

Agenda

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What's driving damages? The *2 Travel v Cardiff Bus* competition law ruling

The UK Competition Appeal Tribunal recently issued a judgment in a follow-on competition law damages action between 2 Travel and Cardiff Bus. The latter had previously been found to have abused its dominant position, leading 2 Travel to claim £50m in damages. The decision, which awarded £33,818.79 in lost profits and £60,000 in exemplary damages, provides important precedent on how courts use facts and economic evidence in determining the amount of lost profit

Follow-on antitrust damages cases rarely make it all the way to trial. In a follow-on action, courts assess the loss and damage sustained by a company based on a previous infringement decision by a regulator or competition authority. *Enron Coal Services Limited (in liquidation) v English Welsh & Scottish Railway Limited* was the first such follow-on case to be heard at the UK Competition Appeal Tribunal (CAT), although the claim was ultimately dismissed.¹ The case of *2 Travel Group Plc (in Liquidation) v Cardiff City Transport Services Limited*,² the first to award damages, is therefore an important addition to the limited precedent on the subject.

The *2 Travel v Cardiff Bus* case involved two bus operators in Cardiff. In April 2004, 2 Travel, a small entrant, began no-frills bus services on four routes in Cardiff, with a fifth route intended to begin operating in November 2004. These were in-fill services—ie, commercial bus services that operate in between 2 Travel's morning and afternoon school services using the same buses. In response to 2 Travel's entry, Cardiff Bus, the incumbent bus operator, introduced its own no-frills bus service on the same five routes, known generally as 'white services'. This was in addition to its existing bus services, known as 'liveried services', which already operated in Cardiff on routes partly overlapping with those of 2 Travel. 2 Travel ceased operations in December 2004 and Cardiff Bus closed down its white services shortly thereafter. 2 Travel went into liquidation in May 2005.

In November 2008, the UK Office of Fair Trading (OFT) determined that Cardiff Bus had engaged in anti-competitive practices against 2 Travel by abusing its dominant position and operating with exclusionary

intent.³ In 2011, 2 Travel brought a follow-on claim against Cardiff Bus before the CAT, claiming that it had sustained loss and damage of £50m⁴ as a result of the infringement, under seven broad categories:⁵

- exemplary damages;
- loss of profits;
- loss of a capital asset;
- loss of a commercial opportunity (growth of a successful bus company);⁶
- loss of a commercial opportunity (Swansea depot);
- wasted staff and management time;
- costs of liquidation.

In July 2012, after a two-week hearing in March, the CAT issued its judgment based on a detailed assessment of the facts and economic evidence. It rejected the last five categories, noting that 2 Travel was a 'poorly run and administered [business] in almost constant financial difficulty' and that the lost revenue resulting from the infringement would not have been enough to prevent 2 Travel from entering insolvency.⁷ The only claims that the CAT upheld were that for lost profits suffered by 2 Travel between April 2004 and May 2005, and exemplary damages. The Tribunal awarded £33,818.79 in lost profits, as well as £60,000 in exemplary damages.⁸

Establishing the counterfactual

The assessment of damages in the form of lost profits involves a comparison of the financial position that the claimant was in at the relevant time against the position that it would have been in without the infringement—ie, the counterfactual. The OFT determined that Cardiff Bus launched the entire white services operation only

Dr Gunnar Niels, Oxera Director, acted as the economic expert for Cardiff Bus in this case.

for the purpose of driving 2 Travel out of the market. As such, the experts for both sides, and the CAT, agreed that the relevant counterfactual scenario was what would have happened had Cardiff Bus not operated its white services at all, as opposed to operating them on some different, legitimate, basis. Determining this scenario required an assessment of the passengers who actually used Cardiff Bus, and the revenue they generated.

Both the experts and the CAT agreed that, in the absence of Cardiff Bus's white services, the passengers who travelled on this service would have travelled on either 2 Travel's in-fill services or Cardiff Bus's liveried services (it was also commonly accepted that the overall market would not have grown following entry). Since Cardiff Bus's liveried services operated in both the factual and the counterfactual scenarios, it was considered that none of these passengers would have transferred to 2 Travel. Therefore, the maximum number of additional passengers (ie, in addition to those who already travelled on 2 Travel) that 2 Travel could possibly have attracted were those 150,727 passengers who travelled on the white services over the relevant period.

The overall approach to determining how many of these passengers would have travelled with 2 Travel, and the revenue that would have been generated, was similar among both experts and the CAT. However, their analyses differed on some key assumptions.

The expert for Cardiff Bus developed a model of 2 Travel's operations on the relevant bus routes that incorporated a range of assumptions about the main parameters, including:

- the number of services that 2 Travel actually ran from April to December 2004;
- the number and types of additional passengers that 2 Travel would have gained; and
- the costs that 2 Travel would have incurred.

Scenarios were developed to reflect the uncertainty concerning the facts behind a number of these factors, and presented such that the CAT could determine which scenario it preferred following its assessment of the facts.

For the purposes of allocating white services passengers between Cardiff Bus and 2 Travel, three types of passenger needed to be considered: single/return, multi-journey/season, and concessionary. Multi-journey/season tickets were purchased for the liveried services, but also allowed passengers to travel on white services. Both the experts and the CAT assumed that no passengers on these tickets would have transferred to 2 Travel. The expert for Cardiff Bus

assumed that concessionary fare passengers get on the first bus that comes along, as they do not pay a fare for travelling on buses. In order to determine the number of concessionary passengers who would have travelled on 2 Travel, the passenger allocation between the two operators was approximated by considering the relative frequencies of their services.⁹ For example, if one operator runs six buses an hour on a particular section of the route and another operator runs two buses an hour on that same section, it is not unreasonable to assume that the first operator would get 75% of the passengers and the second 25%.¹⁰

Since the facts on the actual frequency of 2 Travel's services were unclear, the expert for Cardiff Bus explored three sets of frequencies: the services reported by 2 Travel (58% of its timetabled services); the services reported by a bus monitoring agency (32% of its timetabled services); and the services that 2 Travel would have run had it operated its full timetable. If 2 Travel ran all the services on its full timetable, it would have been able to achieve an average market share of 19% across all sections of the five routes.

For passengers on single/return fares, two scenarios were considered by the expert for Cardiff Bus: one where all passengers travel on 2 Travel; and one where passengers are allocated according to the relative frequency of services using the same method as for concessionary passengers.¹¹ The method for allocating passengers based on frequency is explained further in the box overleaf.

Once the counterfactual passenger numbers have been calculated, they are multiplied by 2 Travel's fares to estimate its counterfactual revenue. As a zonal fare system is used in Cardiff, the expert for Cardiff Bus apportioned white services passengers across the sections of each route in order to determine the relevant fare for each passenger type.¹²

The expert for 2 Travel adopted a similar approach in its counterfactual scenario, but some assumptions differed. Instead of allocating passengers based on frequency of bus services, the expert assumed that all white services passengers on single/return tickets, and between 30% and 50% of white services' concessionary passengers, would have travelled with 2 Travel. The fare for fare-paying passengers was determined based on an average of monthly fare data during 2 Travel's period of operation, regardless of the number of zones travelled.

The expert for 2 Travel also applied an additional growth rate to reflect the increase in 2 Travel's market share that it would have been able to achieve between April and December 2004 had Cardiff Bus not engaged

Cardiff Bus routes: allocation of passengers based on share of frequency

The map below shows the Cardiff Bus services that correspond to one of the five routes that 2 Travel operated. Each route is divided into sections, which essentially delineate points on the route where liveried services begin or cease to overlap with the 2 Travel and white services routes, and which correspond to different zonal fares. 2 Travel’s Route 217 (corresponding to the white services Route 117), from Ely to Cardiff city centre, is divided into four sections—shown by the white boxes on the map. Two 2 Travel and two white services buses

(per hour) were planned to operate along the entire route. Two further 2 Travel and white services buses also overlapped on sections three and four near the city centre. Cardiff Bus operated six liveried services on section one, 14 on section two, 19 on section three and 21 on section four. As such, in the absence of white services, 2 Travel’s market share along this route would have ranged from 13% to 25%, and concessionary and single/return passengers are allocated based on the relevant market share for the corresponding section.



Source: Cardiff Bus.

in predatory conduct. This relied on an assumption that, in the absence of white services, 2 Travel would have been able to grow its market share further. The CAT did not accept this assumption.

The CAT’s judgment

The CAT undertook its analysis in three stages. This included an assessment of the period prior to the infringement, the period of the infringement, and the counterfactual scenario. It then considered whether, in the absence of the infringement, 2 Travel would have continued and expanded operations in Cardiff from December 2004 until its actual insolvency.

The CAT stayed close to the facts and undertook its analysis based only on the four services that 2 Travel actually operated between April 2004 and May 2005 (the date of 2 Travel’s liquidation), and did not consider the fifth route, which was never operated. Using an approach similar to that employed by the expert for Cardiff Bus, the CAT allocated the actual number of white services passengers (125,269, excluding those on multi-journey/season tickets) to 2 Travel based on frequency.

Rather than using one of the service scenarios provided by the experts, the CAT developed its own counterfactual scenario by making adjustments to

the data. For example, it doubled the frequency of 2 Travel’s buses to reflect its lower price compared with those of liveried services, the different routing between liveried services and 2 Travel, and the alleged operation of white services immediately in front of 2 Travel’s buses. These frequencies were used to allocate white services passengers between 2 Travel and liveried services, and passengers were then apportioned equally across sections. In order to determine the relevant fare, the CAT divided the total revenue for each white services route by passenger numbers to provide an average fare for white services. It then applied an uplift of 9.3%, to reflect 2 Travel’s higher fares.

Based on the CAT’s assessment that, in the absence of white services, 2 Travel could have attracted an additional 41,255 passengers between April and December 2004 at an average fare (for fare-paying passengers) of almost £0.82 per passenger per journey, the CAT estimated damages of £33,818.79. This is in the range provided by the expert for Cardiff Bus and an order of magnitude less than that claimed by 2 Travel. The CAT determined that 2 Travel is also entitled to interest on this sum, at the base rate of the Bank of England at the relevant time plus 2%. The CAT left it to the parties to calculate the precise amount of interest that is due on this basis.

Relevance of costs

Having reached a view as to what revenue 2 Travel lost as a result of the infringement, the additional costs that the bus operator would have incurred in order to generate that revenue needed to be considered to reach a figure for its lost profits. There was some disagreement between the economic expert for Cardiff Bus and the accounting expert for 2 Travel about the treatment of incremental costs in the counterfactual analysis.

2 Travel argued that it could not operate its registered services in full because of a driver shortage caused by Cardiff Bus's conduct. The expert for Cardiff Bus considered that if, in the counterfactual situation, 2 Travel had operated to its full registered timetable, it would have required extra drivers. These drivers would have constituted incremental costs compared with 2 Travel's costs in the actual situation. The additional driver costs, it was argued, should therefore be deducted from the estimates of lost profit for the counterfactual scenarios in which 2 Travel operated more services than it actually did.

Ultimately, the issue of incremental costs was not directly addressed in the judgment, since the CAT rejected the counterfactual scenario with 2 Travel's additional services.

The role of the tribunal in quantifying damages

The *2 Travel v Cardiff Bus* judgment illustrates the importance of economic evidence in reaching a decision about the quantification of damages. The damages assessments of the experts on both sides had to strike a balance between determining the real damage value as accurately as possible and using approaches that are clear and easy to apply while acknowledging the complexities of the case.

Although the CAT chose to perform part of the analysis itself, it noted that the role of the experts had been helpful in the assessment of damages:

We consider that each of the experts did their best to assist the Tribunal and were punctilious in complying with their obligations, as experts, to the Tribunal. All the experts were assisting the Tribunal in determining what would have happened in the counter-factual scenario, which is a difficult issue that involves the weighing and consideration of multiple factors – including the opinion evidence of the experts. The fact that we have not necessarily accepted the opinion advanced by one or more of the experts in no way diminishes the fact that all the experts were, very professionally, doing their best to assist the Tribunal.¹³

Based on limited factual information and financial data, the experts on both sides broadly agreed on the approach for assessing damages. It is clear from the judgment that, in addition to the experts' analyses, the CAT undertook its own detailed calculations of certain aspects. For example, there was overall revenue and passenger data, but insufficient detail for the revenue figures to determine a precise fare per passenger that reflected the mix of passengers. Each expert made certain assumptions in order to estimate the revenue per passenger. The CAT calculated this in its own way, making slightly different assumptions and arriving at its own estimate of revenue per passenger, and its estimate was similar to that of the experts. The CAT also adopted a similar approach to the expert for Cardiff Bus in considering frequency as the basis for the passenger allocation, but then made adjustments to 2 Travel's timetabled frequencies.

In the end, the CAT used its own assessment as the basis to award £33,818.79 in lost profits, several orders of magnitude less than the £50m that was originally claimed. This raises a question about how the balance between the roles of experts and courts will evolve in future damages calculations. Will other courts go as far as the CAT has in this case in performing its own calculations, or will they instead decide on which scenario they prefer, and then rely on the experts' calculations of the figures in this scenario?

¹ Competition Appeal Tribunal (2011), *Enron Coal Services Ltd (in liquidation) v English Welsh & Scottish Railway Limited*, January 19th.

² Competition Appeal Tribunal (2012), *2 Travel Group Plc (in liquidation) v Cardiff City Transport Services Limited*, July 5th.

³ Office of Fair Trading (2008), 'Abuse of a Dominant Position by Cardiff Bus', November 18th.

⁴ 2 Travel originally claimed £50m, but by the time of the CAT hearing the claim was just over £20m.

⁵ 2 Travel also claimed interest on these damages.

⁶ This head of claim was included in 2 Travel's original claim form, but 2 Travel subsequently accepted that it duplicated its claim for loss of a capital asset and involved double-counting. This separate head of loss was therefore not pursued before the CAT.

⁷ Competition Appeal Tribunal (2012), op. cit., paras 223 and 429.

⁸ The award of exemplary damages is a contentious legal question. The economic and accounting experts did not give an opinion on this issue, and it is not considered in this article.

⁹ This is consistent with the UK Competition Commission's 2011 investigation into the local bus market, which noted that bus passengers usually board the first bus that arrives at the stop. Competition Commission (2011), 'Local Bus Services Market Investigation – Provisional Findings Report', May.

¹⁰ This assumes that passengers and buses arrive at the bus stop at evenly distributed intervals. This seems a reasonable assumption for relatively frequent services, such as those at issue here. Where services are less frequent, passengers are more likely to arrive at the bus stop just before the time indicated on the timetable.

¹¹ The second scenario was the expert's preferred one, as it is consistent with the general finding, also confirmed by the Competition Commission's 2011 investigation, that passengers are generally more time-sensitive than price-sensitive and therefore tend to get on the first bus that arrives at the bus stop.

¹² As data for white services passengers was not available, the proportional split of Cardiff Bus passengers along the equivalent route was applied to white services.

¹³ Competition Appeal Tribunal (2012), op. cit., para 54.

If you have any questions regarding the issues raised in this article, please contact the editor, Dr Leonardo Mautino: tel +44 (0) 1865 253 000 or email l_mautino@oxera.com

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