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Siobhan Carty
Competition and Consumer Policy Team
Office of Rail Regulation
1 Kemble St
London
WC2B4AN

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Office of Rail Regulation Consultation on the potential impacts of regulation and industry arrangements and practices for ticket selling

Dear Ms Carty,

I am pleased to write on behalf of Keolis UK in reply to your consultation document dated September 2014. Our responses are provided in italics overleaf.

As we consider customer outcomes to be the most important factor, we believe that the basic objective of this review should be ensuring consumers have a choice of channels and can buy their ticket easily and with full confidence that they've selected the most suitable option irrespective of the channel.

As a general comment, we support the ORR's actions to ensure that current rail industry structures don't stifle innovation, change and competition. Furthermore because almost twenty years have passed since rail privatisation, it seems sensible to ensure that the current framework is sound for today's challenges.

We also agree that consumer ticket buying habits are changing, a trend that is likely to continue indefinitely and whilst there has been considerable change in the marketplace as railway companies seek to meet these emerging demands, innovation has been held back by some aspects of the current arrangements.

In particular we believe that Schedule 17 ofthe TSA, which sets ticket office opening hours, has effectively made ticket offices a fixed cost. As a result our freedom to meet changing consumer needs with innovation is severely constrained. The current trial of third party retailers selling season tickets is a good example. This initiative is designed to give consumers a choice and allow season tickets to be sold via a lower cost channel, however if TOCs are not able to adjust ticket office provision because of Schedule 17, then the result will be higher than necessary industry costs and that makes finding a positive business case for this idea difficult.

Keolis supports maintaining impartiality requirements, because they ensure customers are presented with the full range of options and can therefore make an informed purchase decision. For example a customer buying a ticket from the Virgin Trains operated ticket office at Birmingham New St for travel to London Euston, can today feel assured they will be offered both the quicker Virgin

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Trains service and the cheaper London Midland fare, allowing them to decide which option best meets their needs. It is difficult to see how loosing this facility is in customers' interests and we feel any such moves would be widely opposed by passenger groups.

We also strongly oppose withdrawing through ticketing requirements as we struggle to see any way in which removing this convenience could be regarded as a consumer benefit and we believe passenger groups would strongly oppose their withdrawal. However a cost-benefit review could be used to drive efficiencies in the way RSP deliver this service.

We are concerned customers don't always understand that every franchised train company offers an impartial sales service and consequentially consumers often pay unnecessary booking fees to third party agents when they could have received an identical service for free from any TOC. Whilst we welcome the efforts made by third party retailers to promote rail travel and work with them to do so, customers unwittingly paying unnecessary fees for no added value is not a desirable outcome. We are not opposed to booking fees, in fact there are situations outlined within where we believe TOCs should be able to charge fees to help protect more expensive sales channels such as ticket offices, however their levying should be transparent to consumers.

Third party agent growth has outpaced the market allowing them to increase their share, which suggests that the market has functioned well. Commission rates taken in isolation can be misleading as it is the combination of commission rates and average transaction value that determines how much remuneration a retailer gets. For instance, TMCs receive 3% commission, which means that they earn an average of £1.75 per transaction before booking fees which are estimated at around £9 per transaction on average, significantly higher than the £1.15 per transaction received by TOCs for non-Season Ticket sales at station ticket offices.

We accept that in principle there might appear a conflict of interest in the way that TOCs through ATOC set commission rates for third parties. However, this is offset by the need of TOCs to incentivise third parties to increase sales, especially as TOC premium payments now exceed our subsidy. Furthermore TOCs are reliant upon third party retailers for the supply of white label online ticket issuing systems, a market place in which third/party retailers are oligopolists. As such the dynamic between TOCs and third party r is much more balanced than might first appear to be the case.

Our responses within are designed t orm the basis of Keolis' ongoing engagement with ORR on this matter and as such please feel fr to contact me should any clarification be necessary.

Yours sincerely

Ruud Haket
Chief Operating Officer

Question 1:

We believe that the consultation document has broadly captured the key trends, although greater emphasis should be given to the very high growth levels achieved as this suggests the market functions reasonably well. We also feel the dynamic between TOCs and Third Party Retailers isn't entirely captured, because Third Party Retailers typically provide white label online booking solutions to TOCs, a fact which creates a dynamic of mutual reliance.

Question 2:

Broadly we consider the consultation document appropriately captures the most significant changes to ticket retailing.

The pace and level of developments has not always been appropriate to meeting passengers' changing needs. As discussed above, Schedule 17 of the TSA has turned station ticket offices into a fixed cost, which severely hampers the business case for innovation.

Separately ticket fulfilment is still overly focused upon credit card sized tickets, whereas customers have become used to print at home or app based bar code fulfilment in other industries such as airlines and hotels or Smartcards in London. Voluntary efforts on the part of TOCs to co-ordinate ticket types have been widely welcomed, suggesting there is strength in the concept of adopting a straight forward industry approach. The lack of progress in ticket fulfilment is because there is no industry wide strategy, which means progress is piecemeal and generally limited to operator specific tickets. An across industry forum to resolve this problem would help co-ordinate industry innovation.

Question 3:

Rail operates as part of a wider consumer travel environment and the move towards print at home and app based fulfilment described above is important because customer expectations are to a large extent driven by their experiences elsewhere.

Question 4:

There are a number of areas where we found some inaccuracies:

Paragraph 3.7: TOCs are not restricted by the TSA or any other aspect of the regulatory framework to change fares at only three points during the year. The fact that this is currently the case simply reflects the technical/imitations of industry systems, although this constraint will be removed following implementation of the new fares system (called the Product Management System or PMS}.

Paragraph 3.10: Third party retailers earn a base rate of commission from TOCs through the centralised ATOC arrangements but can earn additional remuneration through bilateral arrangements with individual TOCs or owning groups. This is relatively uncommon in the consumer market but much more widespread in the TMC/travel agent market.

It is misleading to state that 'some' third party retailers charge fees, as the vast majority of third party retailers choose to do this and are not aware of any who do not charge a fee.

Paragraph 3.14: The obligation upon retailers to provide accurate information essentially stems from general consumer law rather than the rail industry's specific regulatory framework.

However, accuracy and impartiality are completely different concepts. For example a retailer might provide information on all the available fares for a specific journey accurately but still sell partially (for instance by giving greater prominence to the fares of one train company over others).

The impartiality obligation in the TSA was designed to ensure that partial retailing of the kind highlighted above does not happen. This was driven by the fear that post-privatisation, private sector train companies would, through their own retail channels, give greater prominence to their own fares rather than those of their competitors. Safeguarding against discriminatory behaviour was therefore the principal driver behind the impartiality obligation.

Paragraph 3.15: Retailers do not have to offer the same prices as other retailers or through every channel. However, all retailers, TOC and third party must settle with RSP at the full price.

Paragraph 3.21: TOCs have a regulatory obligation to offer Senior, 16-25 and Disabled Persons Railcards. However other Railcards are offered by TOCs on a voluntary basis.

Paragraph 3.24 and 3.25: This paragraph characterises the TSA and other industry 'Schemes' as being 'owned' by TOCs. However, for 'mandatory' schemes (the TSA, Senior, 16-25 and Disabled Persons Railcard Schemes and NRE Scheme}, which form part of the regulatory framework, this is essentially not an accurate description.

Whilst they are inter-operator agreements, all were drafted prior to privatisation and became immediate regulatory obligations upon the newly created franchises. After this, any change to the agreements was subject to OfT (in effect government) approval. Whilst this has been given in some areas, it has been denied in others. In particular, long standing proposals from TOCs/ATOC to fundamentally reform fundamentally the TSA have been consistently rejected over a period of many years by the government.

In effect this amounts to the TSA and other mandatory schemes being government/OfT created arrangements that are subject to government/OfT change control. There are inter-operator schemes 'owned' by the TOCsin name only.

Paragraph 3.34 (a): This requirement does not apply to all third party retailers as implied by this paragraph, but only to Third Party Investor Licence holders (of which there are currently three).

Table 2: At the request of the retailer, interim licences can extend beyond twelve months.
Paragraph 3.38 (g): There is also an £0.90 ToO fee for tickets issued through ticket offices, although it is not a popular method of fulfilment.

Paragraph 3.38 (h): The reason that for third party and inter-TOC sales the carrying TOC does not receive all of the revenue from the sale of a fare is not because of ORCATS but because RSP deducts the commission owed to the retailer prior to settlement.

Question 5:
As an operator retailing activity is driven by the need to increase travel revenue rather than commission from retailing. We place particular emphasis on customer ownership to help build a good long term relationship and generate repeat travel.

Schedule 17 of the TSA significantly weakens our business case for investment in new services and facilities because potential cost savings from station retailing cannot be realised.

For third parties the clear driver is revenue from TOC commission and customer/client fees. However, investment in new services or facilities to increase market share is also a driver, as is the ability to leverage investment more widely through technology supply deals or 'white label' arrangements. The key market for 'white label' solutions is in fact the TOC community, who rely on third party retailers to supply their online booking engines.

Question 6:

We believe that the impartiality obligation helps ensure customers purchase the most suitable fare against the backdrop of a complicated fares system, although we doubt many people are conscious of this service.

The impartiality obligation in rail fundamentally changes the role of third parties when compared to most industries. Traditionally in regulated industries third parties add value by providing impartial consumer advice but in the case of rail, customers get this for free anyway and encouraging consumers who are unaware of impartial retailing to pay unnecessary booking fees is not in their interests, although we recognise the TMC market is different. As such we feel where fees are charged there should be an obligation to make it clear rail companies provide equivalent services for free.

The need to offer the full range of fares to support impartiality almost certainly drives cost, although the quantum has never been estimated as far as we are aware. When coupled with the regulatory obligation with regard to through and inter-available fares, this certainly drives a degree of complexity for both retailers, TIS providers and customers.

Question 7:

Although the combinations of tickets made possible by split ticketing can be cheaper than the equivalent through fare, split ticketing is inherently complex and confusing for customers.

Even where specific anomalies exist that could be removed, TOCs are prevented from doing this as the necessary inter-TOC discussions would count as collusion under competition law. It is also worth noting that fares capping regulation also exacerbates the problem, particularly now that reduced flex provides less opportunity to remove anomalies. This core problem needs to be addressed to avoid a situation where rail pricing is partly or largely driven by fare anomalies rather than the sensible market drivers, which cannot be a sustainable position.

Question 8:

We believe that there is quite an important difference between the requirement to create and sell inter-available and through tickets, and the requirement to offer a timetabled walk-up service.

In terms of inter-available and through tickets, these regulatory obligations clearly provide some customer benefits, but equally they have also driven complexity for consumers, retailers and TIS suppliers. There needs to be a critical review and evaluation as to whether, on balance, through and inter-operable ticketing along with other 'network benefit' elements of the regulatory framework still provide benefits to consumers. However we find it very difficult to imagine that breaking up the ability of customers to buy through tickets could ever been seen as a consumer betterment.

Equally, timetabled walk up services are a core element on shorter distance routes where advance purchase is uncommon and consumers expect to be able to purchase a ticket and travel immediately. We do not believe that there is any obvious market rationale for changing this. However on longer distance routes around 60% of customers now choose to buy advance purchase tickets, a trend which *is increasing. Eurostar operate very successfully using a reservation only model as does the French TGV network and such a model may have advantages in managing capacity and yield if allowed in the UK.*

Question 9:

The rail retailing market does not satisfy the conditions of an efficient market because the ability to vary supply for a key channel to market, station ticket offices, is constrained by regulation (Schedule 17 of the TSA). Efficient Markets exist to allocate scarce resources efficiently. This does not mean that they meet the needs of every individual in all respects, but in general they deliver the best 'on balance' way of maximising the meeting of consumer needs at the lowest cost. In order to do this, supply needs to be able to be varied to meet demand and incentives need to exist to encourage investment to meet unmet demand. Clearly the Schedule 17 of the TSA prevents this.

Station Ticket Office costs are essentially fixed by the TSA and account for around 50% of all industry retailing costs, despite station ticket offices representing less than 39% of total sales and just 26% of industry transactions. Furthermore, current market trends where customers are increasingly making a free choice to use other channels mean that this disparity is growing. Given the high cost of this channel, there is little doubt that in an unconstrained efficient market, we could have delivered industry savings by incentivising customers to move to more cost-effective methods through differential pricing.

For example in Holland customers pay a small surcharge for buying their ticket at a ticket office. This allows NS to recoup some of the costs incurred by maintaining this more expensive channel, but maintains consumer choice.

Question 10:

It is our clear wish that the current regulatory restriction on TOCs charging fees for more expensive sales channels are lifted and that we are allowed to enjoy the same degree of commercial freedom as third parties.

Current arrangements mean that TOCs are not able to charge fees of any kind where extra costs are incurred, including credit card fees, for ticket office retailing, on-train retailing, or sales through call centres. As outlined above these fees could be used to promote more cost-effective retail methods, reducing overall industry costs. The inability of TOCs to charge fees in the consumer market is a clear market distortion, as third party retailers are uniquely able to recoup their costs.

The ability of TOCs to charge fees in the corporate market via Business Travel Service (BTS) arrangements is very limited in comparison to TMCs. This has left many BTS departments unviable and lead to their closure against a backdrop of thriving TMC sales.

Question 11:

The current approach to third party retailing creates some tensions within the market, given that TOCs through ATOC, set commission for third party retailers who compete with the TOCs in the rail retail market. However within wider industry it is not unusual for an operator to set the commission it is prepared to pay intermediaries.

ATOC goes to some considerable lengths to be even-handed in the way that it balances third party and operator interests which includes a degree of consultation with third parties on key changes. From an operator's perspective, it is difficult to quantify what value third party retailers deliver us, as TOCs have to provide an essentially identical service (including impartiality obligations) directly to the *public from within our cost base. The benefit third parties deliver is arguably via their marketing activity. This makes it difficult to agree what level of commission, if any at all, should be set. We note that most of the industries outlined in the ORR's research don't pay third party intermediaries any commission, who instead make their revenue from consumer charges. As such one might argue that the current form of industry governance has in fact benefited intermediaries ahead of operators because against the general trend we still pay sales commission.*

For both operators and third parties the TIS market has seen limited innovation on the part of suppliers which has to some degree reduced our ability to meet customer demands.

Question 12:

Returning to our opening statement, that we believe an important objective of this review should be ensuring consumers have a choice of channels and can buy their ticket with full confidence that they've selected the most suitable option irrespective of the channel, overall we do not believe the rules placed upon retailers to be excessive or disproportionate.

For the most part they are designed to ensure that retailing is conducted to the high standards that customers might reasonably expect, helping to ensure the consumer objective highlighted above is met.

To meet the same consumer objective TOCs are subject to a wide range of rules relating to retailing, include the many requirements contained within the TSA. It would seem inequitable in competition terms if TOCs were obliged to conform to these sorts of rules when third parties weren't.

Question 13:

With regard to the potential opportunities offered by a wholesale market in rail products, there are a couple of points worth making on current arrangements:

(a) The current ITX licence does provide a form ofwholesale arrangement, with agents able to combine and mark-up net fares with other travel elements to form 'packages' for consumers usually consisting of travel and accommodation. We are eager to see this market grow;

(b) Other agents are entitled to combine public fares with other travel elements to form packages, adding a mark-up to the rail fare if they wish (they are only required to settle at the public rate). As part of an overall package they are free to use the commission earned from accommodation to charge consumers less than the public rate fare, presenting the public with a saving. Arrangements around commission are quite common place in the wider travel sector.

More generally, we would be open to further discussion on this opportunity. It is not immediately apparent what the benefits would be to TOCs or consumers, but we would certainly be open to any development for which there was a strong commercial rationale.

There are many examples of long distance train operators working with third party travel management company retailers to provide upgraded facilities (e.g. lounge access when travelling with a standard class ticket; free car parking) for their customers.

Question 14

The systems and processes which support the retailing of train tickets are designed to keep a balance between the positive benefits of preserving 'network benefits' (i.e. the fully interoperable railway}, and the positive benefits of enabling individual train companies and third party retailers to innovate in terms of the customer experience.

In practice this means there are shared back office systems primarily operated by RSP, and front office systems, particularly TIS and Customer Relationship Management Systems run by train companies and third party retailers. Whilst it may be that individual train companies could drive innovation more quickly if they also ran their own back office, this would inevitably dilute the current range of networks benefits enjoyed by customers.

Further, one of the benefits of central procurement is that investment can be written off over the life of the asset (sometimes 15 or more years}, and the relatively short term nature of franchises doesn't therefore, impact on investment decisions.

By way of example:

- *The issue of multiple IT systems was explored more than thoroughly when the question of OfT sponsored SEFT project (South East Flexible Ticketing) HOPS architecture was discussed, and the consensus was that a central service was the cheapest and simplest solution.*
- *The Rail Journey Information System was replaced in a very reasonable timescales, given the complexity of the system, and was operational before the expiry of the legacy system contract, with a 70% saving in annual operating costs.*

In conclusion, although we believe a cost/benefit study to justify maintaining network benefits against the costs associated with them could be justified, not least to help identify where efficiency savings could be achieved, we strongly argue that the concept of RSP's provision of central industry systems to ensure network benefits remain must be maintained.

Question 15

The railway industry has come under considerably consumer criticism for the supply of contradictory information in the widest sense, for example passenger information at times of disruption. This suggests to us that customers prefer simple consistent information. One of the abiding principles with regard to data related to the retailing of rail tickets {which now includes passenger information data}, is that there should be a single point of truth. So, we support a single fares database which feeds all rail retailing systems, we use the Network Rail timetable as the basis for all journey planners, we have a central seat reservation system, and so on.

This enables the best quality data to be made available at the right time in the right place, and ensures that it is consistent. A particular type of ticket priced at, say £15.00, will be £15.00 in every one of our 10,000 points of sale because that data is sourced from a single point. Returning to our opening statement about consumer confidence, we believe this is key.

Whilst it is true that other travel sectors such as airlines feed third parties via multiple global distribution systems, that is mainly due to the heritage of flag carriers competing with each other and having to develop their own individual systems which later merged along geographical lines into the various Global Distribution Systems {GOS} used today. GOS market share is largely geographically based upon that heritage, thus the market is much less competitive than it appears. Whilst we support moves to sell train tickets on the GDS, especially in long distance markets where rail competes directly with airlines, this is an expensive approach that stands to increase industry costs if implemented more widely.

Question 16

We believe that the proposed approach to assessing the materiality and relevance of the impacts is reasonable.

We have also highlighted the issues associated with the current regulatory framework, making a case for changes in some areas (Schedule 17 of the TSA for instance) and encouraging review in others. We emphasise that supply-side costs are excessively high, largely due to market-distorting regulation but partly due to an insufficiently competitive supply chain.

Question 17

We agree that it is sensible for the ORR to develop options for change as a first step in Stage Two. Keolis will continue to engage constructively with ORR and our industry partners throughout this review.