as a benchmark for Tube Lines.

14. The Arbiter’s Independent Reporter has reviewed the basis of London Underground’s cost projections for the former Metronet companies and raised a number of concerns about the robustness of the projections. A further review will be undertaken by the Reporters in the New Year.

**What contractual arrangements are appropriate for the future?**

15. Experience with the PPP Agreements over the first Review Period suggest that areas where contractual changes might be considered for the future include the following:

- a requirement to produce data in a stable (DBS) format that tracks progress against the financial baseline for Net Adverse Effects;
- a requirement for Infraco to prepare, in DBS format with appropriate commentary, a delivery plan for each Review Period following completion of the Periodic Review;

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3 This “Materiality Threshold” was £200 million for Tube Lines in the first Review Period.
4 London Underground has also indicated that it has no intention of involving me in the Periodic Review of the agreements.
— an annual review (either by London Underground or the Arbiter) of contract delivery based on a comparison between updated plans for the remainder of the Review Period and the delivery plan;
— clarification of the treatment of investment to deliver improved efficiency where the payback period straddles a Periodic Review;
— clarification of the potential overlap and conflict between Extraordinary Review and contractual claims;
— clarification of overlapping jurisdiction between the Arbiter and an Adjudicator at Periodic Review, for example in relation to financeability; and
— review of the Extraordinary Review mechanism given the lower materiality threshold for RP2.

16. Although a number of these matters are covered by “entrenched provisions”, which means that London Underground is unable to propose changing them as part of the Periodic Review, I have the power in giving directions to make directions which are ancillary and incidental to the matter referred. As with all my directions, these have the effect of modifying the contract unless both Parties agree to set the directions aside. I will therefore want to consider as part of the Periodic Review reference whether there are matters in respect of which I have the power to make such ancillary or incidental directions in order better to achieve the objectives set out in my statutory duty.

17. I have no role in respect of contractual arrangements which are not designated PPP Agreements. This includes, for example, the proposed contract for resignalling of the Sub-Surface Lines. However, many of the principles outlined above are equally relevant to other contractual models.

18. Given my limited remit, it would not be appropriate to comment in detail on alternative contractual models. However, I have previously compared the PPP structure with the regulation of the national rail network, noting the greater flexibility under a licence structure than under a contract. My conclusion then was that “if the Parties are able to agree changes in the incentive structures where there are weaknesses, learning from the experience of the regulated utilities, then the outcome in terms of efficient delivery of customer requirements could be very similar to that achieved by economic regulators—even with an Arbiter reacting to disputes rather than driving the process. But if these opportunities cannot be taken, then the superiority of a licence structure will have been demonstrated.” I stand by that conclusion.

What risks, if any, are associated with the PPP Agreement with Tube Lines?

19. The main risks associated with Tube Lines’ PPP Agreement are, in my view, as follows:
— inability for Tube Lines to finance the difference between the efficient costs of delivering contract obligations in the second Review Period and London Underground’s Affordability Constraints, leading to a requirement to descope or, in certain circumstances, Special Mandatory Sale;
— increases during the second Review Period in efficient costs of delivering contract obligations, leading to additional ISC payments by London Underground, or a requirement to descope for affordability reasons, at an Extraordinary Review;
— financial failure as a result of Tube Lines incurring costs inefficiently, or failing to deliver contract obligations as a result of inefficiency; and
— “regulatory risk”.

20. I have yet to make any directions under the provisions of the GLA Act, which inevitably creates a degree of uncertainty about the basis on which I would reach decisions. I have sought to mitigate this by:
— consulting on, and publishing a Procedural Framework for handling references, with accompanying Procedural Approach documents for different types of reference updated in the light of experience;
— sharing technical reports and advice (for example benchmarking reports) with the Parties, seeking comments on that advice, and in most cases publishing the reports;
— responding positively to requests for guidance, even where I have discretion not to give it, and giving full reasons for guidance, supported by detailed technical reports; and
— in respect of the Periodic Review, establishing and (with the agreement of Tube Lines and London Underground) chairing a regular tripartite meeting to ensure adequate preparation for the Review.

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8 GLA Act, section 229(3)(b).
10 Under the provisions of section 230(2) of the GLA Act, I may give guidance if the reference comes from one party; I shall give guidance where both the Parties to an Agreement request it.
THE FUNCTIONS AND DUTIES OF THE PPP ARBITER

1. The role of the PPP Arbiter was established by the Greater London Authority Act 1999 (GLA Act). Under the terms of the GLA Act, the Arbiter is independent of Government and of the PPP Parties and can only be dismissed by the Secretary of State on grounds of incapacity or misbehaviour, or for unreasonable delay in the discharge of his functions.

2. The Arbiter is a corporation sole. I was appointed as the first Arbiter on 31 December 2002, and my appointment now runs to 30 December 2010. I am supported by a small permanent staff. As I am appointed as an individual, and am personally responsible for the exercise of my statutory functions, I have also appointed an Advisory Board to provide independent and expert challenge to my decisions and procedures. Although I am not required by statute to do so, I have published each year a Business Plan and my Annual Report and Accounts setting out the work programme of my Office and the resources used.

3. As PPP Arbiter, I have two principal statutory functions:

— to give directions on matters specified in the PPP Agreements, when asked to do so by one of the Parties to a PPP Agreement; and
— to give guidance on any matter relating to a PPP Agreement, when asked to do so by either (or both) of the Parties to a PPP Agreement.

4. When the Arbiter is asked for guidance by one Party only, the Act gives me discretion about whether to give guidance. Where I am asked for directions, or am asked for guidance by both Parties to an Agreement, I am required to give directions or such guidance as I consider appropriate.

5. Although the Arbiter can be asked for guidance or directions at any time, it was expected that he would exercise formal functions in three main circumstances:

— in giving an annual “definitive statement” on the performance of the two Metronet infracos;
— at the Periodic Review of the Agreements which takes place every 7½ years; and
— at an Extraordinary Review of the terms of a PPP Agreement if there were material changes in costs and revenues within a Review Period.

6. In addition, the Act gives the PPP Arbiter further powers “for the purposes of the proper discharge of the functions” conferred on him by the GLA Act. For example the PPP Arbiter may do “all such things as he considers appropriate for or in connection with the giving of a direction or guidance and . . . do such other things as he considers necessary or expedient . . . for purposes preparatory or ancillary to the giving of directions or guidance generally . . . notwithstanding that there is no matter in relation to which a direction or guidance is required”.

7. The PPP Arbiter’s function in respect of directions is limited by the terms of the PPP Agreements: if there is no specific provision in a PPP Agreement for the PPP Arbiter’s involvement then disputes are dealt with through contractual dispute resolution. Even on matters within his remit, he is only brought in if one of the Parties seek a direction from him. The PPP Arbiter therefore has no unilateral power to change, or propose to change, provisions in the PPP Agreements. Even where he has made a direction on a disputed matter within his remit, the Parties may, under the provisions of the GLA Act, jointly agree to set it aside.

8. In exercising his functions, the Arbiter is under a statutory duty to act in the way he considers is best calculated to achieve four objectives:

— to ensure that London Underground has the opportunity to revise its requirements under the PPP Agreements if the proper price exceeds the resources available;
— to promote efficiency and economy in the provision, construction, renewal, or improvement and maintenance of the railway infrastructure;
— to ensure that if a rate of return is incorporated in a PPP Agreement, and taking into account matters specified in the Agreement, a company which is efficient and economic in its performance of the requirements in that PPP Agreement would earn that return; and
— to enable the Infracos to plan the future performance of the PPP Agreements with reasonable certainty.

The Arbiter is also under a duty to take account of any factors which are notified to him by both Parties to an Agreement, or are specified in the relevant PPP Agreement, as ones to which he must have regard.

9. For the purposes of assessing costs at a Periodic Review or Extraordinary Review, the PPP Agreement establishes the concept of the Notional Infraco. This is defined as the entity which has the same obligations as Infraco, which carries out its activities in an overall efficient and economic manner and in accordance
with Good Industry Practice, and has certain other specified characteristics. A key part of the Arbiter’s role is therefore to assess what constitutes Good Industry Practice and the level of performance and cost which would be efficient and economic.

*September 2009*

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**Memorandum from London TravelWatch (UPP 03)**

1. **INTRODUCTION**

   London TravelWatch is the official body set up by Parliament to provide a voice for London’s travelling public, including the users of all forms of public transport. Our role is to:
   
   — speak up for transport users in discussions with policy-makers and the media;
   — consult with the transport industry, its regulators and funders on matters affecting users;
   — investigate complaints users have been unable to resolve with service providers; and
   — monitor trends in service quality.

   Our aim is to press in all that we do for a better travel experience all those living, working or visiting London and its surrounding region.

2. **THE INQUIRY**

   London TravelWatch welcomes the House of Commons Transport Committee’s further inquiry, which will build on its previous work, and will consider:
   
   — Whether the lessons learned from the collapse of the Metronet PPP consortium have been applied to the Tube Lines PPP?
   — How the upgrades are progressing?
   — What contractual arrangements are appropriate for the future?
   — What risks are associated with the PPP arrangements with Tube Lines?
   — What impact is the current economic situation having on transport PPP and PFI schemes and what are the financial implications for other transport schemes?
   — What role has the Government played in these matters?

   Recently, we have worked closely with the London Assembly Transport Committee on this issue, and attached as Appendix A is our written evidence to them.11

3. **GENERAL PRINCIPLES OF THE PPP**

   In general terms Public Private Partnerships (PPP) are typically characterised by the following features:
   
   — long term relationship between the public sector and a private partner for the delivery of a project, typically contracts are between 15 to 30 years;
   — funding is provided by the private partner, however some level of public funding may be included to complete the funding requirements of the project;
   — the private partner is typically involved in all levels of delivery of the project the objectives of which have been defined by the public sector; and
   — a transfer of risk takes place from the public to the private sector. This does not mean that the public sector is left without risk, but much of the risk associated with a portion of the financing, the delivery and operation of the project would typically be transferred. The actual distribution of the risk is dependent on the ability of each party to be able influence and control the risk. The public sector will therefore retain a substantial amount of risk over which it retains control. Examples of retained risk might include:
     — changes in scope of the project;
     — changes in the law;
     — force majeure; and
     — indemnities for specific issues such as existing asset conditions.

   Globally PPPs can vary substantially within these broad features and even within the UK a wide variety of structures can be observed.

   As previously submitted to this committee, London TravelWatch supports the objective of the London Underground PPP to guarantee the flow of investment into the Underground, after many years of inconsistency and fluctuation. We consider it of the utmost importance that the periodic reviews at 7.5 year

11 Appendix A has not been reproduced as already in public domain.
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intervals should not be allowed to become vehicles for under-funded price rises and for the scope of investment plans to be cancelled or reduced in scope. This concern is given added importance by the slippage that has occurred in parts of the investment schedule, and by Metronet going into administration, each of which phenomena increases the opportunity for cuts to be made in previously agreed investment programmes.

We were initially concerned that animosity to the principle of the PPP would adversely affect relationships between London Underground (LU) and the PPP contractors. We are therefore encouraged by the determination of LU’s top management to work constructively for the success of the PPP in the interests of Underground users, whatever may have been the political debate over its introduction.

We are, however, concerned that—despite assurances that the Infrastructure Companies (Tube Lines and Metronet) would get on top of the problems, once the period of climbing the “learning curve” had passed—placing contracts for looking after 70% of the LU network with a single organisation was too much. Tube Lines, with only 30% of the business, has shown itself to be more capable of delivering projects on time and to budget, although its slowness to rise to the challenge of improving performance on the Northern line has been disappointing.

However, we are now somewhat alarmed by the increasing number of weekend engineering possessions being required on the Jubilee line in recent months, and about how the upgrade of the Piccadilly line will take place particularly on the central London section of route. We submitted evidence to the London Assembly Transport Committee scrutiny of this issue and this we attach as appendix A to this submission. We believe that whilst passengers are willing to accept some measure of “pain”, provided that they are informed about alterations to their services well in advance and can plan accordingly, when these are then supplemented by short notice additional closures for example, passengers’ patience can be severely tested. This is particularly important when passengers may be making leisure journeys (say to the O2 arena) or to places of employment which require attendance at weekends.

4. Lessons learned from the collapse of Metronet and progress of the upgrade work subsequently?

As we highlighted in previous submissions the structure of the Metronet PPP and its modes of operation were complex and in many cases did not deliver value for money for the taxpayer or the standard of service expected for the passenger. We believe that in the case of Metronet, now under the control of London Underground, there have been substantial changes in working and accounting practices since the takeover of Metronet that have produced substantial cost savings and increased overall efficiency.

The structure of the Tube Lines PPP shares much in common with the Metronet PPP, but the characteristics of the Tube Lines are fundamentally different in respect of their supply chains. The principal lessons of the Metronet collapse that are applicable directly to Tube Lines are:

— a proactive management of PPP risk by the public sector; and
— formal recourse to the PPP Arbiter in assessing costs.

5. What contractual arrangements are appropriate for the future?

London TravelWatch strongly advocates for the contractual arrangements which balance the least disruption and greatest benefits to passengers. In the shorter term changing the contractual arrangements are likely to result in disruption which would not be in the interests of passengers. In the longer term consideration should be given as to whether PPP is the best means to deliver infrastructure maintenance and enhancements to London Underground’s network. The collapse of Metronet has illustrated the complexity and costs incurred when PPP structures are not successful. It also illustrates that in reality it is challenging to achieve genuine risk transferral.

As an example of the high costs of PPP/PFI projects, the Intercity Express Project incurred £14.95 million of consultancy fees up to March 2009. The complexity of the PPP/PFI structure and the tendency to develop bespoke structures for each deal means that the advisory costs to the public sector are high. These costs have to be recovered by private sector efficiencies. The reality of the efficiency gains are hard to establish given that the life time of a typical PPP of 30 years.

6. What risks are associated with the PPP arrangements with Tube Lines?

The principal risks associated with the PPP arrangements with Tube Lines for passengers are programme overruns. As an example London Underground informed London TravelWatch of additional closures of the Jubilee Line on the weekend of 26 to 27 September and 3 to 4 October in order to allow Tube Lines more engineering access to meet their programmed deadlines for the Jubilee Line signalling upgrade. Line closures are disruptive to passengers at the best of times, but the unplanned closures were announced with minimal warning to passengers on 23 September three days prior to the first altered closure date. It would also appear from recent press statements that Tube Lines, despite additional line closures, is unlikely to be able to deliver the Jubilee upgrade on time.

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12 Page 43, Modern Railways, August 2009.
There are also risks related to the continued disagreement between London Underground and Tube Lines over the restated terms. London TravelWatch urges both sides to come to an agreement over the Tube Lines PPP programme that is in the interest of passengers. This means ensuring that the full planned upgrades are carried out on time and at a cost which means that passengers are not penalised with higher fares.

7. What impact is the current economic situation having on transport PPP and PFI schemes and what are the financial implications for other transport schemes?

PPP/PFI is dependent on the availability of credit to the private sector in order to raise debt to finance projects. The impact of the current economic climate has been to reduce the availability of credit and to decrease the appetite for risk. Increased equity investment may also be required from PPP bidders by commercial lenders. For upcoming transport PPP/PFI deals in the UK transport market the consequences are to potentially reduce the number of bidders as well to increase the cost of finance. Bidders may also find it difficult to make definitive quotes for costs which are dependent on sub-contracts or supply chains. The result is that at the bid submission all bidders’ offers are likely to be higher over the whole life costing to cover that risk and the cost of finance.

The UK is a mature PPP/PFI market with well established legal and contractual structures. Transport is one of the most long established sectors for PPP/PFI in the UK with historically the largest cumulative volume of deals. However, many of the factors effecting PPP/PFI are global because of the debt finance requirements and also because many of the bidders are global companies.

The Treasury has set up the Treasury Infrastructure Finance Unit (TIFU) in an attempt to provide liquidity to this market both for upcoming projects and for existing providers. In the Treasury’s view, “it is unlikely that private sector lending will be sufficient to deliver the scheduled pipeline of projects even taking account of increased lending activity by the EIB.” This action by the Treasury may address the immediate issue as a last resort, but the involvement of the Treasury in providing debt finance calls into question part of the logic of private sector involvement in public sector procurement.

Historically Transport has made up the largest element of the PPP/PFI market in the UK. However, the volume of transport PPP/PFIs have reduced substantially and no deals took place in 2008. Of the current transport projects in procurement, the Intercity Express Project and Thameslink Rolling Stock Project both involve providing financing for the rolling stock to be procured. They are therefore considerably impacted by the economic conditions. It is notable that a number of recent transport procurement projects (not all PPP/PFI related) that either planned bid submission dates have been delayed or bidders have been invited to revise certain assumptions. This suggests that the public sector is likely to have to shoulder a greater portion of the risk of PPP/PFI projects. Bidders’ are likely to ask for greater guarantees and conditions which would reduce the overall risk transfer to the PPP provider. The value for money that is achieved by the public sector from PPP/PFI is therefore also likely to be reduced. This could lead to either greater cost to tax payers and the travelling public, or to a more limited scope of investment.

8. What role has the Government played in these matters?

Given the contractual structure between TIL and the Infrastructure Companies the direct involvement of the Government has not been significant. This is because the DfT had no direct controls over the risks associated with the PPP. The NAO report into Metronet identifies this key issue.

In the demise of Metronet, TIL has been left in the position of control over Metronet’s former activities. The fixed grant settlement for TIL has not been revised in order to address this funding requirement going forwards. London TravelWatch urges Central Government to reconsider this position in order that passengers are not affected by:

1. cost savings in the investment programme; and
2. a rise in fares in order to recover additional expenditure costs.

9. Conclusions

London TravelWatch believes that the scale of the London Underground PPPs meant that they were always a challenging prospect to deliver. Whatever the rights or wrongs of the way in which it was carried out, it has attempted to tackle the historic problem that has faced London Underground and its passengers—namely the need for long term commitment to fund investment in the system. In common with other infrastructure operators LU’s previous funding regime had been hampered by a stop-start cycle of capital funding governed by the fiscal requirements of the Government of the day.

London’s transport users would be seriously disadvantaged if either the costs to LU of taking over the Metronet upgrade programme, or the current issues with Tube Lines restated terms, were to put in jeopardy the commitment to continuing investment that the PPP has sought to guarantee. We therefore urge that the interests of passengers are held as paramount in resolving the issues surrounding the restated terms and TIL’s wider funding.

13 http://www.hm-treasury.gov.uk/d/ppp_tifu_letter_050509.pdf
From the collapse of Metronet, there are lessons that can be learnt about the performance of the PPP which could lead to benefits for passengers, and we await the Select Committee’s conclusions with interest.

October 2009

Memorandum from Tube Lines (UPP 04)

OVERVIEW

1. Tube Lines is the infrastructure and asset management company responsible for maintaining and upgrading the Jubilee, Northern and Piccadilly lines, under a 30 year partnership with London Underground, which commenced on 31 December 2002.

2. Tube Lines consistently learns from its experience of running the PPP Agreement that it has with London Underground (the “PPP Agreement”), as well as the broader experience of its members, and has where possible learnt the lessons arising from the Metronet collapse. That approach, and its particular structure and expertise, has enabled Tube Lines to carry out its obligations under the PPP Agreement in an economic and efficient manner, delivering improved safety and substantial enhancements to the efficiency and effectiveness of the lines for which it is responsible. Although the PPP Agreement could be improved in some respects, Tube Lines still considers that the PPP model is a robust one that can deliver real benefits for passengers and the taxpayer.

3. Tube Lines believes that the PPP would work most effectively if there was greater recognition of the benefits brought by the partnership element as originally envisaged in the PPP. There is not always a clear understanding at all levels of London Underground of how to get the best out of the PPP. Tube Lines considers that this lack of understanding of the PPP arrangements and consequent lack of a partnership approach has made the PPP unnecessarily adversarial.

What lessons can be learned from the collapse of the London Underground PPP Agreement with Metronet?

4. On 5 June 2009, the National Audit Office published its report (the “NAO Report”) on the failure of Metronet. The NAO Report suggests that a number of factors contributed to Metronet’s failure.

5. The main cause identified in the NAO Report was Metronet’s poor corporate governance and leadership. Tube Lines agrees with this assessment, which echoes the Transport Select Committee’s view that Metronet’s structure “contributed to the inefficiencies of Metronet” (p 7, TSC, 25 January 2008).

6. The other principal causes identified in the NAO Report were as follows:

   (a) many decisions had to be agreed unanimously by Metronet’s five shareholders;

   (b) Metronet guaranteed subcontracts for capital works to its shareholders, thereby creating a tied supply chain and so preventing Metronet from being able to act economically and efficiently;

   (c) Metronet’s executive and management changed frequently and was unable to manage the work of its shareholder-dominated supply chain effectively; and

   (d) the poor quality of information available to Metronet’s management, particularly on the unit costs of the station and track programmes, meant that Metronet was unable to monitor costs or have work performed economically and efficiently.

7. Tube Lines agrees that a structure where shareholders are tied suppliers cannot work. The NAO Report rightly criticised a corporate arrangement where the shareholders “adopted governance and management structures which gave power to the suppliers rather than the management of the business” (p 8, NAO Report). Future PPP arrangements with the characteristics of the PPP Agreement14 should be brokered with the Metronet example in mind, along with the NAO Report’s recommendation that “contracts should be awarded to bodies which have clear leadership, a credible corporate governance structure and an approach to securing suppliers which can be demonstrated to be value for money” (p 8, NAO Report).

8. The NAO Report also identified a number of issues specific to the PPP Agreement. These include the need for accurate, up-to-date reporting, the need to involve the PPP Arbiter more in the oversight of the whole upgrade programme, and London Underground’s attitude to partnership as demonstrated by its working relationship with Metronet.

9. It is vital for the achievement of the PPP Agreement’s objectives that all those involved in it follow clear, accurate, transparent, and relevant reporting procedures. This does not mean that there should be an increase in bureaucratic reporting, oversight, or control demands; rather, there should be better quality and more appropriately targeted reporting. It also means, as was recognised by the TSC, that there is a clear need for a reporting process that is “neutral and is designed to provide the information that both the Infracos and London Underground require to address performance issues” (p 19, TSC).

14 There are numerous “PFI model DBFO” PPPs for (say) a single site hospital project, where the fixed supply chain model works very well.
10. The role of the PPP Arbiter needs to be considered in light of the changes that have taken place within the PPP Agreement. The NAO Report clearly recommends that “effective independent scrutiny and evaluation of London Underground’s management of major infrastructure projects, on behalf of both [Transport for London] and [the Department for Transport], could provide greater assurance on value for money” (p 8, NAO Report). The Arbiter could play a role in overseeing London Underground’s operation of the lines previously run by Metronet, which is now the subject of no express scrutiny, as well as London Underground’s role in relation to the lines run by Tube Lines, in addition to his current role.

11. We also agree with this Committee’s recommendation that the Arbiter should “[report on] the effectiveness of London Underground as client during the modernisation of the Tube network” (p 35, TSC). The environment created by the PPP Agreement is unique, and requires extensive reporting and administrative burdens, not imposed on other asset management companies around the world. Tube Lines considers that the structure of London Underground makes the operation of these reporting and administrative burdens challenging. As was highlighted in the NAO Report, “both Tube Lines and Metronet found that London Underground’s horizontal organisation, with several overlapping authorities, led to a number of different approaches being required”. The NAO report refers to “90 individuals” identified within London Underground “who held authority in the scope approval process”. The impact of this structure was then exacerbated by London Underground’s behaviour: Metronet contended that London Underground’s approach and behaviour contributed to the difficulties it found itself in, blaming “cost overruns on a wasteful approach to job specification by London Underground” (p 20, TSC).

Are these lessons being applied to the London Underground PPP Agreement with Tube Lines?

12. The lessons learned from the failure of Metronet are, as far as possible, being borne in mind in terms of the way in which Tube Lines operates. However, as set out below, there are limitations on the extent to which changes as a result of the lessons learned from Metronet are both required to be implemented by Tube Lines, due to the fundamental differences between the structure and characteristics of Metronet and Tube Lines, and are able to be implemented, due to the constraints that Tube Lines faces, as Metronet did, in relation to the nature of London Underground.

**Tube Lines’ Corporate Structure and Procurement**

13. Tube Lines is not the same as Metronet. Tube Lines was set up with a very different corporate structure and, as such, its corporate governance structure and policies ensure that it is not impeded by the inflexibility that affected Metronet’s day-to-day management or the impact that conflicts of interest between Metronet’s shareholders had on preventing effective leadership. Unlike Metronet, Tube Lines has a number of independent members on its board, who are not tied to the consortium partners. This means that the board is able to, and does, make decisions in the best interests of Tube Lines, as it is obliged to do. Additionally, decisions by the board are required to be passed by a simple majority, rather than unanimously, unless the matter to which the decision relates was not included on the meeting agenda or it is a matter reserved for consideration by Tube Lines (Holding) Limited (“TLH”). Even where decisions are required to be made by TLH, there are conflict of interest provisions that effectively disenfranchise the shareholders in respect of decisions in relation to contracts with affiliates of the shareholders.

14. Additionally, and by contrast to Metronet, Tube Lines’ lenders play an additional governance role in that they ensure that Tube Lines’ decision making on major issues is conducted properly. In this sense they provide an additional check. The Technical Adviser to the lenders is fully informed on all relevant matters and takes an active role in this process.

15. Tube Lines’ corporate structure also ensures that the company’s management has access to the information that it needs in order to run Tube Lines in an efficient manner. This is substantially because, while the Tube Lines Board retains overall responsibility for the running of Tube Lines, it is assisted by a number of committees, each made up of experts in the subject for which that committee has responsibility. The Tube Lines’ board delegates to the committees the responsibility for conducting internal reviews and analysis of specified matters in order that they can then make recommendations to the Board. This structure ensures that decisions are taken at the appropriate level, on the basis of the necessary information, without the need for overly-onerous procedures in relation to decision making and approvals.

16. By contrast to Metronet, during the course of the PPP Agreement, there has been a low turnover of Board members: indeed, since the start of the PPP in January 2003, Tube Lines has had a low turnover of board members and only two CEOs and two Chairmen, which has enabled stable and consistent management.

17. As emphasised in the NAO Report, there is a distinction to be drawn between the Metronet tied supply chain approach and Tube Lines’ approach, which is described by the report as a “shopping around approach based on procuring goods and services through open competition”. Tube Lines’ operating model relies on a combination of internal resources and external subcontractors selected through competitive tendering to deliver the obligations under the PPP Agreement. Tube Lines has developed, and follows, a detailed procurement process to be used when resources are not available internally, or where to use such
internal resources would not be the most appropriate way to proceed. The procurement process ensures that Tube Lines is able to establish and manage robust contractual relationships which meet the requirements under the PPP Agreement and deliver value for money.

18. As such, the lessons from Metronet’s failure that arise out of Metronet’s corporate structure and procurement arrangements do not need to be applied to the PPP Agreement with Tube Lines because they are not relevant to it.

**Lessons to be learned by London Underground**

19. There are, however, other lessons from Metronet’s failure that, based on our experience to date, are not being applied to the PPP Agreement but which should be. In particular, these lessons relate to the administrative burden created by, and the approach of, London Underground. Both of these factors were highlighted by Metronet as significantly contributing to the difficulties it faced and they continue to this day. Echoing the experience of Metronet, Tube Lines has found that London Underground continues to refuse to see the PPP Agreement for what it is; a fixed price contract for a fixed scope of work, with no general variation or change provision built into it. It remains the case that the lessons that should have been taken from London Underground’s approach to the PPP agreement with Metronet have yet to be fully taken on board.

20. London Underground has constantly sought to depart from the contractual structure established under the PPP Agreement. It has repeatedly sought changes to the scope and/or manner in which the works are carried out and has repeatedly departed from contract procedures. In other words, the level of involvement and interference by London Underground gives rise to considerable additional time requirements and costs but it also undermines progress towards achieving the upgrade of the Jubilee, Northern and Piccadilly lines.

21. As was seen from Metronet’s experience, London Underground has sought to expand the scope of work agreed in the PPP Agreement. It would appear that certain areas of London Underground have not understood how the PPP arrangements should work. Consequently they have repeatedly sought additional work to be carried out that falls outside the scope of the project and in some instances have made Tube Lines completion of tasks conditional on our acceptance of these out of scope works. Some examples of the approach taken by some parts of London Underground to the PPP Agreement include:

(a) Requirements to change the “off the shelf” signalling system for the Jubilee line by adding bespoke elements unique to London Underground, led to a new bespoke system, after the PPP Agreement had been signed. Instead of using the proven “off the shelf” moving block system that is currently being used in Hong Kong as well as on the DLR and elsewhere around the world, which had been selected in the original tendering process, these requirements meant that Tube Lines had to have the system significantly redesigned. This has resulted in a one-of-a-kind system, untried and untested on other metros, being installed on the Jubilee line. The introduction of new requirements has resulted in substantial additional complexity and therefore substantial additional work for the Jubilee and Northern line upgrades with a consequential increase in the original time frame and an increase in the costs.

(b) Regular use of the standards process by some parts of London Underground to oblige Tube Lines to change, expand or alter works being carried out. An example is the use of standards to require Tube Lines to introduce features to improve mobility within stations. Over a period of time, London Underground introduced, changed and withdrew a number of standards and imposed requirements for additional double and lower handrails on stairways, contrasting stair treads highlighting and coloured bands on columns within stations. Although it was clear that the requirements for these features were in addition to the original scope of the work, London Underground insisted that they were required. Tube Lines referred the issue to an adjudicator who determined that Tube Lines was entitled to additional payment for these features. However by the time this decision was made significant time and resources had been lost on this particular piece of work.

(c) Station supervisors regularly prevented Tube Lines from gaining access to which they were entitled, resulting in successful claims for over £12 million. They have also made unreasonable demands in return for access. For example, Tube Lines’ workers were denied the use of the station’s car park to facilitate upgrade work being carried out at the station. The station manager only agreed to the use of the car park on the condition that Tube Lines provided:

(i) an air conditioning unit and blinds to his office;
(ii) new double gates to the main car park entrance; and
(iii) two posts in the car part to prevent cars reversing into the wall mounted air conditioning unit.

Since Tube Lines could not undertake the work at the station without a place to receive delivery of materials it had little choice but to give in to these out-of-scope demands.
22. These are just a few examples of approach taken in parts of London Underground, which has not significantly changed since the collapse of Metronet. This does not mean the PPP Agreement cannot work; despite these instances, which do make it more difficult for Tube Lines to meet its contractual obligations on time and within budget, it is still delivering its commitments at a lower cost than Metronet (see attached tables).

**How has the upgrade work progressed since the demise of Metronet?**

23. Since the demise of Metronet, Tube Lines has continued to make significant progress on upgrade work, such as track refurbishment, station refurbishment, escalators, lifts, signalling, train performance and fleet reliability. However, London Underground has repeatedly required Tube Lines to carry out additional upgrade work beyond the scope of the PPP Agreement, prevented Tube Lines from carrying out works according to its plans, and hindered Tube Lines from executing the delivery of work which it is contractually obliged to do. Tube Lines believes that there are a number of London Underground issues in terms of their role which are detrimental in relation to upgrade work, including their approach to granting necessary closures, their requirement for bespoke software system features, and the difficulties encountered by Tube Lines in working with London Underground operational and assurance procedures, all of which have significantly extended the time that projects take, as well as the costs involved.

**Achievements to Date**

24. Since the start of the PPP Agreement, Tube Lines has completed the upgrade and refurbishment of 72 of the 96 stations along the Jubilee, Northern and Piccadilly lines it is responsible for under the PPP Agreement. 13 stations are currently being worked on with work on the remaining 11 due to start later this year. Tube Lines has completed 76 lift and escalator refurbishments across the three lines. Seven refurbishments have been done on the Jubilee line, 31 have been completed on the Northern line and 15 on the Piccadilly line. A further 23 have been undertaken at three stations which straddle more than one of the three lines. Step-free access work has been completed at nine stations and is currently underway at a further four stations. During this time Tube Lines has been able to further improve its safety injury rate from 1.40 in 2003 to 0.04 in 2009.

25. These achievements also, however, involved material additional expense as a result of London Underground’s having increased the scope of the works that it required and changing the way in which it required Tube Lines to carry out the work, in spite of the fact that the PPP Agreement contained a fixed scope of works albeit one that was loosely defined, thereby allowing London Underground to add additional requirements, at a cost, once it had been agreed. In addition, London Underground hindered Tube Lines’ ability to carry out the works required by the stations programme by failing to comply with its own obligations under the PPP Agreement.

26. Despite the Northern Line being in a worse state than anticipated at transfer, Tube Lines has replaced track, upgraded stations and signalling, used predictive maintenance techniques, improved train management systems and overhauled train doors. These changes have resulted in a 49% reduction in delays caused by infrastructure, a 10% increase in customer satisfaction levels and enabled the line to operate 98% of its 12 million scheduled kilometres annually as opposed to less than 90% when the line was at its worst. London Underground worked closely with Tube Lines on this improvement, in particular, implementing improvements to the timetable. This is a really good example of what can be achieved when both parties work in partnership as the PPP Contract envisaged.

27. Since the demise of Metronet, Tube Lines has continue to focus its efforts on delivering its work on time and within budget, with a particular emphasis on completing the Jubilee line upgrade and leveraging the experience gained on that project to start the Northern line upgrade. Significant progress has been made on the Jubilee line. Although Tube Lines will now not meet the 31 December 2009 deadline to deliver the project, the level of progress that has been achieved to date is such that the overrun in the project will be limited in time and the costs of any delay will be carried by Tube Lines and not passed to the taxpayer.

28. The upgrade work on the Jubilee line has been carefully planned with a need for it to be carried out in a particular order over the life of the project. To facilitate this Tube Lines has asked for a total of 118 partial or whole line closures since 2002. Although Tube Lines was granted 113 closures, only half of these were at the times and locations we asked for and needed to carry out the work according to plan. While it was possible to undertake work during the closures we were given, it was not possible to do the work according to the long-term plan with the resulting need to reorganise, reschedule and review at short notice, which has not allowed us work as efficiently or effectively as we can.

29. It is difficult to tell how this upgrade work compares to work being undertaken on the Metronet parts of the network. While Tube Lines’ reporting and information provision (both to London Underground and to the Arbiter) on the projects is clear, no comparable, independently-verified, evidence is available showing the progress that London Underground is making on the lines it now has responsibility for. Tube Lines considers that such information should be made available.

30. Tube Lines’ and its costs have been independently benchmarked and are costs across the board have been demonstrated to be between 20–50% less than Metronet’s during 2008–09 when it was under the direct control of London Underground. (charts are included as appendices).
What contractual arrangements are appropriate for the future?

31. One of the primary purposes of a PPP arrangement is the injection of private sector due diligence, management and risk management. Treasury studies have shown that, while there are inevitably some exceptions, such as Metronet, the vast majority of such projects perform better than traditional government procurement in terms of on-time and on-budget delivery. In essence, the PPP model is a robust and flexible one, which, when run effectively, continues to be an efficient approach to delivering the much needed upgrade to the network.

32. Under the PPP Agreement, Tube Lines is obliged to meet particular service output targets (including journey time capability and service consistency and service control) and in doing so upgrade and enhance the network to make sure that these key targets are met. In order for the PPP Agreement to operate as effectively as possible, it is also necessary for London Underground to adopt an approach that is consistent with the scheme of the PPP Agreement and its output-based nature under which Tube Lines’ obligations are based on output targets which give flexibility for Tube Lines to determine the methods of achieving those targets, subject only to overriding criteria governing safety. Such a scheme, in combination with Tube Lines’ structure of independent management and no tied supply chain, gives rise to the economic and efficient day-to-day performance of the company.

33. The NAO report clearly states that Tube Lines’ project management has delivered results. Appendix Five, section C, which compares Metronet and Tube Lines’ differing approaches to addressing problems clearly shows that Tube Lines’ strong stand enforcing its interpretation of the contract and its proactive approach to project management and to reducing the complexity of its own organisation, has improved efficiency and output and resulted in an operation that it is better placed to deliver results. This Committee also recognised this fact, stating that Tube Lines “provides an example of private sector innovation and efficiency”.

34. While the PPP Agreement is not perfect, Tube Lines’ delivery under it demonstrates that it can offer an example of a contractual arrangement that can deliver what is contractually required on time, to budget and to the quality levels one would expect if given real and meaningful support by London Underground.

35. Tube Lines believes that an alternative model for the management of risk is possible which would benefit all parties including London Underground and the taxpayer and it has, therefore proposed an alternative approach to the PPP Arbiter and to London Underground.

What risks, if any, are associated with the PPP Agreement with Tube Lines?

36. We believe that the PPP agreement is robust and is delivering a good value service for London. This is because of a robust corporate governance structure and management of risk. Greater acceptance of the structure of the PPP and wider take adoption of the approach taken on the Northern line would only enhance this.

What impact is the current economic situation having on transport PPP and PFI schemes and what are the financial implications for other transport schemes?

37. Current financial market conditions have deteriorated significantly since the summer of 2007. There are few transactions that have closed in the last year that can be considered appropriate for comparative purposes. However, financing costs even for simpler and smaller PPP projects than represented by Tube Lines are significantly higher than the levels that applied at the time of either Tube Lines’ initial financing in 2002 or its refinancing in 2004.

38. In the current financial market, the complexity that was introduced in the 2004 refinancing, combined with the general complexity of the PPP Agreement itself, would result in a “complexity premium” as it would be likely to deter investors who would not be willing to spend the time required to understand the project and the financing structure.

39. Therefore, any financing raised in the current market would be likely to be substantially more expensive than the existing financing that Tube Lines has in place.

October 2009
BENCHMARKED COST COMPARISON CHARTS
TUBE LINES AND METRONET 2008–09

08/09 Comparison

Fleet maintenance cost per car

08/09 Comparison

Track maintenance cost per km
08/09 Comparison

Lift maintenance cost per machine

<table>
<thead>
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<th>Line Name</th>
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<th>Average</th>
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<td></td>
</tr>
<tr>
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<tr>
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<td></td>
</tr>
<tr>
<td>Northern</td>
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<td></td>
</tr>
<tr>
<td>Piccadilly</td>
<td>£0</td>
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08/09 Comparison

Signal maintenance cost per km

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<td></td>
</tr>
<tr>
<td>Northern</td>
<td>£20,000</td>
<td></td>
</tr>
<tr>
<td>Piccadilly</td>
<td>£0</td>
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</tr>
</tbody>
</table>
08/09 Comparison

Stations maintenance cost per m2

Escalator cost per machine
Memorandum from the National Union of Rail, Maritime and Transport Workers (RMT) (UPP 05)

The National Union of Rail, Maritime and Transport Workers (RMT) welcome the opportunity to respond to the Transport Select Committee inquiry: Update on the London Underground and the Public Private Partnership (PPP) agreements. The RMT is the largest of the unions on the London Underground; our opposition to the PPP is well documented.

The PPP lurches from crisis to crisis, as report after report is published highlighting the structural and operational problems with the scheme. Without exception all of the reports and their recommendations are ignored by Government Ministers who continue to blithely insist, in the best Panglossian fashion, that all will be for the best, in the best of all possible worlds.

In all the discussions about the PPP, it is often forgotten that London Underground’s (LU) infrastructure is groaning under the weight of record passenger numbers and is in desperate need of renovation. Despite recent falls in ridership due to the recession, London’s population will increase by around 500,000 over the next decade. Many of these people will use the Tube. In addition the 2012 Olympic and Paralympic Games will place the network under huge strain.

It is therefore essential that the right lessons are learnt from the disastrous PPP experiment and a competent public sector structure put in place to provide the basis for clear lines of management accountability, effective strategic planning and sustained investment streams to deliver the necessary upgrade of the infrastructure. As part of the process by which engineering functions are returned to the public sector, RMT believes that Transport for London should create a major works department that could be utilised in their subsidiary organisations including London Underground, London Overground and work on the Crossrail project.

Lesson of the Metronet Collapse, the Failure of Private Sector Involvement and the Jubilee Line

In the summer of 2008, Metronet collapsed under the weight of its own inefficiency. At that time PPP defenders rushed to explain the scheme was still structurally sound. Metronet was simply an inefficiently run organisation with an inappropriate governance structure and Tube Lines performance vindicated the sell-off of engineering functions to the private sector. Giving verbal evidence to your committee in the wake of Metronet entering administration, the then Secretary of State for Transport, Ruth Kelly, said she believed that the PPP structure could deliver value for money.15

However, RMT believes that experiences both before and after the introduction of the PPP brings into serious question the assertion made by the Secretary of State. The current mess on the Jubilee Line illustrates our view.

15 Ruth Kelly verbal evidence to Transport Select Committee 7 November 2007.
In the late 1990s, PPP supporters argued that the cost overruns experienced in the Jubilee Line Extension (JLE) project confirmed the inherent failures of public sector project management and provided the rationale for outsourcing the Underground’s engineering functions. In fact, RMT believes the difficulties the project ran into indicates precisely the opposite and demonstrates the financial and operational failings the private sector has caused on the London Underground over the past decade or so.

The signalling contractor working on the extension, convinced London Underground Limited (LUL) management to install a technologically unproven, “moving block” signalling system onto the Jubilee Line. When it became apparent to the contractor that the moving block system would not work and would therefore have to be abandoned, they delayed telling LUL of the engineering problems the project had encountered. The failure of the private contractor was confirmed by the then Deputy Prime Minister (DPM), John Prescott, who explained to the House of Commons on 20 March 1998 “... but, to be fair, London Transport was not to blame for the failure in the signalling system; it was the fault of a private company that did not live up to its contract to produce on time”.

Bizarrely, the DPM identified the failure of the private contractor to fulfil its obligations during the same Commons debate in which he launched the Public Private Partnership. RMT maintains the failure of the signalling contractor should have alerted the Government, at that time, to the potential dangers of wider private sector involvement in London Underground’s engineering functions. That the Government failed to learn the appropriate lesson has led to the waste of billions of pounds in public money and delayed work to upgrade the infrastructure.

Work to resolve the signalling problems caused by the abandonment of the moving block system is now being undertaken by Tube Lines. However, the project is not progressing at all well and once again indicates to the RMT that lessons that should have been learnt after the collapse of Metronet, are simply not being taken on board. Indeed, the recently published 2008–09 Transport for London (TfL) document London Underground and the PPP explains:

“Over the past year the work has advanced and the scale of disruption to customers at weekends has expanded significantly, but progress has been slower than planned. This is evident in the growing requests for additional weekend closures that resulted, in April, with a separate Jubilee Closures Agreement, that provided 12 additional weekends at short notice. This hunger for more closures has stretched stakeholder and customer patience to breaking point, and it is vital that Tube Lines meet their commitment to deliver the upgrade by 31 December 2009. Their reputation—and that of their shareholder Bechtel who is delivering this project—hinges on meeting this commitment”.

To the RMT these comments are all too reminiscent of TfL remarks made in their annual 2005–06 review of the PPP with regard to the upgrade of the Waterloo and City Line. TfL explained at that time “The current closure of the Waterloo & City line for works connected with the upgrade is an acid test of Metronet’s capability to manage major projects”.

As the Committee will know the Waterloo and City Line upgrade re-opened over a week late, exposing Metronet to fines for the late completion of works. The line was subsequently closed twice following the late completion of works due to dust and dirt caused by on-going engineering works which led to train operators experiencing visibility problems.

For the Jubilee Line, RMT understands that the first phase of the current work will not be completed until March 2011 with the whole project overrunning to Quarter 2 of next year. One impact of the delay will be that LUL will have to pay penalties to the Canary Wharf Group caused by the failure of the private contractor to deliver the work on time. No doubt, there will be clauses in the PPP contracts enabling LUL to claw back the money from Tube Lines. However, at the same time as this contractual absurdity is being played out, RMT also understands that Tube Lines has submitted a multi-million pound claim against LUL for “additional works” that were not specified in the original contract. This is precisely what happened with Metronet who claimed that their cost overruns were in part the result of non-contract specified, additional works. LUL had instructed them to carry out.

In the past week, London Underground (LU) seems to have finally lost patience with Tube Lines. Exasperated by the overrun of works on the Jubilee Line acting managing director, Richard Parry has called into question “everything about the PPP” and made a referral to the PPP in an attempt to resolve the on-going dispute over the Tube Lines funding settlement for the next 7½ year PPP period. Given both the experience with Metronet and the evident problems on the Jubilee Line we are extremely concerned that it has taken London Underground so long to act.

The referral further highlights one of the many problems with the PPP. The scheme’s contracts are rightly known as being both extremely complex and shrouded in commercial confidentiality. In our view, complex, multi-billion pound contracts should be subject to the widest possible public scrutiny. RMT therefore shares the view of your Committee’s January 2008 report: the London Underground and the Public Private Partnership Agreements that a mechanism should have been put in place, by amending the Greater London Authority Act 1999 if necessary, to allow the PPP Arbiter to report annually on Infraoco performance whether or not one of the parties had called on him to do so. Government should have taken this step in
the immediate wake of Metronet’s administration; their failure to do so has made public scrutiny and discussion about Tube Lines performance, in the run up to TIL’s referral, more difficult than should have been the case.

Additionally, the structurally flawed nature of the PPP contracts causes unnecessary operational tensions and confusion between LU and the remaining private Infraco. One example is that of a new signalling standard that Tube Lines will not recognise because it was not the standard applied at the time the contracts were signed off. For the Infraco to hold this position is utterly bizarre. The PPP was designed to last for 30 years. During that time virtually every operational and technical standard is likely to be subject to change. Tube Lines’ strict formal adherence to what was originally written down indicates to what the RMT that they are more interested in providing technical solutions to meet financially beneficial capacity, accessibility and ambience targets rather than being committed to running an underground network.

THE TRANSFER OF RISK AND THE IMPACT ON THE UPGRADE OF THE INFRASTRUCTURE

We have consistently made the point that the transfer of revenue risk to the private sector on both the national rail network and the London Underground is wholly inadequate. That the public purse was left to pick up 95% of Metronet debt is unacceptable and brings the London Underground Limited (LUL) national rail network and the London Underground is wholly inadequate. That the public purse was left to upgrade budget. The result of Metronet’s failure is that the public purse could also be exposed to Tube Lines debt should they abandon, for whatever reason, their PPP contracts.

The effects of the 95% clause are already being felt on the ex-Metronet contracts. LUL is struggling with the debt inherited from administration and is therefore seeking to reduce costs. In June 2009, RMT revealed that maintenance work on the ex-Metronet lines was being cut by around £60 million, made up of £26.2 million in track and signal work, £18.9 million from fleet and trains and £18.5 million from the station upgrade budget. The result of Metronet’s failure is that the travelling public and the public purse is being forced to pay twice; firstly by having to pick the huge debt and secondly by facing cuts to vital upgrade work owing to budgetary constraints caused by the debt inheritance.

EFFECTS OF THE RECESSION ON OTHER TRANSPORT SCHEMES

RMT warmly welcomed the Government announcement to electrify the Great Western Main Line. Contained within the announcement was the good news that the Crossrail project would proceed as planned. There had been speculation that funding for the scheme was becoming problematic and that a future Conservative administration might scrap the scheme altogether. Funding now appears to be more secure given the announcement in late September that the Mayor of London has secured a £1 billion loan from the European Investment Bank to pay for the scheme. RMT supports the Crossrail project and believes once it begins operations, passenger services should be run in the public sector. We have already mentioned in this submission the creation by Transport for London of a major works department to work on schemes such as Crossrail.

September 2009 saw stations from the South Central franchise transfer to Transport for London as part of the East London Line extension project. The ELL will re-open next June. In order to complete the orbital London Overground network we are keen to see work begin on Phase 2 of the project at the earliest possible time.

THE ROLE OF GOVERNMENT

Government has not played a positive role during the history of the PPP. Ignoring the opposition of the rail unions, the then mayor of London, your committee and the vast majority of passengers, it pressed ahead with the scheme; a decision that has proved to be disastrous. The best course of action the Government can now take is to bring forward legislation at the earliest possible time to return all privatised services, including out-sourced cleaning services, back under London Underground control. Such a move would restore a clear line of management accountability, enable strategic planning across the whole network and provide the basis for sustained investment to deliver the necessary upgrade of the infrastructure.

CONCLUSION

As stated above a number of independent reports have emphasised the failings of the Public Private Partnership. Sadly these have not been heeded by Government and the taxpayer has been forced to account for 95% of the cost of the failure of Metronet to fulfil its obligations under the PPP contract. This has resulted in important maintenance work being cut back which ultimately will see a deterioration in service at the expense of ordinary passengers.

It is of real concern that similar problems with the upgrade of infrastructure have started to occur with Tubelines in respect of the Jubilee Line. The difficulties being experienced with Tubelines, and in particular Tubelines insistence that work in the next funding period will cost far more than London Underground consider reasonable, has resulted in London Underground losing patience and making a referral to the PPP Arbiter over funding.

This is not a sound basis for moving forward with the essential upgrade of the infrastructure, especially with the numbers of people using the tube expected to grow significantly in the next 10 years. RMT believe that the upgrade of the infrastructure should be returned to London Underground and public control and accountability. As we have demonstrated this will be the most cost effective solution and will end any further contractual disputes with Tubelines, and the consequent waste of resources that this involves.

October 2009

Memorandum from Transport for London (TfL) (UPP 06)

1. INTRODUCTION

1.1 Transport for London (TfL) welcomes the opportunity to comment on the Committee’s update inquiry into the London Underground Public Private Partnership (PPP). Our response provides an update on performance of the PPP and significant developments since the submission of TfL’s evidence to the Committee’s previous inquiry in 2007.

2. BACKGROUND

2.1 TfL was created in 2000 as the integrated body responsible for the Capital’s transport system. The primary role of TfL, which is a functional body of the Greater London Authority, is to implement the Mayor of London’s Transport Strategy and manage transport services across the Capital. London Underground (LU) became part of TfL in 2003 and is responsible for operating the LU rail network. It serves 270 stations and operates services on 11 lines. Up to four million passenger journeys are made on the network on the busiest days.

2.2 Metronet was previously responsible for the maintenance and upgrading of eight of LU’s 11 lines under two of the original three PPP contracts, for the BCV (Bakerloo, Central, Victoria, and Waterloo & City lines) and SSL (“sub-surface” or Circle, District, Hammersmith & City and Metropolitan lines) infracos. After Metronet collapsed and entered PPP Administration in July 2007, TfL emerged as the only bidder for the two Metronet companies, and they transferred to TfL ownership in May 2008. Subsequently all former Metronet staff transferred to LU in December 2008. An organisational review of central support functions across LU, designed to eliminate duplication and deliver the most efficient structure, was then carried out, and a new integrated LU structure was put in place with around 1,000 jobs removed.

2.3 Tube Lines remains responsible for the maintenance and upgrading of the JNP (Jubilee, Northern and Piccadilly) lines under its PPP Contract. The first Periodic Review of this contract is currently in progress (see section 4 below).

2.4 2008–09 was LU’s best ever year in terms of operational performance and customer satisfaction ratings, despite also carrying more passengers than ever before—nearly 1.1 billion during the year, almost as many as the entire National Rail network. A table summarising operational performance in the past six years is at Appendix 1.

2.5 The current economic downturn has since led to a reduction in ridership (around 5–6% so far this financial year) which has had an impact on LU’s revenue. Overall, however, passenger numbers still remain higher than they were five years ago and demand is forecast to continue to grow by around 25% over the next 10 years or so. Delivery of the current investment programme, the largest seen on the Tube in decades, therefore remains essential, in order to deliver the capacity and reliability improvements needed to accommodate this growth. The line upgrades that are at the core of this investment programme will deliver approximately 30% more peak capacity by 2020.

2.6 Given the constraints on funding that have resulted from reduced revenue and the financial legacy of Metronet (see section 3) it is also imperative that this investment is delivered efficiently and economically, providing fare payers and tax payers with the best possible value for money.

3. THE COLLAPSE OF METRONET

3.1 TfL’s submission to the Committee’s previous inquiry was made while Metronet was still in Administration, but even at that time it was possible to identify the root causes of its failure, which were a fatal flaw in Metronet’s structure and its contracting strategy, which committed it to using its own shareholder companies.

3.2 The National Audit Office (NAO) report on the failure of Metronet, published in June 2009, confirmed TfL’s long held view that Metronet’s failure was the result of the failure of its management team and shareholders to properly plan, manage and execute its work. The NAO report also noted that Metronet was effectively managed by LU once it entered administration.

3.3 Since Metronet transferred to TfL and was integrated into LU, maintenance performance has improved and good progress has been made with the two major line upgrades currently in progress on the ex-Metronet lines—the Victoria line upgrade (VLU) and the upgrade of the sub-surface lines (SSL upgrade).
3.4 On the BCV lines in 2008–09, overall Availability—the key measure of day to day asset reliability under the PPP contracts—was 27% better than the contractual benchmark, with a 30% reduction in the total number of Lost Customer Hours (LCH)\(^7\) compared to 2007–08. Further evidence of the turnaround in BCV performance since the administration is a 21% decline in the average number of LCH per period.

3.5 On the SSL lines in 2008–09, overall Availability was 35% better than the contractual 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. An example of the improvement in the delivery of maintenance and renewal works is that LU’s recent delivery of ballasted track renewal works on the District line has set new records for the amount of track being replaced during a weekend possession—on 12–13 September 2009, 812 metres of track were replaced, more than has ever been achieved before.

3.6 Additionally, both the VLU and the SSL upgrade are progressing well—the first of the Victoria line’s new trains is now running in service, having done so for the first time in July 2009, while the first of the new “S-stock” air-conditioned trains for the sub surface lines is currently in the final stages of testing at LU’s test track at Old Dalby and is due to be delivered to London in October 2009. LU has also initiated the tender process for the vital new signalling system on the sub-surface lines, adopting a fresh approach to the procurement process that seeks to utilise the knowledge of the supply market to deliver the best possible value for money. This will offer savings of hundreds of millions of pounds compared to the contract that previously existed prior to Metronet’s collapse and which was terminated prior to transfer to TFL.

3.7 LU has also had to deal with the financial legacy of Metronet’s collapse—the result of poor programme management and system integration, ineffective cost control, a lack of forward planning and inefficient fiscal management. Although initial estimates from the NAO report put the loss to the taxpayer of Metronet’s failure at between £170 million and £410 million, this does not take into account work left undone by Metronet which LU has addressed since transfer or which still needs to be completed by LU in the future.

3.8 Through rigorous review of the Metronet businesses, LU has been able, through renegotiation of contracts, improved procurement, operational efficiencies and a revised work programme, to remove approximately £2.5 billion of projected costs from the budget to 2018, compared with the costs that Metronet would have incurred.\(^8\) As part of this, LU is currently making further savings in maintenance operations designed to deliver £60 million of efficiencies per year, on top of the savings made as a result of the organisational review mentioned in paragraph 2.2 above.

3.9 After Metronet exited from Administration, TFL worked closely with the Government under the auspices of the Joint Steering Committee (JSC) which was set up to examine and make recommendations on options for a long term structure to deliver Metronet’s former contractual obligations. The JSC’s report is currently the subject of discussions between the Secretary of State for Transport and the Mayor of London.

3.10 A more detailed analysis of all these issues is contained in LU’s PPP Report 2007–08 and PPP & Performance Report 2008–09, both of which are available on TFL’s website at www.tfl.gov.uk/ppreport. LU remains committed to regular and transparent reporting of performance and has recently commenced publication, at the same website address, of a four-weekly digest of performance data that complements the annual reports. Other material is also presented publicly to the TFL Board.

4. TUBE LINES AND PERIODIC REVIEW

4.1 TFL’s previous submission in 2007 noted some of the achievements of Tube Lines’ renewal programmes at that time, and it has continued to show some success since then, particularly in its stations programme which is on course to deliver, by the end of the first contract period next year, modernisation or refurbishment of all its stations as envisaged in the contract. It has also showed more consistency in day to day maintenance performance, and has turned around the performance of the Northern line after early difficulties, although the intrusive upgrade programme on the Jubilee line is reflected in a decline in Availability scores on the line in the past two years.

4.2 It is, however, in the delivery of that upgrade of the Jubilee line that Tube Lines faces its biggest challenge. Currently, it is failing to meet that challenge. This is the first of the major line upgrades, and will deliver a 33% increase in capacity as a result of the installation of a new signalling system. TFL has recently expressed its grave doubts about Tube Lines’ ability to deliver the upgrade by the contracted date of 31 December 2009. Tube Lines Chief Executive has also indicated that “we don’t think we will quite get there in December”. At time of writing, the outcome of the independent review of Tube Lines’ programme (which they agreed to undertake after being urged to do so by LU) is urgently awaited, but it seems likely to indicate not only that delivery will be delayed, but also that more weekend closures will be needed.

\(^7\) Lost Customer Hours (LCH): The total additional journey time measured in hours, applying Nominal Accumulated Customer Hours (NACH), experienced by Customers using the Underground Network as a result of Service Disruptions.

\(^8\) More detail is available in the report considered by the TFL Board on 24 June 2009, and published on the TFL website at http://www.tfl.gov.uk/assets/downloads/corporate/Item08_Metronet-Integration-Budget-Implications.pdf
4.3 Tube Lines’ lack of progress is particularly disappointing given the extent of closures that have been necessary—part of the line has been closed on every weekend in 2009 and the number of closures has been significantly more than the number originally planned for at the start of Tube Lines’ programme. These closures are causing considerable disruption to passengers and to businesses who depend upon the line.

4.4 The first Periodic Review of Tube Lines’ 30 year contract is currently in progress. This will determine the scope and the price of Tube Lines’ work programme for the second 7.5 year contract period commencing in July 2010.

4.5 In 2008 LU requested initial Guidance from the PPP Arbiter as to the likely cost of the works for the second period based on the original PPP contract terms. The PPP Arbiter’s Guidance issued in September 2008 (and therefore in 2008 prices) estimated that the total funding required in the second period should be in the range £5.1 billion to £5.5 billion compared with Tube Lines’ estimate of £7.2 billion and LU’s estimate of £4.1 billion.

4.6 LU broadly accepted the PPP Arbiter’s Guidance and then, in finalising its Restated Contract Terms, made a number of further adjustments to reduce the costs of the second period whilst ensuring that the full upgrade programme can be delivered. The re-stated terms did not therefore substantially change the work to deliver major increases in capacity and reliability through new trains and new signalling. However, projected costs have been reduced significantly by LU by, for example, proposing station refurbishment broadly every 10 years as opposed to the seven and a half year cycle in the current contract. The restated terms also reflected changes that had occurred in the economic situation since the request for Guidance.

4.7 LU’s revised evaluation of costs was £4.2 billion. This is not directly comparable to the previous valuation of £4.1 billion—it is coincidence that, after the process of making revisions to scope, and other adjustments as described above, these figures are similar.

4.8 LU issued its Restated Contract Terms to Tube Lines in December 2008. Tube Lines responded to the restated terms in June 2009 but its price was significantly in excess of LU’s evaluation and also still much higher than the price indicated by the PPP Arbiter in his initial guidance last year, which Tube Lines appears not to have taken into account.

4.9 Since receipt of Tube Lines’ response, LU and Tube Lines have made some progress in determining the future work programme and in reducing some costs accordingly. However, Tube Lines’ costs still remain unacceptably high in some areas and LU therefore referred the issue to the PPP Arbiter on 23 September 2009, asking him to set a fair price for the works. LU intends to continue its constructive discussions with Tube Lines, alongside the PPP Arbiter process. It is anticipated that the Arbiter will publish his draft conclusion on second period costs in December 2009.

4.10 Tube Lines has also produced an “alternative proposal”, outside of the Periodic Review process.

4.11 This alternative proposal, currently only at a very outline stage, has been reported as offering a price of around £4.3 billion. However, it is important to make clear that this figure is not directly comparable to LU’s evaluation of £4.2 billion. Tube Lines’ proposal excludes some very significant elements of the work programme for the second contract period, yet still remains above LU’s view of the costs. It also specifically removes the requirement for Tube Lines to remain “economic and efficient” in that LU would become liable for bearing the larger proportion of cost overruns on Tube Lines’ programme, however these were incurred. In effect the proposal seeks to re-engineer the PPP structure which would create significant legal and practical issues. Even if these could be resolved, such fundamental changes would be likely to take significant time and resource to implement.

4.12 Although LU will actively engage with Tube Lines on this, and on any other proposals that may reduce costs, LU’s priority is to see that Tube Lines delivers all the improvements it has promised on time, and that it offers a fair price for the scope of works that LU has specified for the second contract period, such that it delivers value for money for fare payers and taxpayers.

5. Conclusions

5.1 Metronet’s failure was largely the result of its own inefficiency rather than a consequence of the PPP structure. However, the legacy of Metronet’s collapse, and the improved performance delivered since its activities were integrated into LU, has inevitably raised questions about whether an alternative model may be more effective at delivering the improvements and, crucially, may offer greater efficiency and value for money than the PPP was able to deliver.

5.2 As the one remaining PPP contractor, it is on Tube Lines’ shoulders that the case for the PPP model now rests. If the case is to be made, then Tube Lines must resolve the delays to the Jubilee line upgrade and complete that work promptly; and deliver a proposition with costs that offer value for money for the second contract period.

5.3 TFL’s objectives in relation to the former Metronet activities now under LU’s control are reliable day-to-day performance and efficient delivery of the upgrade works, in order that the service and future capacity that London depends upon is achieved for the best possible value for money. LU has so far demonstrated it has the capability to achieve that, and it is committed to continue to ensure that its activities are transparent and open to scrutiny so that its ongoing performance in this respect can be assessed.
APPENDIX 1

LU OPERATIONAL PERFORMANCE 2008–09

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October 2009

Supplementary memorandum from Transport for London (TfL) (UPP 06a)

I am writing further to the evidence that Richard Parry and I gave to your Committee on 9 December 2009. In the light of subsequent events and evidence from other witnesses, I think it is important to clarify and expand on a number of issues.

1. Tube Lines’ Costs

It was suggested by a number of other witnesses that Tube Lines’ costs for maintenance and upgrade work are, and will continue to be, less than those of London Underground (LU). However, this is not substantiated by any objective analysis of the available information.

As Richard Parry pointed out on 9 December, it is important to make meaningful comparisons, taking into account amongst other things the position inherited from Metronet and the nature and condition of the assets. I enclose a paper considered on 10 December 2009 by the TfL Board which sets out a more detailed analysis of this issue. You will note the conclusion that, notwithstanding the legacy of Metronet’s inefficiencies, LU has subsequently achieved significant efficiencies and costs reductions, and that its projected costs going forward are comparable with or better than Tube Lines.

The latter point is salient. Since your Committee met, the PPP Arbiter has published his Draft Directions on Tube Lines’ costs for the second contract period. He effectively rejected Tube Lines’ evaluation of the costs; his draft determination is that the economic and efficient price for improving the Tube over the seven and a half years from mid-2010 to 2017 should be £4.4 billion, rather than the £6.8 billion originally sought by Tube Lines, or the £5.75 billion they subsequently reduced their evaluation to.

The Arbiter’s determination is much closer to LU’s evaluation of £4.0 billion.

Clearly LU will be working with the relevant parties ahead of the Arbiter’s confirmation of his directions in March 2010 in order to address any funding shortfall that remains at that time. However, I remain of the view that any additional cost to LU over and above its budgeted costs should be met by Government, who imposed the PPP structure on London, in order to ensure the vital improvements in Tube reliability and capacity promised by the PPP can be delivered in full.

2. Jubilee Line Upgrade

The TfL Board also considered a PPP Update paper on 10 December 2009, which among other issues sets out the latest position on the Jubilee line upgrade. This is enclosed.

You will see that the paper highlights the importance of Tube Lines setting out, and then adhering to, a credible programme for completion of the upgrade. We have agreed a further closure programme up to Easter 2010, which was published on 11 December—the press release is enclosed. However, Tube Lines require further closures beyond that, and have recently indicated that they will not complete the upgrade until October 2010.

Tube Lines originally predicted a requirement for around 50 weekend closures to deliver the upgrade. To date, they have required around 120 weekend or part-weekend closures and have still been unable to complete the work. Repeatedly last year we were assured that granting a further 12, then a further six, closures was all that was needed. They have now confirmed they need 13 more weekends up to and including Easter and that this will still not be enough.

Tube Lines also need to make clearer what the impact of the delay will be on the programme for the Northern line upgrade, which is intrinsically linked to that of the Jubilee line.

The reasons for the delay to the Jubilee line upgrade are, I know, not the subject of this inquiry. However, I would re-iterate the point made by Richard Parry on 9 December, and echoed by Chris Bolt on 6 January, that the Bechtel secondment arrangements put in place by Tube Lines to manage delivery of the upgrade do not appear to have been effective in this instance.
It was suggested by some of the witnesses that LU’s own staff training needs could mean further delays to the Jubilee line upgrade delivery date and it was also suggested that LU’s staff training programme was not satisfactory. I would like to place on the record that neither of these allegations has any substance. Training of staff has always been an integral part of the upgrade programme and was factored in to the original overall timetable for delivery. It is not the cause of any delay, nor is it the principal reason for further closures in 2010. It is being carried out comprehensively for all staff, in accordance with industry best practice. LU will ensure that all of its staff receive appropriate training within Tube Lines’ delivery timeframe, as was always envisaged when the PPP contracts were put in place.

3. LU’S APPROACH TO THE CONTRACT

It is false to suggest, as some have, that Tube Lines’ inability to deliver on the Jubilee line upgrade and its inflated cost demands for the second period have anything to do with LU’s behaviour as a client. The Arbiter made clear in his evidence to the Committee that he has, in some areas, taken the nature of the relationship between LU and Tube Lines into account. Yet the simple fact is that his draft direction has still rejected Tube Lines’ view of what the costs for the second period should be.

There were some specific allegations about access and scope made on 9 December. The bottom line on access is that LU has at all times complied with the access code in the contract, and indeed has gone beyond it—witness the recent granting of many weekend closures at short notice. The root of the problem has been that, despite having had more than double the number of closures they originally estimated they would need, Tube Lines is still not anywhere close to delivering on its obligations to upgrade the Jubilee line.

Dean Finch also noted that the allegation that LU had sought to unilaterally vary the scope of some projects, particularly to provide step free access to stations, was not representative of the current situation. I am grateful for that, but in fact it is incorrect to state that LU has ever sought to “not pay” for work done. This is a misrepresentation of what are simply normal contractual negotiations around the scope of works, which would happen under any contract between a responsible public sector client and a private sector contractor. Taking step-free access as an example, obligations were set out in the contract and any work beyond that, such as the current lift construction at Kingsbury and Green Park, is paid for entirely separately as additional work.

4. THE ROLE OF THE PPP ARBITER

It was suggested on 9 December 2009 that we have rejected a suggestion that the Arbiter should have a stronger role, and indeed that Tube Lines are seeking this. Neither of those contentions is correct.

Any contractual change to the Arbiter’s remit, to encompass an annual review of Tube Lines’ programme, would require Tube Lines’ consent. It is arguable in any event whether an annual review would assist in identifying issues at a time when there is still a chance to rectify them. When the Arbiter was asked to give his Guidance last year on notional costs for the second contract period, it might reasonably have been expected that the information provided by Tube Lines about its costs for the second period would reveal the current position on the Jubilee line upgrade. It did not.

On the issue of the Arbiter conducting “Periodic Reviews” of the BCV and SSR infracos in parallel with that of the Tube Lines contract, this is not something which either Tube Lines or the Arbiter has sought during the current process. In any event, it is not clear what the benefits of such an exercise would be. LU’s costs are (unlike Tube Lines’) published in four weekly reports—see www.tfl.gov.uk/pppreport—and crucially, subject to the same governance and scrutiny mechanisms that cover all of TfL’s activities. Additionally, I have recently agreed with the Secretary of State that, going forward, there will be scrutiny of the whole TfL investment programme by a new panel of expert independent advisers—see http://www.tfl.gov.uk/assets/downloads/management-of-tfl-investment-programme.pdf for more details. This will give added assurance to me and to the Government.

In the light of this, an academic and costly review process by the Arbiter is neither a necessary nor an efficient measure.

In effect, the Arbiter already has wide information powers and preparatory powers that enable him to monitor and examine both Tube Lines’ and LU’s programmes—we undertake joint benchmarking and the Arbiter’s reporters will be reviewing LU and Tube Lines data to assess it for accuracy and consistency.

I hope this information is helpful and I look forward to reading the Committee’s report.

January 2010
Memorandum from the Department for Transport (DfT) (UPP 07)

Q1. What lessons can be learned from the collapse of the London Underground PPP Agreement with Metronet?

The collapse of Metronet was a major disappointment for both farepayers and taxpayers. Some essential capacity enhancements and improvements in maintenance, promised through the PPP contract arrangements, will now be late in arriving on the ex-Metronet lines.

There are many lessons to be learned from Metronet’s failure. But it would be wrong to conclude that one is that the concept of the PPP itself is flawed. The National Audit Office’s June 2009 report “The failure of Metronet” was clear that the main cause of Metronet’s failure was poor corporate governance and leadership rather than the PPP contract mechanism.

The interim Managing Director of London Underground Ltd (LUL), Richard Parry confirmed at the London Assembly Transport Committee on 3 September 2009 that Tube Lines has so far delivered largely to time and budget. It has done so by managing higher costs in some areas (stations) by securing efficiencies in others (escalators). Tube Lines continue to work closely with LUL within the contract structure to actively manage delivery challenges, such as the upgrade of the Jubilee line. Where key deadlines or outcomes fail to materialise, Tube Lines will bear the cost of this through reductions in Infrastructure Service Charge. Despite Metronet’s failure, PPP contracts have the capacity to deliver when parties engage constructively within the contract framework.

Furthermore, while the performance of Metronet was clearly unacceptable, its failings should be considered against the background of previous experiences of cost overruns and delivery slippage on the London Underground. The Jubilee line extension and Central line upgrade both presented the taxpayer with cost overruns of 30% and were significantly behind schedule, some six years in the case of the Central line upgrade. By comparison, and using the NAO’s own methodology, the cost to the taxpayer generated by Metronet’s failure lies somewhere in the range of 4–10% against the total value of the investment.

The Department remains committed to a process of continuous review and improvement. Lessons learned from the establishment and implementation of the PPP and other PFI contracts have fed a continuous process of development in DIT and across Whitehall.

Central standardised PFI contract terms are now mandated for departmental use. This has enhanced and systematised the rights of contracting bodies with regard to:

- contract monitoring;
- changes in project documents and financial arrangements;
- maintenance and access to contractor’s records—extending rights to access sub-contract details and information provided to Senior Lenders; and
- managing contractor distress.

The application of these lessons to the recent M25 Widening PFI translate into:

- a Secretary of State right to appoint an observer to the DBFO Co (decision making) Board and therefore has the ability to monitor the financial performance of the company on an ongoing basis;
- the provision of an annual certificate of compliance to the Secretary of State;
- a requirement for a detailed quality management system for the whole supply chain;
- a mandatory value for money criteria for all maintenance works (with any over £10 million requiring a competitive tender);
- detailed record keeping based on open book accounting principles;
- a specified range of events triggering Expanded Interim Project Reporting (potential default, cost overruns, distress indicators, profit warning, etc);
- a Secretary of State right to require the DBFO Co to prepare and implement a Remedial Action Plan on any area which he believes is inadequate, unsatisfactory or failing;
- payments are made to the DBFO co based on the performance of the motorway. These payments increase as key stages of the widening are delivered. Hence if the contractor does not deliver according to the contract the payment is withheld; and
- in addition, the absence of underpinning of the debt financing by the Department during the construction period means that the bank lending is fully at the lenders risk for delivery failure.

Turning to the particulars of Metronet, it is clear from the company’s demise that one of the chief problems facing interested parties—Metronet itself, shareholders, lenders, LUL, the Arbiter and the Government—was the lack of, or the poor quality of, information flowing between them. This meant that the scale and nature of the problems confronting Metronet became known too late in the day for effective remedial action to be taken.

We are, therefore, taking steps to ensure that, across the Underground investment programme, information on progress of projects and economy and efficiency is available early enough for problems to be picked up and addressed.
The National Audit Office report on the failure of Metronet suggested that LUL should not have had to go to the Arbiter to get hold of cost/performance information and that it should have been able to request it directly from the infraco. There will have been some commercially confidential information, which it would not be appropriate for the infraco to share directly with LUL—that is why the Arbiter is there as an impartial source of expertise and guidance. Whilst under the Metronet contracts it was for LUL to manage and request any information it thought necessary, the option of asking the Arbiter for guidance on any matter relating to the PPP agreement was always open to them. It is, therefore, important that each party uses the information that is freely available to them, including the DIT, so that each party can manage the risk to which they are exposed.

The Arbiter, for example, is able to request the infraco to provide any such information as he considers relevant and in that sense the Arbiter does provide assurance on whether the work performed is affordable and value for money and can work with LUL and both parties in analysing the information. He is able to use his powers to the full extent he considers appropriate, such as conduct as detailed an investigation as he thinks appropriate.

With regard to the incentives in place for project funders to ensure contract delivery, we review the approach for each contract based on the nature of that agreement. It should be noted that the circumstances prevailing at the time that the PPP contracts were let meant that the provision of a significant degree of underpinning to the lenders to Metronet was necessary.

Since the award of Metronet contracts, the Department has not provided any similar guarantees to lenders on its PFI contracts and has sought to ensure that the incentives on both equity and debt providers are real and substantive in order to support delivery of project objectives.

As part of the evaluation of PFI contracts, the Department is considering the robustness of the corporate governance arrangements for each contract in the context of the particular contract. The nature of the PPP contracts—in particular the Periodic and Extraordinary Review mechanisms—allowed for significantly greater revisions to contract prices than exist in standard PFI contracts. In the recently awarded M25 contract, there was specific requirement for a detailed Governance Statement that set out the role of the Special Purpose Vehicle and nature of its decision making processes.

Q2. Are these lessons being applied to the London Underground PPP Agreement with Tube Lines?

Tube Lines has so far delivered largely to time and to budget and has had to find innovative ways to do so. For example, while Tube Lines also incurred higher costs in delivering their PPP station programme, they ultimately managed these pressures using contingency funds and by finding offsetting efficiencies in other areas.

Tube Lines greatest challenge to date has been the delivery of the Jubilee Line Upgrade. Complex technical challenges have obliged the company to revise delivery plans and timetables. While disappointing—for LUL if the upgrade is delivered late and at the cost of additional closures, and for the company who face significant abatements to ISC payments—these challenges are now being addressed. Tube Lines are also confident that the lessons now being learned will realise benefits when signalling upgrades on the Northern Line and the Piccadilly line are delivered. While real delivery challenges remain, therefore, the Department’s view is that the PPP agreement with Tube Lines is working in the manner envisaged.

Although the DIT is not party to the PPP Contract between LUL and Tube Lines, with large amounts of government money being invested Ministers and Officials will continue to meet regularly with LUL, Tube Lines and the Office of the PPP Arbiter to monitor progress.

We are also taking steps to ensure that the Review for 2010–17 runs as smoothly as possible and that (within the bounds of propriety and commercial confidentiality, and in view of the fact we are not a party to the agreement) we are kept fully informed by both parties as to developments. The Arbiter set out his proposed timetable for receiving and responding to a reference on cost, and any further references on financing. We indicated to the parties that we considered this a sensible timetable and encouraged the parties to move to an early reference to ensure clarity on costs in good time for the start of Period 2, to minimise cost to LUL and disruption to passengers. We are therefore pleased that a reference has been made at an early stage (23 September). Our liaison with the parties is geared to identifying and understanding where the risks to the taxpayer may be and doing as much as we can (within the constraints of the devolution framework for London, and without being a party ourselves) to ensure these are effectively managed by the contracting and other interested parties.

In the context of the second period review, the Department acknowledges the recommendation in the NAO Report that the Arbiter should be able to highlight issues affecting the taxpayer’s interest. We have, therefore asked both Tube Lines and LUL to consider how the Arbiter’s role can be strengthened and improved to protect the wider public interests. These changes might include increasing the Arbiter’s rights to undertake reviews of PPP programme delivery, economy or efficiency without formal reference by one of the contracting parties. Such changes must, however, as the NAO Report recognises, be agreed by the parties themselves and cannot be applied retrospectively by Government.
Q3. How has the upgrade work progressed since the demise of Metronet?

Since the TSC Inquiry into the PPP Agreements in the autumn of 2007 there has been a considerable progress on line upgrade programmes.

It is LUL’s and TfL’s responsibility to ensure that the former Metronet upgrade programme is delivered to time and budget and that they meet the outcomes in terms of increased passenger capacity and reduced journey time that were specified in the original PPP Contracts.

Examples of progress so far include:

— The TfL run Metronet BCV business is progressing the Victoria line upgrade, which has seen the first new train enter passenger service on 21 July 2009 during limited late night operations in order to grow system reliability. In parallel the new automatic train control and signalling system is being installed.

— The TfL run Metronet SSL business has seen new trains with air conditioning being tested at the Old Dalby test track facility during the summer in order to grow system reliability of the train interface with the upgraded signalling system. The first train is due to be tested on the Metropolitan line in December 2009 with the first train expected to enter passenger service in May 2010. Signalling upgrade works on the Metropolitan line is progressing to schedule.

Metronet’s failure to deliver its station programme has meant that LUL has had to recast the programme and scope of the work and we look to LUL to ensure that this revised programme is delivered in a timely and cost effective manner. Nevertheless work on 124 stations has now been completed, which is a further 33 since the TSC Inquiry of autumn 2007 meaning that 48% of the total has now been completed.

Delivering the upgrades is only part of the story. For passengers using the tube on a daily basis having a reliable journey is key. Perhaps the most important indication on the improved performance of the Network is the availability indicator as recorded in “Lost Customer Hours”, which has been published in “London Underground PPP & Performance Report 2008–09” on the TfL website at http://www.tfl.gov.uk/corporate/modesoftransport/londonunderground/management/1582.aspx. By comparing previous reports we can see that there have been some substantial improvements since Metronet administration and since the PPP commenced as indicated in the table below:

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For 2008–09 the Jubilee line is just below benchmark for the reasons explained above in the problems encountered in the delivery of the signalling upgrade, but all other lines are performing well above benchmark with the exception of the Waterloo & City line, which was due to train defects and signalling issues causing train cancellations. LUL are addressing this with a “hit squad” and already seen substantial improvements so far in 2009–10. One of the most significant improvements can be seen on the Northern line where Tube Lines has spent much of the first period making the infrastructure more reliable, through track replacement and improving the signalling. For the former Metronet lines we can see that for many their performance dipped during the lead up (2006–07) and period in administration (2007–08) as Metronet’s problems crystallised.

Tube Lines are now close to completing the Jubilee line upgrade. The project has presented real delivery challenges and the need for additional closures has been disappointing. We are aware that it has been frustrating for LUL. We have received reassurances from Tube Lines that lessons learned from this project will be applied to upgrades of both the Northern and Piccadilly lines. We look to both parties to agree to innovative solutions to minimise inconvenience to the public in the future.
Q4. *What contractual arrangements are appropriate for the future?*

A Joint Steering Committee consisting of LUL, TfL, DfT and HMT was tasked with considering a range of options for the permanent structure of the Metronet contracts, with the objective of:

- providing a stable and safe operational framework for the Tube;
- delivering the modernisation, upgrade and maintenance of the Tube infrastructure;
- being affordable; and
- delivering Value for Money for the taxpayer.

The Joint Steering Committee has now reported and the Mayor and Secretary of State have accepted its recommendation that the existing Metronet contracts should remain under the direct control of LUL on a permanent basis. LUL will remain responsible for all asset management decisions, but there will continue to be substantial private sector involvement with much of the work carried out through contracts managed by LUL. In detail:

- Existing contracts for the Victoria line upgrade (signalling and rolling stock) and for the Sub-Surface line upgrade (rolling stock) will continue—these contracts were inherited from Metronet (and have been varied).
- A new contract will be awarded for the Sub-Surface line signalling upgrade—an Invitation to Tender was issued this summer.
- The Bakerloo line upgrade is not due to start until 2020. A decision on the most appropriate contracting arrangement will be taken nearer the time, reflecting lessons learnt from both the Jubilee and the Victoria line upgrades.
- Track renewal and civil engineering work (bridges, tunnels, embankments etc) will be carried out through direct procurement with the appropriate form of contract.
- For station refurbishment, LUL will award a new framework contract based on a detailed client specification—offering a degree of risk transfer whilst retaining budgetary control at LUL.
- LUL will retain safety critical maintenance and inspections, among other things, with other line maintenance and station cleaning/facilities management carried out via bundled service contracts.

In awarding new contracts, LUL will include robust performance incentives and transfer risk where appropriate.

The JSC rejected the option of new long-term performance based contracts for the Victoria and Sub-Surface line upgrades as prohibitively expensive. In both cases major contracts for elements of the upgrades are already underway and would either need to be unpicked at great cost of time and money, or passed on to a new delivery partner, limiting their flexibility to innovate and achieve efficiencies and again resulting in a high risk premium. This is not the case for the Bakerloo line upgrade which is still some years off. A long-term performance based contract may therefore be more appropriate for the Bakerloo line upgrade.

The JSC concluded that longer term value for money will turn on LUL’s ability to deliver on time and within budget. LUL has not had direct responsibility for upgrades of this magnitude since the PPP began, and will need to build its capability if it is to improve on its pre-PPP record and deliver major upgrade projects successfully. The Mayor and Secretary of State are considering the most appropriate way to scrutinise the delivery of the ex-Metronet (and other) works in order to protect the public interest.

Q5. *What risks, if any, are associated with the PPP Agreement with Tube Lines?*

The Government is fully aware that the involvement of the private sector cannot always guarantee success, nor that it will deliver innovation, efficiency and economy. However there are also examples when the public sector management of major projects, including LUL in the 1990s, has also been unsuccessful. It is clear that there is no single procurement model or formula for success in delivering major and complex projects, and the appropriate structure must be adopted in each case.

As noted by the PPP Arbiter’s evidence at the TSC in 2007, the private sector can successfully deliver projects when there are clear outcomes specified in the contract and the company is free to decide the approach that it should take to deliver those outcomes. Tube Lines to date has had reasonable success working to the same contract that was applied to Metronet, though with different materiality thresholds, ie the point at which an Extraordinary Review can be triggered with the Arbiter to give a direction on costs.

It is clear that the private sector will continue to be the major force in delivering improvements to the London Underground, whether the contracting mechanism is through the intermediary of the PPP agreement with Tube Lines, or direct with LUL now that they have taken over the contracts with private suppliers that were once Metronet’s.
Under the permanent structure which replaces the Metronet PPPs, LUL intends to continue public reporting of performance and will maintain the PPP performance measures to provide a basis for performance assessment and comparison with Tube Lines. Moreover, LUL undertakes that it and (to the extent practicable) its sub-contractors will make available to the statutory PPP Arbiter such level of information as he requests and requires to assess the performance of Tube Lines.

Part of the Secretary of State and Mayors’ consideration of any new arrangements will be the extent that scrutiny applies across TfL’s investment programme, including management of the former Metronet business, other private sector contracts and those elements of the investment programme delivered in-house (such as some types of maintenance).

Q6. What impact is the current economic situation having on transport PPP and PFI schemes and what are the financial implications for other transport schemes?

The most relevant aspects of the economic situation for transport are falls in passenger numbers and the deterioration of the financial markets. It is also worth considering any potential decline in market interest in PPP schemes.

Fall in passenger numbers: The majority of transport PPP schemes do not include volume risk (ie payment is on delivery of services rather than linked to passenger numbers) and therefore the fall in passenger numbers observed across transport modes is not adversely affecting the performance of PPP deals which are already signed. This is true for the Tube Lines PPP scheme where the charges to LUL are based on infrastructure maintenance and delivery of upgrades.

In a few transport PPPs, such as the M6 Toll and Second Severn River Crossing, traffic risk has been passed to the private sector to manage. We are not aware of any transport PPPs in which the drop in passenger linked revenues is having sufficient impact to destabilise the concession.

Deterioration in financial markets: The deterioration in financial markets has led to much tighter credit conditions and significantly more expensive funding terms. For PPP projects which have already closed, however, there is minimal impact.

New transport PPP projects have managed to raise finance and close since the downturn, notably the M80 in [February], the M25 upgrade in May (which raised £1 billion from EIB and commercial banks) and the Carlisle Northern Development Route in July. Generally however progress to financial close has been slower and final costs have reflected higher funding terms. The higher financing costs have been partially offset by the reduction in underlying interest rates and no transport schemes have been cancelled due to unaffordability or inadequate value for money.

A notable result of the recent financial upheaval has been the withdrawal of the capital (bond) markets from the infrastructure arena and a reduction in the number of banks prepared to commit large sums to long term loans. This has meant that whilst smaller deals can get done with relative ease, larger deals (£500 million plus) have required a combination of EIB and/or strong sponsor support.

Market appetite: There is no evidence that the current economic conditions are having an adverse affect on market appetite for bidding for transport PPP schemes. For construction companies and operators, PPPs represent attractive opportunities in relatively quiet markets. This has been most recently demonstrated by the strong bidding field for the Sheffield Highways Maintenance scheme (with a capital value of over £500 million) which came to the market this summer. There equally does not appear to be a constraint in attracting the equity required to support the financing of PPPs. Over £200 million of contractor equity was raised for the M25 and strong equity bids have been received on the current Inter-city Express Programme and Thameslink rolling stock procurements.

Q7. What role has Government played in these matters?

Government has worked closely with TfL and LUL during the period of Metronet administration to expedite the smooth transfer out of administration of the Metronet companies and above all to ensure the continued safe operation of the tube. The process has also included engagement with the European Commission who needed to consider whether the restructuring (when Metronet’s businesses were transferred to two TfL nominee companies in May 2008) was in compliance with our Treaty obligations. This was a critical step in putting the tube back on a stable footing while work to agree a permanent restructuring continued.

Over the course of 2008, DfT and HM Treasury, supported by Partnerships UK, worked with TfL and LUL to consider the full range of options for Metronet’s permanent structure. Recommendations were then made to the Mayor and Secretary of State who have now accepted that the contracts should continue to be managed directly by LUL on a permanent basis—subject to compliance with our Treaty obligations in respect of state aid. The Government will continue with its discussions with the Commission accordingly.
Alongside this the Mayor and Secretary of State will be considering ways of improving efficiency, effectiveness and economy in the delivery of TfL’s obligations under the former Metronet and ancillary contracts.

We have also considered the future role of the Arbiter who, under the PPP arrangements, will continue to have a pivotal role in driving Tube Lines towards being economic and efficient. While it is of course for London Underground and Tube Lines as contracting parties to manage the Periodic Review process to a successful outcome, DfT has been liaising with all parties to ensure that the process runs as smoothly as possible.

Department for Transport

October 2009

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**Supplementary memorandum from Department for Transport (DfT) (UPP 07a)**

In response to a request from Mr Stringer MP during my oral evidence to the Committee on 9 December 2009, I undertook to provide details of funding London Underground Ltd (LUL) has received from central government, the farebox, the private sector and London’s council taxpayers.

The attached table sets out the sources and amount of funding for the six full years since the introduction of the PPP and so that you can compare, the six years prior to this. I have also included details of the substantial “other revenues” that this public and private sector investment has attracted, including advertising revenues and contributions from developers and other train operating companies. Once inflation has been taken into account, farebox and “other revenue” has increased by over 20% (£2.77 billion).

From 2007–08 onwards the grant to Transport for London (TfL) has not included a ring fenced element for LUL. The figures provided for 2007–08 and 2008–09 are therefore based upon the amounts we expected to be allocated to LUL in these two years at the time of the CSR 2004 settlement.

Mr Stringer also asked how much local tax payer’s money has gone into the Tube. TfL receives revenue from the Mayor’s precept on council tax bills in London, and in their current business plan they forecasts receipts of £12 million a year from this. This does not include a ring-fenced amount for the Tube.

I hope this clarifies the position on funding.
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</thead>
<tbody>
<tr>
<td>DfT Grant</td>
<td>£554m</td>
<td>£313m</td>
<td>£640m</td>
<td>£227m</td>
<td>£518m</td>
<td>£860m</td>
<td>£3.157bn</td>
<td>£3.33bn</td>
<td>£1.146bn</td>
<td>£1.256bn</td>
<td>£1.376bn</td>
<td>£1.744bn</td>
<td>£1.540bn</td>
<td>£8.395bn</td>
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<tr>
<td>Private sector borrowing &amp; equity raised by PPP infraco</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>£281m***</td>
<td>£281m</td>
<td>£281m</td>
<td>£281m</td>
<td>£281m</td>
<td>£281m</td>
<td>£281m</td>
<td>£1.686bn</td>
</tr>
<tr>
<td>Tube Lines</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>£281m***</td>
<td></td>
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<td></td>
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<tr>
<td>Metronet</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>£50m***</td>
<td></td>
<td></td>
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<td></td>
</tr>
<tr>
<td>Other Revenue**</td>
<td>£61.7m</td>
<td>£68.6m</td>
<td>£36.7m</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>£167m</td>
<td>£216m</td>
<td>£196m</td>
<td>£251m</td>
<td>£35m</td>
<td>£235m</td>
<td>£222m</td>
<td>£21.919bn</td>
</tr>
</tbody>
</table>

*LUL only report the total sales revenue in these years so will include “other revenue”.

**Other revenue includes items such as advertising space and capital contributions, eg from Train Operating Companies and developers

***Tube Lines & Metronet’s loans and equity are given an even profile over the first period (7½ years) for Tube Lines and for four years for Metronet. It is for the infraco to determine when spent.

**** The CSR 07 settlement to TFL in these two years and beyond is not ring fenced but the figures provided are the amounts the DfT set out in its agreement for CSR 2004 would expect to be paid to LUL in these years and on top includes the sums following the collapse of Metronet. It is for TFL to determine the precise allocation from all their source of revenue streams. The row also includes grants for the Kings Cross redevelopment project from 2000–01 onwards.
Memorandum from M. Blaiklock (UPP 08)

You may recall my appearance at your Committee on February 27, 2002, as part of the Inquiry into the London Underground PPP. It is interesting to recall the Minutes:

Para 35: (Mr Donohue) “Do you believe that London Underground retains sufficient leverage at this seven and a half year period for the review?”

(Mr Blaiklock) “I am not sure who will have leverage. I think there will be a contractual mess.”

Para 38: (Mr Donohue): “So do we need a regulator?”, viz: The PPP arbiter

(Mr Blaiklock) “I am not sure. We are into uncharted territory here because I do not know another situation where you have this kind of possibility arising”.

I, therefore, took great interest when the PPP Arbiter, Chris Bolt, was interviewed by your Committee on 6 January 2010.

Two comments:

(a) Mr Bolt was asked:

Q170: (Mr Wilshire) “I want to go back to the point Mr Stringer raised but get there via a general question first, if I may. Do you consider that it in the interests of passengers and the taxpayer that Tube Lines survives or is it in their interests that it finishes?”

Mr Bolt: “My view very clearly is that it is in the interests of taxpayers and users of the Tube that Tube Lines does survive because the ability to compare performance is a very powerful spur to improvement”.

Had it occurred to the Committee that, without Tube Lines, there would be no need for there to be a PPP Arbiter, and so there would be a saving to the Taxpayer?

The cost of the PPP Arbiter’s Office in 2008–09 was £3.5 million (ref. PPP Arbiter accounts, www.ppparbiter.org.uk). Mr Bolt had an undeclared conflict of interest in answering this question!

(b) When Tube Lines originally was awarded the PPP contract end-2002, the funding comprised:

<table>
<thead>
<tr>
<th>Amount (mn)</th>
<th>Terms</th>
</tr>
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<tbody>
<tr>
<td>Equity</td>
<td>£135</td>
</tr>
<tr>
<td>Sub-Debt (Shareholder loan)</td>
<td>£135</td>
</tr>
<tr>
<td>Bond</td>
<td>£630</td>
</tr>
<tr>
<td>Bond (AMBAC)</td>
<td>£600</td>
</tr>
<tr>
<td>EIB</td>
<td>£300</td>
</tr>
<tr>
<td>Standby loan</td>
<td>£200</td>
</tr>
<tr>
<td>Misc facilities</td>
<td>£77</td>
</tr>
<tr>
<td>Total Debt</td>
<td>£1,800</td>
</tr>
<tr>
<td>Total</td>
<td>£2,150</td>
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</table>

(Source: S and P; Euromoney “Project Finance”)

Since that time the finances of Tube Lines have been re-financed (a few times!), such that as of end-2008 the loans outstanding comprised:

<table>
<thead>
<tr>
<th>Amount (mn)</th>
<th>Terms</th>
</tr>
</thead>
<tbody>
<tr>
<td>EIB Loan</td>
<td>£269.9</td>
</tr>
<tr>
<td>Interest</td>
<td>5.36% pa</td>
</tr>
<tr>
<td>Term A Loan</td>
<td>£1,065.6</td>
</tr>
<tr>
<td>Interest</td>
<td>5.54% pa</td>
</tr>
<tr>
<td>Term B Loan</td>
<td>£75.5</td>
</tr>
<tr>
<td>Interest</td>
<td>7.45% pa</td>
</tr>
<tr>
<td>Term C Loan</td>
<td>£119.7</td>
</tr>
<tr>
<td>Interest</td>
<td>8.68% pa to 2010, then LIBOR plus 7%</td>
</tr>
<tr>
<td>Term D Loan</td>
<td>£17.9</td>
</tr>
<tr>
<td>Interest</td>
<td>1.17% pa to 2010, then LIBOR plus 9.5%</td>
</tr>
<tr>
<td>Unsecured Loan</td>
<td>£90.0</td>
</tr>
<tr>
<td>Interest</td>
<td>16% pa to 2025</td>
</tr>
</tbody>
</table>

(Source: Tube Lines Limited Accounts 2008.)

The 2008 Accounts also show that Corporation Tax was £17.1 million on a turnover of £806 million, and no Dividends were paid for that year. Under the PPP Concession dividends were not allowable during the first (7 year) review period. “Secondment service fees” to Bechtel and Ferrovial companies (ie the shareholders) amounting to £26 million were also paid in 2008 (ref Note 31).

From the above one concludes that:

(a) Tube Lines was quite highly geared (ie 85% debt and 15% equity). Lenders must have perceived the borrower as “low risk”;

(b) at least half of the Tube Lines equity was injected as shareholder loans at an inflated interest rate. This provides a mechanism for the shareholders to extract, in effect, dividends before corporation tax is applied;
(c) using this mechanism, it is likely that over the last seven years Tube Lines shareholders will have been able to extract “dividends” in the order of their original equity investment;

(d) given that the shareholders are non-UK entities, it is quite probable that no UK tax would be payable on such investment income or capital gain; and

(e) significant amounts may also have been extracted from the Company by shareholders via service fees, enhancing shareholders’ return on investment. This mechanism is similar to that which arose with Metronet!

As a result, the residual financial risk to Tube Lines’ shareholders in current circumstances could well be minimal and, if the Tube Lines franchise collapsed, the shareholders will have lost little, if anything. One therefore questions what financial risks, if any, Tube Lines will actually assume if the status quo prevails and they continue to operate the JNP PPP Concession over the next review period.

*January 2010*