

Office of the PPP Arbiter

23 April 2008

Reference for guidance from London Underground of 14 April 2008 Arbiter's decision on whether to give guidance

Background

1. On 14 April 2008, London Underground Limited ('London Underground') made a reference to the Arbiter for guidance pursuant to section 230(1)(b) of the Greater London Authority Act 1999 ('the Act') in relation to its PPP Agreement with Tube Lines Limited ('Tube Lines'). The reference seeks the Arbiter's guidance on the costs that Tube Lines could incur in the second 7½ years of its PPP Agreement and on associated performance levels. Part A of the Reference Application Notice has been published as an attachment to the Arbiter's Press Notice of 15 April 2008¹.
2. As the reference was made by only one party to the relevant PPP Agreement, the Arbiter is, under the provisions of section 230(2)(b) of the Act, not obliged to give guidance.
3. The Arbiter has received representations from both Tube Lines and London Underground as to whether he should give guidance. This document sets out his decision.
4. London Underground argued in its statement of case that it "would be valuable to seek the Arbiter's Guidance on the matters set out in this notice to provide greater confidence that its Restated Terms will be affordable thus (a) reducing the risk that Restated Terms will need to be de-scoped late in the Periodic Review process, with the attendant risk that this will result in sub-optimal results and (b) increasing the likelihood that Periodic Review will be successfully completed before the Review Date".
5. Tube Lines' representation to the Arbiter argues:
 - a. since there is no basis on which the requested Guidance could in any way be calculated to achieve any of the objectives in s231 of the Act, there is no proper basis on which the Arbiter can conclude that he should proceed to give the guidance requested;
 - b. without prejudice to this primary proposition, the Arbiter should not decide in favour of giving the requested guidance even if he considers that he is entitled to give it, for example because the limited benefit of the guidance would be more than outweighed by the time and effort required to complete the reference and the adverse impact on the overall Periodic Review process; and

¹ See

http://www.ppparbiter.org.uk/files/uploads/i_pressNotices/20084151331_Press_Noteice_01_08%20and%20reference%20application%20notice.pdf

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- c. even if guidance is given, it should not cover the performance element of the reference.

Arbiter's consideration

6. The Arbiter has reached his decision on whether to give guidance on the basis of the statutory duty placed on him by s231 of the Act. He considers that the reference has been properly made in accordance with the provisions of the Act, and of his Procedural Framework². He considers therefore that the reference is valid.
7. The Arbiter has been discussing with Tube Lines and London Underground since late 2007 the timetable and process for the first Periodic Review of Tube Lines' PPP Agreement, which is due to be completed by 30 June 2010, including the use that will be made of the 2008-09 Annual Asset Management Plan in preparing for the Review. Although the procedures for Periodic Review in the PPP Agreement are intended to allow time for Tube Lines and London Underground to negotiate revised Infrastructure Service Charges (ISC) for the second Review Period and make a reference to the Arbiter for direction only in the event that negotiations are unsuccessful, it is, in the Arbiter's view, common ground that the contractual timetable will not permit this, given the likely timescales for completing a reference for direction.
8. Although the PPP Agreement makes provision for the existing ISC to be extended in the event that the Arbiter has not given his direction by the Review Date, the Arbiter also believes that it is common ground that in such a situation Tube Lines would need to apply for an Interim ISC direction to enable it to finance its continuing obligations. This would have cash flow implications for London Underground.
9. Accordingly, the Arbiter considers that completion of the Periodic Review by the Review Date is highly desirable, in terms the following objectives in s231 of the Act:
- s231(3): the promotion of efficiency and economy;
 - s231(4): ensuring that an efficient and economic Infraco can earn the equity rate of return specified in its PPP Agreement; and
 - s231(5): enabling any PPP company which is a party to the PPP Agreement in question to plan the future performance of the agreement with reasonable certainty.
10. The first important step in the Periodic Review process is for London Underground to issue Restated Terms and its Affordability Constraints. Under the terms of the PPP Agreement, this is to be done by 30 December 2008, although London Underground has indicated that it is aiming to do this before the last date in the contract. However, it has argued that it will be better placed to do this if it has received guidance in the form requested.

² See

http://www.ppparbiter.org.uk/files/uploads/g_proceduralFrameWork/2007651842_Procedural%20Framework,%20June%202007.PDF

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11. The Arbiter is of the view that the ISC payable to the three Infracos may exceed the resources currently available to London Underground in the second Review Period. Accordingly, the objective in s231(2) of the Act (to give London Underground an opportunity to review the requirements imposed, or proposed to be imposed, in those circumstances) is also relevant to his decision whether or not to give guidance.
 12. The Arbiter's view is that giving guidance on the matter referred to him by London Underground will better enable it to determine Restated Terms for Tube Lines, and to issue these before the last date allowed for in the PPP Agreement, and that this will increase the likelihood of successful completion of the Review by the Review Date. Agreeing to give guidance would therefore support all four of the objectives specified in the Act as part of the Arbiter's statutory duty.

Arbiter's decision

13. The Arbiter has decided that it would be appropriate to give guidance in respect of the reference from London Underground.
14. The Arbiter will be discussing with the Parties the approach which he should take to the reference in terms of procedures and timetable, and will publish his conclusions on 30 April 2008.