



Government Legal Department

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Your ref:

Our ref: Z1622408/SCX/CLGA

9 August 2016

Dear Sirs

South Western Rail Franchise (“the Franchise”)

I refer to your letter of 28 July 2016, addressed to Mr Philip Rutnam, the Permanent Secretary of the Department for Transport (“the Department”).

I am instructed to reply on behalf of the Department. This letter is written in accordance with the Pre-Action Protocol for judicial review under the Civil Procedure Rules.

Please address any further correspondence relating to the proposed claim to me: my contact details and reference are as shown at the head and foot of this letter.

The proposed claimants

Mr David Pugh – 31 Silver Trees, Shanklin, Isle of Wight PO37 7ND

Mr Warren Drew – 7 Fir Tree Close, Shanklin, Isle of Wight PO37 7EX

The proposed defendant

Your letter states that the defendant to your proposed claim is Mr Rutnam. The Department’s position is that Mr Rutnam would not be the appropriate defendant to your proposed claim, which relates to the content of an invitation to tender for a rail franchise issued by the Secretary of State for Transport pursuant to section 26 of the Railways Act 1993 (“the Act”). (The Secretary of State is “the appropriate franchising authority” for the purposes of section 26: see section 23(3) of the Act.)

Should you wish to bring the proposed claim, the appropriate defendant would be the Secretary of State for Transport, whose address is Great Minster House, 33 Horseferry Road, London SW1P 4DR.

In this letter the terms “the Department” and “the Secretary of State” are (except where the context indicates otherwise) used interchangeably and without distinguishing between them. The Secretary

Wendy Hardaker - Head of Division

Zane Denton - Deputy Director, Team Leader Commercial Litigation A



of State for Transport is responsible, as a matter of public law, for the actions and decisions of the Department.

Details of the matter being challenged

I understand the subjects of your proposed challenge to be:

- (i) the inclusion in the Invitation to Tender published by the Secretary of State for Transport in June 2016 (“the ITT”) of one of the Franchise Objectives as follows:

“...work with the Isle of Wight Council to secure a long-term sustainable solution to the future of the Island Line during the course of the next franchise that will enable it to become a self-sustaining business...”

and in particular the reference to “a self-sustaining business”. You suggest that the Secretary of State included that Franchise Objective in the ITT without taking into account relevant considerations, in particular the lack of adequate financial data for the Island Line (“the Line”).

- (ii) You also allege that it is irrational to believe that the Line could be better run outside the Franchise than within it.

It appears that you believe that the Secretary of State has, by issuing the ITT, effectively taken a decision, or otherwise somehow pre-determined, that the Line should not form part of the Franchise.

Response to the proposed claim

Summary

As explained in more detail below, the Department considers that your proposed claim is based on a misunderstanding of the ITT and its legal consequences. The position at the present time is that the Secretary of State has not taken any decision to remove the Line from the scope of the Franchise. Nor has the Secretary of State come to any view as to whether the Line should, in the event of any separation from the Franchise, operate without subsidy or other State financial support, or as to the amount of financial support to be provided for the Line.

The reference in the seventh Franchise Objective to “a self-sustaining business” in table 2.1 of the ITT is to be read in the context of the ITT as a whole, including the other paragraphs of the ITT referring to the future of the Line: see in particular paragraphs 5.6.4 and 5.6.6(g) of the ITT; and see also paragraphs 5.72 – 5.80 of the Stakeholder Briefing Document (“SBD”) published alongside the ITT. The use of that phrase does not signify that the Secretary of State has at this stage decided that the Line should cease to be the responsibility of the Franchisee or should become self-sustaining *without any State financial support*. Rather, what is meant by that phrase is that the Franchisee should work to secure a sustainable future for the Line, including by establishing the Line as a separate business unit within the overall Franchise operation so that transparent financial and other data is available to assist the Franchisee, the Isle of Wight Council and the Department in considering options for the future development and operation of the Line (which currently has the oldest rolling stock in standard service of any railway in the country and would benefit from investment and modernisation).

The Secretary of State, in deciding to proceed that way, took account of the submissions received to the stakeholder consultation relating to the Franchise (as discussed at paragraphs 5.72 – 5.80 of the SBD). The Secretary of State has deliberately not taken any decision now as to whether or not the Line should remain part of the Franchise in the longer term, and has instead specified the Franchise in such a way as to enable the Isle of Wight Council and other stakeholders to work together to identify and consider the various options.

The Department regrets the misunderstanding that appears to have arisen from the phrasing of the seventh Franchise Objective and has therefore decided to amend the wording of that Franchise Objective to remove any scope for confusion, and has notified all intending bidders of this change.

Fuller response

The Department has made clear throughout the process of re-letting the Franchise that it regards it as most important that the Line should continue and flourish. As stated in the SBD at paragraph 5.76:

The Department understands that the Island Line provides important transport for residents and visitors to the Isle of Wight, and that there should continue to be the provision of passenger transport services on the island.

Exploring options and obtaining financial data: however as you recognise in your letter, the Line is currently loss-making and faces the need for costly infrastructure upgrades. You also recognise the lack of reliable data as to the financial position of the Line.

It is because of these factors that the Department has made clear the need for the new Franchisee to explore all options to meet the financial challenges facing the Line and, as a first step in that exercise, to generate reliable financial data for the Line by establishing a separate business unit for it (SBD, paragraph 5.77):

With the view to securing a more sustainable, long-term solution, the next franchisee will be required to work with stakeholders, including the Isle of Wight Council, Network Rail, and the Department to explore options for the future provision of services that meet the needs of passengers, the local community and the taxpayer. This will also include establishing a business unit for the Island Line, which will provide separate financial and operational data to inform the consideration of potential options.

These aims are reflected in the ITT (paragraph 5.6.4):

The Department requires a Franchisee who will work with the Isle of Wight Council and other stakeholders to help develop a sustainable future for the Island Line

and in the provisions in the draft Franchise Agreement (section 5 of Schedule 6.1) which will require the Franchisee to create a separate Island Line Business Unit.

Giving effect to the exploration of options: in the context of a rail franchise which is planned to last for at least 7 years and in which the Franchisee is required to explore with stakeholders options for the Line, it is important for the Department to retain the flexibility to give effect during the period of the Franchise to any option which emerges and meets the approval of stakeholders. It is conceivable that such an option could involve someone other than the Franchisee running the line. For this reason the Department has included provisions in the draft Franchise Agreement which, in such an event, would facilitate the Secretary of State bringing about the transfer of the Line to another operator.

However another operator running the Line is only one possible outcome of the exploration of options; and the draft Franchise Agreement expressly recognises that such a step would require a variation to the Franchise Agreement. At this stage the reason for making contractual provision for such possible future developments is simply to avoid artificially restricting the options for the Line during the life of the Franchise, but rather to leave open the opportunity for the next Franchisee to provide innovative and cost effective solutions and the Department's ability to implement them. The draft Franchise Agreement does this, whilst at the same time ensuring the continued provision and improvement of passenger services on the Line. As you will know, the Department is proposing an annual £50,000 Customer and Communities Improvement Fund which will be available from the second year of the franchise for investment in improvements to facilities and services on the Line.

For these reasons it is not irrational to require the Franchisee to work with the Isle of Wight Council in exploring options. The Council has a strong interest in securing a sustainable, long-term solution for the Line and can be expected to engage actively with the Franchisee in developing options to secure that.

“Self-sustaining business”: You have drawn attention to the reference in one of the Franchise Objectives in the ITT to “work[ing] with the Isle of Wight Council to secure a long-term sustainable solution to the future of the Island Line during the course of the next franchise that will enable it to become a self-sustaining business”.

It is important to note that the Franchise Objectives are not included as such in the draft Franchise Agreement. Rather, the ITT requires bidders to fulfil the Franchise Objectives by meeting the requirements as to bid submissions in the ITT. The relevant requirement in this case is paragraph 5.6.6(g) of the ITT, which requires each bidder to explain in its bid how it will work with the Isle of Wight Council and other stakeholders to help develop a sustainable future for the Island Line. I am sure all parties will agree that a long-term sustainable solution for the Line is needed and that it is necessary for the Franchisee to work with the Council to achieve that aim.

In relation to the reference in that Franchise Objective to “a self-sustaining business”, it appears from your letter that (as I have already set out above in the ‘Summary’ section of this letter) you may have interpreted that phrase in a way that differs from its intended import (as reflected in the SBD and paragraphs 5.6.4 and 5.6.6(g) of the ITT). Nevertheless, the Department is keen to avoid any scope for misunderstanding, and has therefore amended that Objective to:

“Work with the Isle of Wight Council to secure a long-term sustainable solution to the future of the Island Line during the course of the next franchise that will enable it to become a more sustainable business.” (emphasis added)

This amendment brings the wording of that Objective more clearly into line with the questions in the original Consultation document which referred to “a more self-sustaining business” and the SBD, which referred to “a more sustainable, long-term solution”. I hope this change of wording resolves your concerns on this point.

Conclusion: I trust this letter answers the concerns expressed in your letter. For the reasons I have explained, it appears that the proposed claim may arise out of a degree of misunderstanding which is resolved by this letter and by the change to the wording of the seventh Franchise Objective. For completeness, however, I make clear that the Department does not consider the proposed claim to be well founded and will therefore resist any such claim in full.

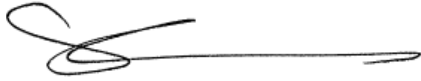
ADR

The Department shares your wish that this matter can be resolved without court proceedings and the Department has therefore sought to resolve your concerns as set out above.

Your letter sets out a specific proposal that the Department amend the Franchise Objective so as to refer to the long-term sustainable solution for the Line to be “wholly delivered within the wider franchise model”. The Department’s amended wording of that Franchise Objective differs from your proposal in that it does not seek to pre-determine the future operational arrangements for the Line by precluding certain options from being considered. The Department does not agree that it would be appropriate to rule out any options at this stage, or that it is legally required to rule out consideration of any options which may involve the Line being operated by anyone other than the Franchisee. As I

have explained above, no decision has been taken as to whether the Line will, or will not, continue to be part of the Franchise in the long-term.

Yours faithfully

A handwritten signature in black ink, consisting of a stylized, cursive 'S' followed by a long horizontal line that tapers to a point.

Stephen Cromie
For the Treasury Solicitor

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