



EUROPEAN COMMISSION

Brussels, 02.10.2002

C(2002)3578fin

**Subject: State aid No N 264/2002 – United Kingdom
London Underground Public Private Partnership**

Sir,

1. PROCEDURE

1.1. Notification by the UK Government

- (1) In accordance with Article 88(3) of the EC Treaty, and by letter dated 12 April and registered on the 12 April 2002 under reference SG(2002) A/3932, the Government of the United Kingdom notified to the Commission certain arrangements to modernise London Underground by way of a Public Private Partnership (PPP) scheme (hereinafter referred to as to the London Underground Public-Private Partnership or PPP arrangement). According to the notification, the British authorities were seeking confirmation from the European Commission that the arrangements being contemplated are all compatible with the common market and the EC Treaty rules on State aid. The British Government is also seeking confirmation that the consequential amendments of the existing Private Finance Initiative (PFI) contracts and all the new measures constituting a part thereof are in conformity with the EC Treaty.
- (2) By letter dated 21 May 2002 and registered under reference (TREN D/8102), the Commission requested further information on the scheme. Answers to those questions were submitted by the British authorities by means of a letter dated 24 May 2002 and registered under reference TREN A/59368 and by means of various electronic mails addressed to the Commission.

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- (3) In the meantime, various meetings were held by different services of the Commission with the British authorities in order to clarify the various aspects involved in this case.
- (4) By letter dated 19 July 2002 and registered under reference (TREN D/11612), the Commission requested further information on the scheme. Answers to those questions were submitted by the British authorities by means of a letter dated 16 August 2002 and registered under reference TREN A/64814 and by means of various electronic mails addressed to the Commission dated 30 August (with reference TREN A/65331), 3 September (with reference TREN/A 65333 and TREN A/65360) and 19 September 2002 (with reference TREN/A 66479).

1.2. A submission on behalf of Transport for London (“TfL

- (5) By means of letter dated 12 February 2002 and registered under reference TREN A/52897, (TfL) wrote to the Commission to inform that the London Underground PPP arrangements under examination could “raise material issues under EU rules on State aid”.
- (6) TfL is a functional body of the British local authority, Greater London Authority, responsible for transport in London. It will inherit the London Underground as a subsidiary (hereinafter referred to as “London Underground” or “London Underground Limited” (“LUL”) at the conclusion of the PPP process. TfL will have the ultimate responsibility for the implementation of the measures envisaged by the British Government.
- (7) By means of various letters dated 4 April (with reference TREN A/56229), 15 April, 2002 (with reference TREN A/57187), 29 April 2002 (with reference TREN A/57850), TfL submitted further information.
- (8) Other letters were sent to various services of the Commission (dated 7 May with reference TREN/A 58584, 17 May , 4 June, 17 June). These letters were completed with a letter dated 31 July 2002 (with reference TREN A/63795), and a letter dated 23 August 2002 (with reference TREN A/65018).

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2. DESCRIPTION OF THE MEASURES

2.1. General introduction

- (9) The public private partnership (**PPP**) for the London Underground was announced by the British Deputy Prime Minister on 20 March 1998. Its objective is to develop a better Underground through an efficient public sector

operator working with an enhanced infrastructure managed by the private sector. In order to implement this, London Underground has been divided into an operating company (which will remain publicly owned) (London Underground Limited (LUL)) responsible for delivering services to the public, and three infrastructure companies (*Infracos*) (to be transferred to the private sector) providing services under contract to London Underground. Each Infraco will be responsible for a set of three groups of underground lines. 30-year contracts will be signed with the Infracos to maintain, improve and upgrade the Underground's infrastructure for the three groups of lines. Under the PPP procurement process which ensued, the private sector was invited to bid for the acquisition of shares in the Infracos and the conclusion of 30-year contracts.

2.2. Context and UK Objectives for the London Underground PPP

- (10) In the early 1990s, the British Government introduced the Private Finance Initiative (PFI) as a means of securing private sector investment in assets used by the public sector. Beginning in 1995, the London Regional Transport (LRT), a Government-owned entity established under the London Regional Transport Act 1984, entered into a number of separate PFI deals to finance improvements in discrete aspects of its London underground infrastructure and operations, following competitive tendering in each case. These were:
 - (a) *NLTS Contract* (1995) for the provision and maintenance of new trains and related equipment for the Northern Line;
 - (b) *Power* (1998) - for the renewal, upgrade, operation and maintenance of the high voltage electricity supply across the Underground network;
 - (c) *Prestige* (1998) - for the provision and maintenance of a new ticketing system for both the Underground and other LRT services;
 - (d) *British Transport Police Facilities* (1999) - for the construction of certain new police station facilities for British Transport Police and for related support services; and
 - (e) *Connect* (1999) - for the provision of an integrated radio and communications service across the whole of the Underground network, including interfaces with emergency services.
- (11) One further PFI-type deal currently under consideration is the extension of Piccadilly Line to Heathrow Airport Terminal 5, which would involve the construction of an Underground link to the proposed new terminal at London Heathrow airport.
- (12) The notification by the British authorities concentrates on the London Underground PPP scheme (described below in point 2.3.) and also covers the existing PFI contracts (described below in point 2.4.), which are taken into consideration to varying degrees in the PPP.

- (13) The Government's plans for a more widespread modernisation of the Underground by means of the PPP are intended to reverse the deterioration of the system caused by a sustained period of underfunding over the last sixty years. Despite the steady growth of London Underground's operating surplus, it has been insufficient to meet the Underground's investment needs. By 1998, the value of the backlog of work arising from past under-investment was valued at £1.2 billion (€1.9 billion). This means that assets were still being used beyond their design life with consequent increases in maintenance and inspection costs and increasing unreliability.
- (14) Though the PFI mechanism had already been used to fund investment that could not be paid for from the Underground's operating surplus or Government grant, in London Underground's experience it was not well suited to major investment in infrastructure assets across the system where, to avoid fragmentation of management responsibility for assets and to transfer the consequent systems integration risk, a different approach to the introduction of private sector capital was needed.
- (15) The PPP route was therefore adopted to pursue the objectives as follows:
- (a) safeguard and improve service to passengers, with guaranteed safety standards;
 - (b) reduce and eliminate the Underground's investment backlog;
 - (c) deliver genuine transfer of risk to the private sector;
 - (d) provide value for money for the taxpayer through improved efficiency and management; and
 - (e) contribute towards an integrated transport policy for London.
- (16) Development of the PPP has taken place against the backdrop of a fundamental reorganisation of local governance in London. Following an initial White Paper in March 1998, the Government has set up a Greater London Authority (**GLA**) consisting of an elected Mayor of London and a London Assembly to take over responsibility for a number of strategic issues including transport planning for London. On 3 July 2000, following creation of the GLA in May 2000, transport in London became the responsibility of the GLA through a new executive body, TfL.
- (17) However, the Government decided that the Mayor and TfL should not assume responsibility for the Underground until its long term funding was secured under the PPP. The Greater London Authority Act 1999 (**GLA Act**) provides for interim arrangements, under which LRT will exist alongside TfL so that London Underground will remain in Government control until the conclusion of the PPP transaction. Thereafter, LRT will be wound up and responsibility for the Underground will pass to TfL.

2.3. Structure of the London Underground PPP

2.3.1. Division of London Underground

- (18) According to the plan submitted by the British authorities, London Underground will be split into an (i) operating company to be retained in the public sector and (ii) three infrastructure companies, or Infracos, to be transferred to the private sector under the terms of PPP contracts awarded.

2.3.2. The public running of passengers services

- (19) First, under the PPP proposals outlined below, the Underground will continue to be run by a single public sector operating company, which will employ train operators, station staff and line/network controllers ("London Underground" or "LUL" which, as already described, will be controlled by TfL).

- (20) On implementation of the PPP, the operating company, London Underground will:

- retain responsibility for passenger service provision on the Underground, including operation of trains and stations;
- be responsible for collecting and retaining all fares and other revenues (including from advertising, car parks etc.);
- continue to manage the existing network-wide PFI contracts, and any other PFI contracts let before or after completion of the PPP (other than the NLTS Contract, which will transfer to Infraco JNP);
- manage its relationship with the Infracos through the Service Contracts;
- continue with marketing and planning of the whole network;
- take a leading role in ensuring that the PPP arrangements maintain and improve safety in accordance with its statutory responsibilities. For this reason, London Underground will actively concern itself not only with the effectiveness of its own health and safety regime, but also with the way in which the Infracos conduct their asset maintenance and investment activities; and
- participate in changes to Underground standards and operational practices in accordance with a contractual standard setting and change process.

2.3.3. Private management of the infrastructure

- (21) Secondly, the maintenance, renewal, enhancement and modernisation of the Underground's infrastructure, together with raising the financing required, is to be undertaken by the three Infracos. For this purposes, three long-term Service Contracts (30 year-period) will be signed with three private Infracos. Infracos will be obliged to remove the Underground's investment backlog and

modernise the system's assets including rolling stock, track, signalling, stations and escalators during this 30 year-period.

- (22) For these purposes, each Infraco will be granted a lease of the property for which it has responsibility (subject to lease back arrangements to London Underground). The public sector will retain the freehold of the real property elements of the network. During a first transitory phase, however, the Infracos were created as entities within the public sector. In Spring 2000, staff, assets, contracts and other rights and liabilities were transferred to the still publicly owned Infracos by way of a statutory asset transfer scheme under the London Regional Transport Act 1984. Prior to transfer to the private sector, each Infraco will aim at managing its business so as to meet the performance requirements of the Service Contracts and, to the extent practicable, at acting in accordance with the other terms of those Contracts (known as “Shadow Running”).
- (23) In a second phase, private operators become the shareholders of the Infracos. Private companies acquire, for a nominal sum (subject to any adjustments to reflect changes to an assumed balance sheet), the share capital of the relevant Infraco. As a result, Infracos will become private infrastructure companies. The European Commission in its merger decision dated 21 June 2002 examined this operation, as it concerns two of the three Infracos, in case M.2694/ Metronet / Infraco and decided to authorise it because it did not raise any competition concerns. .
- (24) All relevant moveable assets have been transferred to the Infracos (with certain exceptions, including 103 of the trainsets operated on the Northern Line, which Alstom NL Service Provision Limited (*Alstom*) leases from the Finance Parties (*FP*) and 3 of the trainsets operated on the Northern Line which are owned by Alstom. All of the key assets necessary for running the Underground are subject to a special mechanism allowing London Underground, or a successor Infraco, to regain full control of them under specified circumstances, and in any event at the end of the Service Contracts.
- (25) The Infracos were structured around the existing Underground lines. The three Infracos identified were as follows. A consortium was selected for each Infraco (see below).

INFRACO SSL	INFRACO BCV	INFRACO JNP
District Line	Bakerloo Line	Jubilee Line
Metropolitan Line	Central Line	Northern Line
Hammersmith & City Line	Victoria Line	Piccadilly Line
Circle Line	Waterloo & City Line	
East London Line		

Scope of works

- (26) Within the scope of the PPP, Infracos will have to ensure that in the future (i) the existing backlog of asset maintenance and renewal is recovered, enabling London Underground to achieve its performance and safety objectives and focus its attention on delivering high-quality customer service. Further, Infracos will also need to be able to (ii) raise significant finance because the costs of recovering the backlog of maintenance and renewal will not all be covered by Infraco regular revenues in the early years of the contract.
- (27) The principles of the scope of works under the PPP scheme can be summarised as follows:
- (28) Performance: First, wherever possible, payments will be made for defined outputs. These outputs focus on measures which significantly affect customers or London Underground's ability to serve customers. The main performance outputs are for availability¹, capability² and ambience³. Infracos will earn payments related to the scores or levels they reach in these three performance outputs. Infracos' performance will be compared with benchmarks. Further, Infracos must also ensure that a range of facilities for customers and staff such as toilets and clocks are available for use. Infracos are also required to refurbish and modernise every station and each fleet of trains.
- (29) Major station enhancement schemes. Second, London Underground can foresee the need for major development schemes at stations to increase capacity or provide access for mobility-impaired people. Infracos can be required to carry out these works on a case by case basis.
- (30) Asset Management. Third, Infracos must take decisions about when to upgrade, renew or maintain the assets bearing in mind a whole-life cost approach to those assets. The key objective is to ensure the Underground infrastructure is restored to full health and maintained in a condition consistent with good industry practice. Infracos must provide assurance that the maintenance, renewal and investment decisions being taken by the Infracos will deliver both these asset health requirements, and the performance requirements described earlier (availability, capability, ambience, etc).
- (31) Standards. Fourth, in carrying out its scope of works, Infracos must comply with standards in order to ensure safety, define important operational procedures and working arrangements and finally, to ensure technical

¹ Infracos should make the railway infrastructure available in a fit and proper condition.

² Capability is the measure of the potential performance of each line. The higher the capability, the lower the average journey time on that line is.

³ Ambience is the quality of the travelling environment.

compatibility between equipment. Standards have been grouped in various categories.

- (32) Remedies for Poor Performance. Fifth, the PPP has been structured so that the Infracos' economic incentives for achieving their obligations should be sufficient to incentivise good performance. However, there exist a range of remedies should an infraco fail to meet any requirements of the contracts. It is worth noting the following: service points, increased monitoring, corrective action notices⁴, the right for London Underground to step-in where an Infraco fails to comply with a corrective action notice. Further, if London Underground receives substantial and sustained under performance, it may request an extraordinary review. The ultimate remedy is a mandatory sale, under which the contract is transferred to new owners. This is to ensure that a change of management can occur with no break in service under the contract.
- (33) Possibility for variation of the scope of works. Sixth, the PPP scheme is periodically reviewed at 7½ year intervals. Periodic review provides the opportunity for London Underground to reassess its changing service requirements. At the same time, Infracos can re-set their prices to achieve an "appropriate rate of return". The Scheme provides for the re-setting of both requirements and pricing within the 30-year contract period at a periodic interval.
- (34) Extraordinary review. When carrying out their responsibilities, Infracos must be efficient and economic. Infracos have to bear the cost and performance consequences of failing to be efficient and economic. They also bear the impact of net adverse effects which would have befallen even an efficient and economic Infraco up to a pre-agreed limit. Beyond this limit, Infracos can call for an extraordinary review. On its part, London Underground is entitled to call for an extraordinary review where there has been a substantial shortfall in the level of service performance and/or asset stewardship.
- (35) Co-operation and Co-ordination. Infraco and London Underground must co-operate with one another and act reasonably and in good faith in performing the Service Contract. When performing its obligations or exercising a "specified right" (a right to have work done outside the established scope of the PPP), London Underground must act in a manner which is consistent with the key objectives as a whole. If London Underground fails to do so, Infraco can claim compensation for costs and relief from performance.
- (36) Monitoring and Audit. London Underground has wide rights to monitor and audit Infraco's activities for both *financial* and *assurance* reasons. First, information relating to the pricing of variations and other payments due to Infracos is available to London Underground on an 'open book' basis, so that London Underground has full access to the build-up of sums payable. Secondly, Infracos are required to have an assurance regime to demonstrate

⁴ These notices can be used to require the Infraco to correct a specified breach.

that their activities are ‘controlled processes’ as defined under safety control standards and provide London Underground with the confidence that they are complying with their contractual obligations.

- (37) Direction and Control. London Underground’s rights of direction and control under the Service Contract arise in two main circumstances, safety and inadequate performance. First, London Underground has the right to instruct Infraco, or step in, where London Underground believes such action is necessary for health, safety or security reasons. If London Underground exercises its step-in rights, it shall still continue to make the relevant payments to Infraco. Secondly, from a performance perspective, in the event that an Infraco fails to perform its obligations under the Service Contract, London Underground can serve a corrective action notice on Infraco as discussed above.
- (38) Infraco Governance. The Contracts require Infracos to exhibit best practice standards of corporate governance. In addition, there is to be a Shareholders’ Agreement between the private sector shareholders and London Underground which holds a ‘special share’ in each Infraco. In particular, the Shareholders’ Agreement provides for the appointment of an independent, non-executive ‘Partnership Director’, nominated by London Underground, to each of the Infraco boards.
- (39) Risk share. In determining the appropriate contractual risk share, London Underground has been guided by the approach which aims at protecting Infraco from extreme or remote risks, but requiring them to manage a risk portfolio, including a range of risks outside their control. Risk share is delineated and clarified in the text of the contracts. In particular, four major types of risks are defined: (a) revenue risks; (b) cost risk; (c) event risks; (d) default risks.
- Revenue risks: London Underground’s revenue is determined to some extent by the quality of service it delivers, but much more significantly by economic factors, such as the level of employment in London. As Infracos cannot influence this, Infracos are not required to take risk on London Underground’s revenues. Thus, Infraco's revenue risk flows directly from the level of performance they deliver, as measured under the performance regime.
 - Cost risks: Infracos will take the risks of changes in its projected costs. It can look to London Underground to cover additional costs in meeting its performance requirements: through indexation of the ISC for inflation; through the annual usage adjustment payable if London Underground’s operated mileage exceeds a predetermined limit; and if the Infraco incurs additional costs which exceed a threshold defined in the contracts and which could not have been avoided by an efficient and economic Infraco, in which case it can seek an extraordinary review.
 - Event risks: Infracos are not required to take risk on pre-transfer events with potential impact on future costs. Neither do they take risk on unforeseeable

events with major potential cost consequences, such as discriminatory changes in law, safety changes and material damage in excess of certain caps.

- Default risks: These are risks other than those arising through the performance regime. Consequential losses are not payable by Infraco other than in defined circumstances.
- (40) Financing. Further, Infracos must put finance into the scheme. This is important particularly during the first period where the regular payments (described below) to the Infraco will not suffice to meet the funding needs. The amount of finance that each Infraco will require will depend on a number of factors, including cost and performance projections, the method of delivery and timing of line upgrades, balance between committed equity funding and parent company guarantees, and finally the rate at which the ISC increases in later years, including the size of any step-ups relating to line upgrades.

Duration of the schemes under examination

- (41) The scheme under examination will be in place for 30 years. The 30-year PPP contracts will be subject to Periodic Reviews at 7.5, 15 and 22.5 years.

Payment structure

- (42) Regular, four-weekly payments⁵ of an Infrastructure Service Charge (ISC) will be made to each of the Infracos by the public sector operating company (London Underground) over the life of the Service contracts. London Underground will pay the Infracos for their services according to a fee structure that is fixed for the first 7½ years. These fixed basic payments will be subject to adjustment by defined bonuses and abatements relating to performance. The performance factors taken into account will be capability (the maximum capacity of the system); availability (the day-to-day ability of LUL to make use of this capacity); and ambience (the quality and comfort of the system as experienced by passengers)⁶.
- (43) The basic ISC payments are renegotiated during the periodic reviews for the three following 7½ year periods (again subject to adjustment by defined bonuses and abatements). The objectives of the periodic reviews are thus to allow the ISC to be re-set to take account of the possible changing service requirements of London Underground and the changing costs of the Infraco. Further the renegotiated ISC will serve to fully compensate the projected costs of an efficient and economic Infraco and provide for such an Infraco to earn the agreed rate of return.

⁵ Thirteen payments per year

⁶ The ISC payments are based on an improving level of service, which the bidders are targeting. This level of service is in excess of LUL's theoretical targets, and in excess of current performance. In the event that bidders fail to reach their targets, this will have a material effect on rates of return.

(44) It is intended that changes to London Underground's requirements and Infraco's payments will be agreed by the parties working together. If it is not possible to reach agreements, either side can make a reference to a PPP Arbiter. The purpose of the provisions relating to the PPP Arbiter is to reassure the parties that differences between them about the price to be paid to the Infracos can be resolved independently, swiftly and with certainty. The amended ISC should normally reflect changes in requirements and costs, to a level that an efficient and economic Infraco following good industry practice would require.

(45) The submission shows that the average annual value of the ISC payments (in millions of pounds, at 2002 prices) for each Infraco will be as follows:

	JNP	SSL	BCV
<i>first 7½ year years</i>			
Average basic annual payment to the Infraco	£439m	£363m	£299m
Average annual performance adjustment (likely range)	worst: -£25m best: +£11m	worst: -£8m best: +16m	worst: -£1m best: + £25m
Average total annual payment	between £414m and £450m	between £355m and £379m	between £298m and £324m
<i>full 30 years</i>			
Average basic annual payment to the Infraco	£356m	£323m	£275m
Average annual performance adjustment (likely range)	worst: + £70m best: + £100m	worst: + £38m best: + £60m	worst: + £28m best: + £47m
Average total annual payment	between £426m and £456m	between £361m and £383m	between £303m and £322m

(46) London Underground wants to overcome the investment backlog on the network as soon as possible. The ISCs available during the first 7½ year period will not cover the full costs of work to be done during that period. Therefore, the private sector Infracos will finance some of the works themselves – with the cost being paid back through higher ISCs during the remainder of the

contract. From the submission, the value of the work to be funded in this way (in Net Present Value terms) appears to be approximately £700m (JNP), £640m (SSL) and £570m (BCV).

- (47) An estimation in net present value terms for the whole 30 year period of the total value of ISC can be summarised, for each of the three Infracos, as follows⁷:

Evaluation price at	Infraco JNP (millions)	Infraco SSL (“sub-surface lines”) (millions)	Infraco BCV (millions)
7½ years	£3758 (€5825) ⁸	£3056 (€4737)	£2607 (€4041)
30 years	£6378 (€9886)	£4836 (€7496)	£4135 (€6409)

- (48) In addition to the ISC (which is the Infracos’ main revenue stream), certain exceptional sums may become payable during the course of the PPP contract. These sums include the payments for major items such as LUL Specified Rights (i.e. projects which LuL has the right to request the Infracos to undertake but which are not included in the original specification contained in the PPP contract) down to minor items.⁹ These payments are to be made separately rather than through the ISC, as the amount cannot be specified at the outset.
- (49) The Government will back up (by means of a funding structure to TfL plus a series of guarantees) the payments linked to the PPP arrangements. The current policy is that central Government funding for TfL should take the form of grant. The sum corresponding to this grant will take account of the obligations of LUL under any PPP, and existing PFI contracts. In particular, it is the intention that this element of grant should be based on the difference between LUL’s Net Revenues¹⁰ and the Infrastructure Service Charge payments. An additional provision will be made as necessary to reflect LUL’s commitments under the PPP contracts in relation to Infrastructure Company expenditure on Safety Change and Qualifying Change of Law provisions. The British

⁷ All figures represent Net Present Values (NPV) as calculated by the UK authorities.

⁸ Rate of exchange taken 1.55 € = 1 Pound.

⁹ Such as cleaning equipment for delivery to the London Transport Museum

¹⁰ Net Revenues is the difference between LUL’s projected revenues and overall costs of the Operating Company. These LUL’s costs reflect the normal day-to-day operation of the Underground as well as costs associated with the PPP and existing PFI contracts.

authorities also intend to include provision for the exercise of LUL specified rights. Finally, a reserve provision from which to manage LUL's business risks will also be granted. These measures will also be accompanied by certain guarantees that can be regarded as being in favour of LUL. In particular, it is worth quoting a "parent company guarantee" of LUL's obligations given by LRT (which will be taken up by TfL when LUL is transferred to TfL).

Other measures potentially capable of being construed as compensation within the context of the above PPP schemes

(50) This Part sets out a brief summary of a number of contractual and other measures or provisions, which are part of the arrangements under examination and that, could potentially be relevant for the purpose of this decision.

(51) The principal measures can be summarised as follows:

- a "parent company guarantee" of the publicly owned company London Underground's obligations given by the public body, London Regional Transport (LRT) (which will be taken up by TfL when London Underground is transferred to TfL);
- provisions specifying payments to be underpinned by the public company London Underground in the event of a mandatory sale of a Service Contract following: (i) breach of the Contract by Infraco or by London Underground; and (ii) each 7½-year Periodic Review, where this becomes necessary either due to changes required by London Underground which increase the risk borne by the Infracos or lead to a requirement of additional financing, or due to Infraco being unable to raise financing to continue its existing obligations;
- a "non-legally binding comfort letter" issued by the UK Government to the bidders' funders, which makes statements about the Government's current intentions and likely reaction to certain eventualities. In particular, the Secretary of State states that in the event that London Underground was unable to meet its financial obligations under any PPP contracts, he regards it as untenable that (i) he would not consider whether it was appropriate to adjust the transport grant for the GLA or make payment of a special grant; (ii) he would not take London Underground's financial obligations in respect of sums owed by Infraco to the lenders into account; and (iii) he would stand by and do nothing in those circumstances. The letter also states that in circumstances where the Novation Price (which could include the Grossed-up Underpinned Amount) becomes due and the Secretary of State determines that an amount of grant should be made in respect of meeting that liability, it is the intention of the Secretary of State to seek that payment of such amount be made direct to the lenders' security trustee. The Government's willingness to contemplate a comfort letter of this nature was known to the bidders participating in the tender for the PPP prior to the BAFO stage.

- an Extraordinary Review procedure which enables Infracos to obtain additional compensation where the net adverse effects of increased costs and/or decreased revenues exceed agreed thresholds, provided that the Infraco in question was operating in an efficient and economic manner;
- measures, including a letter from the Government to London Underground confirming that the Government would expect to be prepared to provide the necessary funding to London Underground, dealing with compensation for increased costs arising from a change in law or safety requirements, which are outside of the Infracos' control;
- requirements on London Underground in the event of changes of control;
- the avoidance of certain charges in respect of services required by the Infracos in order to perform the Service Contracts (i.e. avoiding circulating charges);
- certain changes to the legislative regime in respect of taxation, property law and insolvency;
- restrictions on the Infracos' ability to dispose of or grant security over key assets which are required to be returned at the end of the Service Contracts, in order to preserve the ability to provide the infrastructure services which are the subject of the London Underground PPP; and
- payment of bid costs.
- [...]*

Ownership of the assets pursuant to the PPP arrangements

- (52) Under the PPP Schemes, London Underground Limited-owned assets will pass under the control of the Infracos. In order to achieve the transfer, real property is leased to the Infracos and, where necessary (e.g. at stations), leased back to LUL. New and replacement assets will remain the property of the Infracos, subject to an applicable "hand-back" scheme.
- (53) The principle underlying the asset ownership regime of the PPP is that the Infracos will, with very limited exceptions, only be entitled to use PPP assets in order to provide services to LUL under the terms of the PPP contract.¹¹

* Confidential information. It refers to the negotiations between the British Government and the EIB of various aspects in respect of loans to be granted to the London Underground PPP project).

¹¹ For the most part, Infracos are not entitled to undertake any business, operations or activity other than for the purpose of performing their obligations under the PPP contract. The very limited exceptions to this prohibition are (a) where reasonably required to perform an ancillary agreement

Equally, LUL should at all times be able to take back a fully functional business including all the assets required to continue to provide the infrastructure services currently provided by the Infracos.

2.4. Other contractual arrangements ancillary to the PPP schemes

- (54) The UK Notification also refers to various arrangements amending a series of existing contracts (the so-called Private Finance Initiative (PFI) contracts). It is worth noting in particular the arrangements relating to Northern Line Trains Contract (NLTS Contract) and other pre-existing PFI deals (Power, Prestige, British Transport Police facilities, Connect). They are described below.

2.4.1. Northern Line Trains

- (55) The series of contracts collectively known as the NLTS Contract (which, inter alia, include the Usage Contract and the Direct Leases) were entered into in 1995 by the company NL Service Provision Limited (*Alstom*) and the Finance Parties (*FP*) following a process starting with a call for competition in the OJEC¹²). Alstom is responsible under the NLTS Contract for providing trains and equipment to London Underground to a defined standard, capacity and capability every day. The NLTS Contract is for a primary period of 20 years. Not less than 18 months before the end of this primary period, London Underground can opt to end the NLTS Contract at the end of the primary period by payment of a fee or continue the agreement for a secondary period of a further 10 years. Thereafter, London Underground can opt for a further period of extension. London Underground is entitled voluntarily to terminate the NLTS Contract at any stage subject to a substantial termination fee (which in practice means this right would only be exercised in extreme circumstances).
- (56) The outline of the transaction is as follows. The current financing arrangements involve UK tax leases between the FP and Alstom in respect of 103 train sets and certain train-borne and trackside equipment (the *Head Leases*). Alstom makes available the trains (which include the 103 trains referred to above and 3 trains owned by Alstom) and equipment to London Underground under the *Usage Contract*. London Underground makes payments for the use of the trains and equipment to Alstom under the Usage Contract, which payments are used by Alstom to pay rentals to the FP under the Head Leases. London Underground has entered into direct leases with the FP to guard against the risk that the FP could terminate the Head Leases (and thereby deprive London Underground of trains and equipment) as a result of a default by Alstom which is not caused by a default of London Underground

or a centralised service agreement (in other words, subsidiary PPP agreements) or (b) where it consists of supplying services to other members of the Infraco's group, provided that certain conditions are met.

¹² See in particular: Doc-ref. 21535, OJ S 066 and Doc-ref. 49842-92, OJ S 243.

under the Usage Contract. Other related material contracts include two train depot leases.

- (57) Pursuant to the PPP arrangement, London Underground's interests under the NLTS Contract will be transferred to Infraco JNP (the Infraco responsible for the Northern Line) because train provision and maintenance will be the responsibility of the Infracos under the PPP.
- (58) However, as a new private sector entity with limited financial history, Infraco JNP represents a much greater credit risk for Alstom and the FP than London Underground. Thus London Underground agreed changes to the NLTS Contract, in particular to the effect that if Infraco JNP were to fail to perform any of the obligations that it owed to Alstom and/or the FP, either Alstom or the FP could oblige London Underground to perform such obligations at their request (*Step-in*). These deals also include additional security, amendment/release of certain financial covenants.

2.4.2. Other pre-existing deals

- (59) The other pre-existing PFI deals (Prestige, Power, British Transport Police, Connect) will remain with London Underground following the PPP arrangements. These contracts were awarded following a process starting with a call for competition in the OJEC (see above). Certain obligations under the PFI contracts are passed onto the Infracos via back-to-back obligations which are set out in the Schedules to the PPP Service Contracts. It is worth noting the following deals:

2.5. Selection of the private Infracos in light of the PPP arrangements

The winning consortia

- (60) The consortia selected for the Infracos are Tube Lines Limited for Infraco JNP Limited (*Infraco JNP*); and the Metronet Consortium for Infraco BCV Limited (*Infraco BCV*) and Infraco SSL Limited (*Infraco SSL*)¹³.
- (61) Each consortium is made up of a series of shareholders drawn from the industries of construction, engineering, rail services, project management, etc.
- (62) In particular, the shareholders of Tube Lines Limited are affiliates of the following companies: (i) Amey Plc, a construction and engineering group engaged in constructing and maintaining railway assets; (ii) Bechtel, Inc. an international construction, engineering and project management group; and (iii) Jarvis Plc, a facilities management company providing outsourcing solutions both in the private sector and through PFIs and PPPs.

¹³ The Metronet Consortium is proposing to hold the shares in the two Infracos via Metronet Rail BCV Holdings Ltd and Metronet Rail SSL Holdings Ltd.

- (63) The participants in the Metronet Consortium are affiliates of the following companies: (i) Balfour Beatty plc, which operates in building, building management and services, civil and specialist engineering services, rail and engineering services, investments and developments; (ii) Bombardier Inc, a Canadian corporation engaged in design, development, manufacture and marketing in the aerospace, rail transportation equipment and recreational product industries; (iii) SEEBOARD Group plc (part of the American Electric Power Company Inc. group), whose principal activities are the distribution and supply of electricity, gas supply, electricity generation and electrical contracting; (iv) Thames Water plc (part of the RWE group), engaged in water and waste operations management; and WS Atkins plc, engaged in the provision of professional, technologically based consultancy and support services.

Summary chronology of the tender process

- (64) These consortia were selected according to a negotiated tender process described below. In particular, a summary chronology of the tender process observed by London Underground in relation to the PPP is as follows:
- A Periodic Indicative Notice (PIN) was published on 21st July 1998 concerning the United Kingdom Government's proposal to implement the PPP for the London Underground. The PIN referred to a more detailed description of the proposal contained in the Deputy Prime Minister's Parliamentary statement of 20.3.1998 and the Government's White Paper entitled "A mayor and Assembly for London" of 25.3.1998. The Notice invited potential partners to apply for a briefing pack. Information contained in the pack gave an outline of the Government's proposal for the PPP, namely, "The infrastructure contractors will be under an obligation to eliminate the investment backlog and to maintain and modernise the Underground trains and other assets such as track signalling, stations and escalators. There will be a performance regime with incentives and stiff penalties".
 - **24th March 1999:** London Underground published a Periodic Indicative Notice (PIN) in the OJEC, stating that it was its intention to issue a "call for competition" for the provision of all infrastructure services necessary to enable London Underground to operate its railway network, and the provision of necessary funding.¹⁴
 - **19th June 1999:** London Underground issued a call for competition in the form of an OJEC Notice.¹⁵ This Notice was issued "on a voluntary basis". This invited candidates to apply to pre-qualify as bidders for the "deep tube lines",

¹⁴ 99/S 58-37515/EN of 24.03.1999.

¹⁵ 99/S 118-87811/EN of 19.06.1999.

i.e. BCV and JNP. According to the notification, in light of the size and complexity of the project, London Underground chose to adopt the negotiated procedure approach to the conduct of the tender. This notice did not describe the detailed aspects of the services and/or works that were to be the object of the PPP contracts.

- **October 1999:** London Underground announced the bidders that had pre-qualified for the BCV and JNP competitions. These were four consortia in respect of BCV (Metronet, Linc (London Infrastructure Consortium), NewMetro and TubeRail), and another four in respect of JNP (Metronet, Linc, Tube Lines and TubeRail). Invitations to Tender (ITT), as well as a draft of the Service Contract, were issued to the pre-qualified bidders on 19th October 1999. By this date, the Infracos (which were incorporated as three limited liability companies under the Companies Act 1985, wholly owned by London Underground) had been set up to implement the detail of the PPP and undertake initial “shadow running” within London Underground.¹⁶
- **31st December 1999:** London Underground issued a call for competition in the form of an OJEC Notice, inviting candidates to apply to pre-qualify as bidders for the “sub-surface lines”, i.e. SSL. As with BCV and JNP, the negotiated procedure was adopted (see above on 19th June 1999).
- **March 2000:** bidders submitted tenders for BCV (bids were received from Metronet, Linc and TubeRail) and JNP (bids received from Metronet, Tube Lines and TubeRail).
- **July 2000:** the bidding consortia short-listed for the BCV and JNP competitions were announced. In respect of BCV, the two bidders were Linc and Metronet; for JNP the two bidders were Tube Lines and TubeRail.
- **September 2000:** bidders submitted tenders for the SSL competition. There were wide differences in the bidders’ approaches to meeting line upgrade requirements, and all bidders were short-listed. Accordingly, Metronet, Linc and Sub Surface Lines Group remained in the competition.
- Following evaluation of tenders by LRT and London Underground, the remaining bidders in all three competitions went through a period of due diligence. The bidders carried out visual inspections of assets, discussed issues with Infraco managers and staff and reviewed documentation made available to them via a data room. They were also able to ask for further information through a tender enquiry process. There also followed legal and commercial negotiations between London Underground and the bidders, and a series of detailed technical negotiations. These were to enable the bidders, in due course, to establish a price for their “Best and Final Offers” (*BAFOs*).

¹⁶ This shadow running with still three publicly owned Infracos can be regarded as a transitory period.

- **November 2000:** the BCV and JNP bidders submitted BAFOs. The BAFOs, which were evaluated by London Underground and professional advisers, all contained contractual mark-ups, which were considered unacceptable to London Underground, and were also qualified to some extent. According to the UK notification, while the bids offered value for money, as guided by a comparison with the cost of retaining the Infracos within the public sector – the Public Sector Comparator (*PSC*) - they implied a level of Government grant that was unacceptable to Government/London Underground. The bidders were asked to submit re-priced proposals for the purposes of affordability, which were received in January 2001. These affordability constraints were London Underground’s best estimates at the time of the level of ISC to which it expected to be able to commit.
- **February 2001:** the SSL bidders submitted BAFOs.
- **Capability resubmission–December 2000- January 2001.** In evaluating the BAFOs, London Underground formed the view that the bidders had used unrealistic assumptions about train and power systems. Each bidder was therefore required to provide a “capability resubmission” providing more detailed information about its plans, in order to ensure that they addressed certain key technical requirements.
- **2nd May 2001:** the LRT Board made a final decision on preferred bidders for BCV and JNP, which was announced on the same date. The decision followed a period of statutory consultation with the Mayor and TfL under section 298 of the GLA Act. As mentioned above, the preferred bidders selected were Metronet for BCV and Tube Lines for JNP.
- **19th September 2001:** the preferred bidder for SSL was announced as Metronet.
- **January 2002:** Conditional final offers (CFOs) were presented by each of the selected bidders.
- **February 7, 2002.** London Underground announced that negotiations had concluded and that contracts had been finalised, and that contract award would take place after the conclusion of required consultation with the Mayor and Transport for London.
- **March 22, 2002 and April 16, 2002.** Pursuant to negotiations with the selected bidders, further revised contracts were adopted .

The criteria for the selection of the bidders

- (65) The Calls for Tenders did not contain a detailed description of the works/services/supplies. However, at each stage of the bidding process London Underground provided information to bidders. For example, the prequalification documents were accompanied by a briefing document. This described the underlying principles of the transaction and the asset base that

the Infracos would inherit. At various stages (i.e. ITT), the documentation was expanded.

(66) The selected tender process was a negotiated one as described in the OJEC notices. In addition the ITT:

(a) stated that “the information in the ITT may change as a result of a further development of the PPP structure prior to or during tender evaluation and subsequent negotiations with bidders”; and

(b) contained a requirement that bidders should identify any required amendments to the contract and other documentation and that “...any amendments which indicate that it will be unlikely that London Underground and the bidder will be able to negotiate a contract acceptable to both parties within a reasonable timetable will not be entertained...”.

(67) According to the notification, the initial tenders were evaluated in four areas:

(a) technical/safety, (b) organisational, (c) financial and (d) legal/commercial . For the first two of these areas, the evaluation criteria were as follows:

a) technical: bidders were required to show a high level of coherence, experience, innovative thinking and internal consistency in the proposals in relation to performance, asset management, health, safety and the environment, and working methods.

b) organisational: bidders’ proposals were evaluated to the extent to which they provided, in particular, evidence of a well-considered management approach overall.

c) The financial evaluation considered the financial impact of each bid on London Underground, both in terms of the ISC and any implied increases or decreases to London Underground’s operating costs as a result of accepting the bid. In a parallel manner, evaluation of the bids identified a number of areas that required clarification with bidders prior to short-listing. In addition to comparing the bids against each other, a financial comparison of the cost of the bids against the PSC (both on the basis of traditional financing and of bond financing) was undertaken

d) The legal/commercial review assessed the impact of the bidders’ mark-ups of the draft contractual documents.

(68) London Underground’s evaluation of BAFOs remained essentially as above, although, according to the notification, the emphasis changed to reflect the pre-existing knowledge and experience which London Underground had of the bidders and their proposals. The BAFO bid requirements were specifically designed to test coherence and integrity, and bidders were required to:

(1) update and re-submit the key principles of their asset management regimes, recognising subsequent work completed on the technical

case studies and information and experience gathered as part of due diligence;

- (2) update work plans;
- (3) re-submit case studies developed as part of the technical engagement process; and
- (4) provide updated details of the impact of the bids on London Underground's operations (e.g. cost impacts such as increasing train numbers, which would increase London Underground's train operator requirements).

(69) Negotiations with preferred bidders followed their selection. These negotiations gave rise to certain changes if compared with previous phases of the tendering procedure. These changes can be described as follows:

(a) **Refinements relating to the capability targets.** Some of the Journey Time Capability target scores, along with their Earliest and Latest Implementation Date (dates for the implementation of the works) have been modified. The key modifications are:

- The Victoria, Bakerloo and Sub-Surface Lines Journey Time Capability targets have been reduced due to the power constraints;
- The Victoria Line Latest Implementation Date (i.e. date for completing the works) for the full line upgrade has been moved to 1/9/2012;
- The Jubilee Line interim upgrade has been removed leaving a single upgrade with a Latest Implementation Date of 31/3/2009 (brought forward when compared to the original full line upgrade). This interim upgrade will now be dealt with as an LUL Specified Right;
- As a result of bringing forward the full Jubilee line upgrade the Northern line upgrade has been deferred to a Latest Implementation Date 31/3/2011;
- SSL upgrades are to be done in 3 stages with Latest Implementation Dates of 31/3/2011, 31/3/2014, and 31/3/201 respectively.

(b) **Refinements relating to the treatment of performance abatements due to “delay events”.** Delay events are events outside the control of the Infracos, such as Force Majeure that may impact on the delivery of Specific Projects. Two refinements have been identified:

- Originally, Infracos would obtain full relief from performance abatements in the case of Delay Events impacting on Line Upgrades but only 50% relief from performance abatements where Delay Events impact on Station & Train Refurbishment or Modernisation. The transaction documents have been

modified to state that Infracos will now get full relief from abatements for late delivery due to Delay Events affecting Train & Station Modernisation, Train & Station Refurbishment, Enhanced Station Refurbishment, Station Accessibility Projects as well as Additional Projects.

- At BAFO, abatements for the late delivery of projects were cumulative. In the latest set of contract documents, an Infraco, no longer is obliged to pay separate abatements for late Train Refurbishment deliveries if the deadline for the refurbishment coincides with a deadline for a Specified Line Upgrade on the same line.

(c) **Refinements relating to the measurement of performance.** Under the PPP, contractual performance is measured by system outputs (*availability*, measured by nominally accumulated Lost customers hours; *capability*, measured largely by theoretical journey times; and *ambience*, measured by various objective criteria and mystery shopper surveys of noise, cleanliness and similar matters. Bonuses and abatements are payable by LUL depending on how actual Underground performance compared to benchmarks set in the contract.

In particular the following refinements were introduced:

- Relating to availability (Temporary speed restrictions –TSR): TSRs are normally imposed where track quality needs to be improved. They require trains to run more slowly which causes delays to customers, yet delays improve dramatically as the track is replaced. The refinement reduces the potential impact of temporary speed restrictions imposed by the contractors on the performance penalties they incur.
- Relating to availability: Bonus payments are calculated on the basis of time delays experienced by passengers and attributable to the Infraco being less than the Benchmark. Originally, these bonus payments would only be paid for performance up to a cap (set at 65% less delays than the Benchmark performance). Beyond this cap, no further bonus payments would be made to Infracos for improving availability performance. The cap has now been removed. Infracos will continue to receive a bonus payment whenever it performs better than its Benchmark.
- Relating to availability: A new Service Point regime has been introduced to deal with overrunning engineering works. Service Points (a sort of negative points which may give rise to bonus abatements) will be awarded for every minute that the engineering works overrun into LUL's service hours, up to a maximum of 120 minutes. This regime will include all disruptions to services caused as a direct result of Infraco's

works being extended beyond engineering hours without agreement.

- Relating to availability (introduction of a Service Points threshold for Fault rectification faults): Under the Fault Rectification regime Infracos have a specified time for clearing different types of faults, called the Standard Clearance Time (SCT). Where Infraco takes longer than the SCT they are awarded Service Points (negative points giving rise to bonus abatements¹⁷). Originally Infracos were able to apply for an Extended Clearance Time (ECT) in cases, where for good reasons such as requiring booked access or specialist materials or equipment, they were unable to achieve the SCT. After Shadow Running, it has been decided to remove the ECT process for Fault Rectification and replace it with a clearance time threshold, based on current network performance.
- Relating to availability (Fault rectification – rolling stock faults): During the first 12 months following transfer to private bidders, Infracos will not suffer penalties for rolling stock faults or rolling stock cleaning faults that do not result in disruptions to services (grace period granted).
- Relating to requests for change of customer information: Under the transaction documents, Infracos have always had an obligation to deal with LUL's requests for changes to customer information on stations and trains. After Shadow Running, it has been decided to introduce a separate regime to measure fault rectification for requests for changes to customer information for Trains and Stations.
- Relating to the obligations for refurbishment and modernisation: The affordability review resulted in the period between station refurbishments being extended from 5 years to 7 ½ years. Some station modernisations are being replaced by station refurbishments. There is a new category of "Enhanced Station Refurbishment". This requires more extensive renewal of floor, wall, ceiling and staircase finishes than the scope of the normal station refurbishments. An abatement regime for non or late delivery of Enhanced Station Refurbishments of £125,000 per payment period after the date when the refurbishment should have been completed has also been introduced.
- Relating to the obligations for refurbishment and modernisation: Under the transaction documents, Infracos are

¹⁷ Each Service Point can result in an abatement of £50.

subject to abatements for late delivery of Station or Train Refurbishment or Modernisation. Originally the regime did not take account of the fact that the work may be virtually complete with only a few 'snagging items' to be cleared. Under that regime Infracos could still suffer the full abatement under these circumstances. The concept of "Practical Completion" has now been introduced to the transaction documents to allow for earlier delivery of refurbishment and Modernisation works where only snagging items are outstanding. A list of outstanding snagging items is required to be agreed and all items on the list cleared within 4 payment periods of Practical Completion. If snagging items are not cleared by then, abatements of £10,000 per payment period are imposed on Infraco. Snagging items in existence after 10 payment periods are to be dealt with under Facilities or Fault Rectification processes.

- Relating to ambience. Historically LUL has not cleared all graffiti from track-side structures, mainly due to affordability reasons. The transaction documents originally required that all track-side structures be free of graffiti and unauthorised stickers. The transaction documents have been modified to reflect the provision that trackside structures shall be clean and free from *Offensive Graffiti and Stickers*, and that non-offensive graffiti is to be dealt with under Minor Works. Non-offensive graffiti should however be removed where repair etc. is being carried out by the Infracos on track-side structures.
- Relating to trains ambience. Originally, most of the Trains Ambience regime was to be subject to the Mystery Shopper Survey (MSS) used for all other ambience attributes. However, 5 attributes, Ride Quality, Noise, Lighting, Heating & Ventilation and Quality of PA were to be subject to technical tests. In view of technical difficulties in identifying the technical test for measurement, the 5 ambience attributes will, for the first 12 months of the transaction documents, be measured under the MSS regime and a methodology to measure these areas of performance is to be agreed between LUL and the Infracos to allow a new regime to be introduced thereafter.
- Relating to Trains ambience: Originally, there were Station Minimum Ambience Targets for each station so that if Infraco performance fell below this level they would be allocated Service Points and therefore suffer abatements. This regime was there to protect small stations as aggregate Ambience performance is calculated using weightings based on passenger numbers. However, there was no equivalent regime for Trains. Minimum Ambience Targets for Trains have now been

introduced for each Line, to protect the smaller train fleets. 1000 Service Points per payment period per Line are to be awarded to Infracos for each point they fall below the Trains Ambience Minimum Target.

- Relating to minor works. Initially, London Underground could require Infracos to perform works, not otherwise required under the PPP contract, which have a value of less than £ 10,000, subject to a maximum of £2 million per contract year. The annual allowance for minor works has been increased to £4 million per contract year, and the limit for each minor works job increased to £20,000.
- The introduction of the concept of intermediate works. Infracos may now be required to implement intermediate works which are works with a value over £ 20,000 but less than £5 million, with a maximum aggregate value of £5 million per annum. Funding for intermediate works is not included in the base ISC payable to Infracos and thus was not bid for as part of the baseline ISC. Under the new regime Infraco provides a cost estimate for it providing the Intermediate Works within 30 days, although LUL can procure the works from an alternative provider if that alternative provides better value for money. If Infraco provides the works it has to deliver them within 6 months (longer if agreed by both parties). If LUL has used an alternative provider, once completed Infraco will subsequently be responsible for maintenance. Service Points are awarded for a delayed cost estimate, and/or for late delivery of Works (if provided by Infraco).
- Relating to the limits on London Underground before the use of contractual remedies (i.e. step-in notices, corrective action notices, etc). From the start it was envisaged that these remedies could only be used, in cases where the Infraco availability, ambience or facilities faults scores fell to the Unacceptable level, if the problem was not corrected within 3 payment periods and - if worse than a Benchmark level - within 10 periods. After the modifications, these restrictions on the use of these remedies are also valid for the Capability performance criteria.
- Relating to train declaration. The transaction documents have been renegotiated so that while a declaration of trains as available for bringing into service will normally take effect 12 months subsequent to the date on which the declaration is made, now, if London Underground and Infraco agree, the declared trains can enter service earlier. This should allow London Underground to utilise the additional trains earlier for the benefit of its customers. Infraco will accrue the

corresponding payment adjustment from the time the new trains enter into service.

- Relating to Capability: Capability is the measure of the potential performance of each line, the higher the capability, the lower the average journey time on that line. Tests are to be carried out to measure capability performance. The transaction documents have been modified so that Capability tests are not carried out in the event that any asset is not available or defective through loss, destruction or damage arising out of any of the circumstances set out in the Fault Attribution Rules (i.e. performance adversely affected by factors outside of Infraco control, such a depot or whole section of line not being available due to a terrorist attack).

(d) **Refinements relating to the asset management.** The so-called “Grey Asset” regime has been revised. Under the contracts, assets whose condition is unknown (called Grey Assets) are to be brought up to an improved condition. At BAFO the requirement was that by the end of the first review period, the Grey Assets along with the other Assets would be required to meet the relevant benchmarks. In discussions with bidders, LUL was told that such a risk could not be accepted and it was decided that the requirement should be amended so that Grey Assets are only to be put into a safe condition until the next review (not improve then). The obligation to improve their condition to set levels will now not apply until the second review period.

(e) **Refinements relating to termination of the contracts.** The contracts define the situations in which the relationship between London Underground and Infraco can end before the expiry of the Service Contract (Infraco or London Underground default). Compensations payments are foreseen. Certain of these arrangements have been developed. In particular:

- Infraco defaults. The documents now include circumstances where Infraco is in default of its lending agreements;
- London Underground (LUL) defaults. The events of default have been modified to include a LUL Default where there is a material failure by LUL to comply with its obligations under the transaction documents. The contracts also include another default event where Infraco’s assets have been nationalised or a change in law renders it impossible for the Infraco to comply with its obligations.
- Modification of the amount to be payable to Infraco in case of Infraco Default. The “Underpinned Amount formula” (payable on Infraco Default) has been revised. In the original formula, performance was assumed not to improve throughout the remaining contract term. In the new formula, the lack of

improvement is only assumed to last for 7.5 years, but with Infraco suffering a deduction equal to the additional costs that it would have incurred to restore performance to the required benchmarks.

- Modification of the minimum amount that is payable to an Infraco on Infraco Default and that is underpinned by London Underground Limited (the so-called "Grossed-up Underpinned Amount value). The transaction documents originally provided for an "adjusted fair value" to be paid by London Underground Limited in case of Infraco fault. According to the submission, bidders were unhappy with this position, as lenders were unsure of the protection this offered them and wanted more certainty. As a result, a "floor" of 90% of approved debt (minimum amount to be paid to Infracos in case of Infraco default) was introduced in time for the BAFO. This was subsequently increased to a floor set at 95% of approved debt plus all reimbursable law & safety change costs. In both cases, the cap of maximum amount payable has remained constant (at 100% of approved debt plus approved mezzanine debt and any amount of tax which would be payable on those amounts).

- (f) **Refinements relating to payments for costs related to safety and law changes.** The contract documents provide for the payment of costs stemming from unanticipated safety and law changes. Up to a threshold, the Infracos will pay, and will later be reimbursed. For costs above the threshold, LUL will pay directly. The threshold has changed (from £200 million per 7½ year review period to £50 million in each individual year). The timing of reimbursement has also changed. Originally, reimbursement was to be through payments during the following 7½ year period. Now, LUL will reimburse the Infracos the following year.
- (g) **Refinements related to asset life expectancy.** Under the transaction documents, long term assets, such as civil assets and track, are required to meet benchmarks in respect of their condition by a certain point in the contract's term. The benchmark levels are set with regard to the current state of the assets and the rate of improvement judged practicable by LUL. Originally steady state benchmark levels had to be achieved by the second review date. After the modifications, the requirement to meet the steady state benchmark levels has been set back to the third review date.
- (h) **Refinements related to liability.** The documents also refer to the liabilities of each party for various types of possible harms. The following refinements have been introduced:
- Liability in respect of harms to the environment. Infracos were originally to be liable to London Underground for any

environmental harm that occurred prior to the Transfer Date, if Infraco failed to take reasonable mitigation measures to control it. This has now been clarified to cover under the liability of the Infraco, any environmental harm identified in an environmental assessment within 2 years of the transfer to the bidders or identified prior to the second Review date.

- Insurance against the risks arising out of contracts of works to cover asset damage, loss, employer's liability, product liability, public liability and professional indemnity. At BAFO, Infracos were required to take out insurance against the risks arising out of contracts of works to cover asset damage, loss, employers' liability, product liability, public liability and professional indemnity. However, when bidders went out into the insurance market to obtain the level of cover they considered they required, the premiums were extremely high. This was mainly due to the effect of the attacks of September 11th 2001. LUL did not want to pay costs for 7½ years based on quotes obtained at such a sensitive time in the market. London Underground decided that better value for money could be obtained if it required the bidders to obtain insurance (in respect of the public section of the policy) up to a specified level, while LUL would use its own insurance cover to indemnify the Infracos for claims in excess of that figure.
- Pursuant to the negotiations, London Underground has now agreed to pay any excess costs for this insurance, over and above an agreed threshold . This change affects the BCV and SSL Infracos only .
- London Underground is responsible for claims that result from its actions before the transfer of the Infracos to the bidders takes place. The cap on the amount London Underground can be required to pay in respect of claims between April 2000 and the date of the transfer has been increased. Previously, London Underground's maximum liability for "claims" under each Share Purchase Agreement was £50 million, except that liabilities for certain disclosed third party claims were not to be subject to this cap. Now, London Underground's maximum liability under the JNP Share Purchase Agreement is £50 million plus £10 million related to tax matters. In each of the three Share Purchase Agreements, the liabilities excepted from the cap are also broader.
- Originally, where a Specific Line Upgrade was delayed due to certain force majeure events, the risk associated with lost Step-up in performance was borne by Infracos and covered by business interruption insurance. As a result of the refinements, London Underground is now assuming this risk.

- According to the initial documents, SSL Infraco would be liable for the consequences of latent defects in the Jubilee line extension. As result of the refinements, Infraco would now only bear the first £2.5 million of the consequences of any latent defects until the end of the second Review period. After that time, Infraco would bear all the risk.
 - Initially, Infraco JNP would assume all risks relating to the Northern Line Train Service Contract (NLTSC). However, at BAFO neither bidder for the JNP contract accepted the risk transfer position. The risks relating to the Northern Line Train Service Contract (NLTSC) have been re-aligned following continued negotiations with the parties to the NLTSC.
- (i) **Refinements related to the PFI Contracts.** A cap has now been introduced on the risks carried by the contractors for claims made by other contractors with whom London Underground previously signed PFI contracts.
- (j) **Refinements related to the scope of the periodic reviews (obligation to provide financing beyond the first review period):** Periodic reviews are arrangements for re-setting London Underground's requirements and Infracos' pricing. The original mechanism provided that any increase in financing required would be addressed by increasing the level of the ISC. Infracos had to obtain all financing required for the project and London Underground was responsible for the costs of that financing to the extent that a Notional Infraco would have incurred those costs. New arrangements have now been introduced. In particular, if London Underground imposes new work or services obligations which cannot be financed, LUL must either adjust its requirements to make them financeable or the agreement is terminated. In such a case the debt is fully repaid and the bidders receive an amount which is equal to their base equity plus their base case return for the period that the contract has lasted plus any other amounts that LUL owes Infraco under the Contract. Furthermore, the same amount is payable in the situation where LUL has not changed its contractual requirements if a Notional Infraco (Economic and efficient Infraco) could not have raised the finance required and therefore the inability to raise finance is due to the market not the Infraco. However, where LUL has not changed its contractual requirements and a Notional Infraco could continue to raise the finance for its existing obligations but the particular Infraco in question cannot, debt is repaid, less a margin. No return on the equity is paid in that case.
- (k) **Wording developed with regards to the limitations on reimbursable costs at periodic review.** If financing is required during the first Review Period above anticipated levels, then at a periodic review, the ISC would not be adjusted to compensate such additional amounts. This approach ensures that risk transfer on costs is achieved

in each Review Period. The wording has now been refined to ensure that when considering future costs the PPP Arbiter allows contingencies in base prices to the extent that they would be required by an Infraco working to Good Industry Practice. To the extent that new finance is required for those future costs, including contingencies, this would be allowed for in the future ISC and additional Fixed Amounts would be allowed for to repay that finance. The new contract wording clarifies this process.

- (l) **Wording developed to interpret the notion of non economic and efficient Infraco.** Under the PPP, Infracos are exposed to the risk of cost overruns and revenue shortfalls attributable to their own mismanagement (referred to as behaviour that is not economic and efficient or alternatively, that is “non E-E”). The Arbiter assesses whether an Infraco is E-E or non E-E every periodic review. Now, the PPP contracts for BCV and SSL give guidance to the Arbiter as to what constitutes an E-E Infraco in respect of certain strategic purchasing decisions taken by the selected bidders.
- (m) Refinements related to the extraordinary review (reduction in Infraco responsibility for cost overruns and revenue shortfalls). The concept of Extraordinary Review was included in the ITT to cater for (1) Infracos suffering net adverse affects during a review period exceeding an agreed threshold and (2) LUL suffering a substantial shortfall in Infraco's levels of service compared with those agreed in the contract. The main modification has been to the threshold above which an Infraco can request an extraordinary review. At ITT the figure was a 20% or greater fall in revenues for a 6-month period where such fall was expected to continue. At CFO it was set at £200 million per Infraco¹⁸, per review period and now it is £50 million per review period for each of BCV and SSL. In the case of JNP, it is set at £200 million for the first review period and £50 million in subsequent periods.
- (n) **Refinements related to the costing of the works to be done.** Price adjustments (expressed in terms of ISC) for the work to be carried out by the selected bidder under the arrangements have occurred. In particular, initial evaluation prices at BAFO by the selected bidder and evaluation prices at CFO of the selected bidder are as follows for the three Infraco:

Evaluation price (millions)	Evaluation price at BAFO by Tube Lines (selected bidder) for	At the Committed Final Offer (CFO) :	% Difference
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¹⁸ Infracos would be responsible for cost overruns and revenue shortfalls that even a well-managed Infraco would have incurred up to £200 millions.

for the period ¹⁹	Infraco JNP	JNP (Tube Lines)	
7½ years	£3465 (€ 5370)	£3758 (€5825)	+ 8%
30 years	£6025 (€9338)	£6378 (€9886)	+ 5.8%

Evaluation price for the period	Evaluation price at BAFO by Metronet (selected bidder) for Infraco SSL	AtCFO: SSL (Metronet)	% Difference
7½ years	£3440 (€ 5332)	£3056 (€4737)	- 12%
30 years	£4625 (€ 7169)	£4836 (€7496)	+ 4.5%

Evaluation price for the period	Evaluation price at BAFO by Metronet (selected bidder) for Infraco BCV	At CFO: BCV (Metronet)	% Difference
7½ years	£2585 (€4006)	£2607 (€4041)	+ 0.8%
30 years	£3730 (€5781)	£4135 (€6409)	+ 10%

- (o) **Refinements related to the “agreed rate of return”.** Under PPP, when reviewing the ISC every periodic review, the arbiter will need to take into account the “agreed rate of return” (return that the selected bidders are to receive for the equity they are providing). As result of the negotiations, the initial agreed rate of return has been re-set. In particular:

Evaluation price at	Rate of return ²⁰ Tube Lines in JNP	Rate of return for Metronet in SSL	Rate of return for Metronet in BCV
At Selection	23.9%	14.7%	13.7%

¹⁹ All prices are expressed in Net Present Values and shown in Pounds. Conversion rate used is 1.55 € equals 1 Pound..

²⁰ All rates of return are post tax rates of returns.

of preferred bidder			
At CFO	19.9%	17.8%	15.6%
% Difference	- 17%	+ 21%	+ 13%

- (p) **Refinements related to the UK Government’s various comfort letters (addressed to the bidders’ funders).** The form of the various comfort letters from the UK Government was negotiated after the selection of the preferred bidders.

3. SUBMISSION BY THIRD PARTIES

- (70) In its submission, Transport for London (TfL) wrote to the Commission to inform that the London Underground PPP arrangements under examination could “raise material issues under EU rules on State aid”. In particular, it claims that the proposed PPP arrangements constitute state aid incompatible with the rules of the EC Treaty. TfL further considers that there is no basis on which state aid could be authorised.
- (71) In order to justify its claim, TfL reasons that the procurement process that led to the award of the contracts to certain bidders was not properly conducted under applicable EU law, that the economically most advantageous bid was not and could not be identified in the framework of the procedure that London Underground Limited conducted. It further claims that, as a result, the users of the London Underground and the taxpayer will have to foot a bill that would have been much smaller if competitive forces had had an opportunity to fully determine the outcome of the competition. TfL therefore concludes that the price payable by the UK authorities is higher than any market price and thus, there exists an advantage in favour of the winning consortia. In particular, TfL's concerns about state aid arise from the – according to TfL - absence of an "open and transparent tender procedure" referred to in the privatisation guidelines and the substantive outcome of the PPP negotiations independent of any determination as to whether or not the procurement rules on negotiated procedures were breached. Additionally, TfL's submissions noted the absence of an independent valuation which it believes to be required in these circumstances
- (72) At a certain stage, TfL also informed the Commission that TfL had decided to withdraw the application it had initiated in the United Kingdom with the aim to obtain a declaration by the UK Courts that the PPP procurement process for the London Underground had breached public procurement rules. Despite this withdrawal from the UK Courts, TfL confirmed its intention to go on with the claim initiated, provided further factual information on the PPP process with

the aim of supporting its allegation under EU state aid rules. In particular, it further requested the Commission to initiate the procedure provided for under Article 88(2) EC Treaty.

4. ASSESSMENT OF THE EXISTENCE OF STATE AID

4.1. Assessment of the existence of State aid with regards to the PPP arrangements

- (73) By virtue of Article 87(1) of the EC Treaty, any aid granted by a Member State or through State resources in any form whatsoever, which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods, shall, in so far as it affects trade between the Member States, be incompatible with the common market.
- (74) The concept of state aid applies to any advantage granted directly or indirectly, financed out of State resources, granted by the State itself or by an intermediary body acting by virtue of powers conferred on it.

4.1.1. Direct transfer of state resources

4.1.1.1. Existence of state resources

- (75) First, it needs to be examined whether the PPP arrangements involve any direct transfer of state resources. The various compensation measures (i.e. the infrastructure service charge (ISC), payments to be underpinned by a publicly owned company in favour of Infracos, non-legally binding comfort letters, possible additional compensation for extra work, the avoidance of certain charges, etc) can indeed be considered as State resources either originating from a State owned company (London Underground) or from the State itself.

4.1.1.2. Imputability of the measures to the State

- (76) Secondly, it needs to be determined whether those measures are imputable to the State. According to the judgement of the Court dated 16 May 2002 in case C-482/99 (French Republic v. Commission)²¹, the imputability to the State of a measure taken by a public undertaking may be inferred from a set of indicators arising from the circumstances of the case and the context in which that measure was taken. In the present case, although part of the compensation payments (ISC) and other related measures, are to be granted by a publicly owned company (London Underground Limited), it is clear that the projected arrangements can only take place at the instigation of and with the agreement of the Member State. It is, in particular, the British Government which has developed and put in place this partnership. The Commission notes in

²¹ The so-called Stardust Marine case. See in particular paragraph 55.

particular that the public private partnership for the London Underground was announced by the Deputy Prime Minister on 20 March 1998. Furthermore, there are other measures that could be regarded as part of the compensation mechanisms (i.e. guarantees, etc) that are actually taken by the British State. The measures are therefore all imputable to the Member State. Without this input and support from the UK Government, the PPP arrangements would not be possible. Thus, the measures under examination are all imputable to the State.

4.1.2. *Assessment of the existence of advantage*

- (77) Thirdly, it needs to be examined whether these arrangements are to be regarded as state aid. If these arrangements would take place at an undervalue, for whatever reason, then the Member State would forego the market price, that is resources that would normally accrue to and should accrue to the Member State would be foregone, and the measures would in that eventuality constitute State aid.
- (78) In the present case, which is one of the first case where PPP arrangements are examined by the Commission in the context of state aid rules, the Commission refers to the statements relating to the privatisation of state owned companies outlined in the XXIIIrd Competition Policy Report²², as well as Commission practice in these areas.²³ The recent Commission Interpretative Communication on concessions under Community Law²⁴ may also provide some guidelines in this exercise.
- (79) In particular, the Commission considers that when these types of infrastructure arrangements are concluded after the observance of an open, transparent and non-discriminatory procedure, it is, in principle, presumed that the level of any public sector support can be regarded as representing the market price for the

²² European Commission (Ed.), XXIIIrd Report on Competition Policy – 1993 , Brussels – Luxembourg 1994.

²³ See in particular that the Commission has recently confirmed the applicability of these rules to the transport sector. In a recent proposal for a Regulation concerning aid for co-ordination of transport by rail, the Commission states that: “State support granted to an infrastructure manager, public or private but separate from the State, for the management, maintenance or provision of inland transport infrastructure is presumed to be compatible with the common market if that manager was chosen by an open and non-discriminatory tender, as it was thereby assured that the amount of State support represents the market price to achieve the desired result” (Recital 10 of the Proposal for a Regulation of the European Parliament and of the Council concerning the granting of aid for the co-ordination of transport by rail, road and inland waterway, COM (2000) 65 final, OJ 2000 C365E/179. See also the Communication from the Commission on Public-Private Partnerships in Trans-European transport network projects, COM (97) 453 final.

²⁴ Published in the OJ C 121/2 dated 29.04.2002

execution of a project. This conclusion should lead to the assumption that, in principle, no State aid is involved.²⁵

4.1.2.1. Assessment on the existence of an open, transparent and non-discriminatory procedure

- (80) On those assumptions, it therefore needs to be examined whether there has been an open, transparent and non-discriminatory procedure in this case.
- (81) The Commission notes that in selecting the contractors, the UK authorities followed a negotiated open tendering procedure with a call for competition.
- (82) As a preliminary element, the Commission notes that the PPP arrangements involve the supply of services, works and goods. According to the information provided by the UK authorities, the value of the services elements is greater than the value of the works or supply elements. On this basis, it would appear reasonable to categorise the PPP as services contracts for purposes of the Utilities Directive. In this context, the choice of a negotiated procedure is in line with the requirements laid down in EC Public procurement legislation (see in particular the EC Directive 93/38/EC – the so called utilities directive).
- (83) Secondly, prior to those calls for competition, various periodic indicative notices (PINs) were published in order to ensure that the market had as much time as possible to prepare for participation. These PINs placed potentially interested service providers/contractors/suppliers on notice that a call for competition for the London Underground PPP would be published. Moreover, the PINs stated that “potential partners who wish to provide written responses only should apply for a briefing pack”. They also referred to “consultation meetings” to discuss the PPP arrangements. The PIN published on 21st July 1998 set out the criteria for the selection of candidates for inclusion in consultation meetings stating that these “...must provide evidence of their capabilities and experience, alone or in consortium with others, in 1 or preferably more than 1, of the following: managing and maintaining large-scale infrastructure, especially railway infrastructure; managing, implementing and financing major capital investment programmes; operating within a safety critical environment; working in partnership especially with the public sector”.
- (84) The call for competition indicated also that all registered candidates would be invited to attend a briefing conference. The contract notices briefly described the structure of the PPP and - significantly - expressly referred to the PINs published previously. In these circumstances and having regard to the likely volume, value and specialist nature of the services to be provided under the PPP, it is reasonable to believe that any potential supplier would have

²⁵ See, for example, Case N 617/98 – *The Netherlands – Container Terminal Utrecht*, Decision of 8 February 2000; Case N 517/98 – *United Kingdom – South Wales European Rail Freight Terminal*, Decision of 22 December 1998; Case N 234/96 – *United Kingdom – Channel Tunnel Rail Link*, Decision of 22 May 1996; Commission Communication on State aid elements in the sales of land and buildings by public authorities, OJ No C209, p.3, 1997/07/10.

appraised itself not only of information contained in the contract notice but also details contained in the previously published PINs expressly referred to in the contract notices, would have attended to the briefing meetings and obtain the briefing packs made available. It is therefore stated that the notices published by the London Underground were sufficient for the purposes of an open tendering process. The principle of transparency and equality of treatment have therefore been respected because the proposed contracts were duly advertised in the Official Journal of the European Communities and any modifications or new elements introduced during negotiations respect the parameters of the notices and contract documents, as defined by the United Kingdom authorities.

- (85) Thirdly, the Commission notes that offers were evaluated on the basis of the most economically advantageous tender, including cash price and prospective plans, leading to the drawing up of a short list of final bidders. The non-cash differences between the bidders fell into three main categories: differences in the scope of work covered in their proposals; differences in the level of performance that could be expected; and differences in the proposed allocation of risk between the bidders and LUL. A complex methodology was developed to express these differences in financial terms, in order to permit comparison of the bids and selection of a preferred (most economically advantageous) bidder for each contract. The Commission considers that in this particular case, it was fair to all bidders to develop a procedure, applied in a consistent way, to place a comparative value on the advantages and disadvantages offered by each bid. The Commission considers that in the context of complex contracts like these, this appears to be an appropriate methodology for the selection of the most economically advantageous offer. The Commission concludes that final negotiations for the PPP arrangements were conducted with the bidders that were selected on the basis that their bids represented best value for money and that further negotiations would continue with the preferred bidders.
- (86) It now needs to be assessed whether the modifications of contract terms after the selection of the preferred bidders would have caused discrimination or unequal treatment. Article 4 of Directive 93/e8/EEC (“the Utilities Directive”) prohibits in particular discrimination as between tenders. The negotiated procedure is by its nature flexible. Article 1(7)(c) of the Utilities Directive states that in the negotiated procedure “*the contracting entity consults suppliers contractors or service providers of its choice and negotiates the terms of the contract with one or more of them*”. In the present case, it cannot be stated that the number of modifications introduced after the selection of the preferred bidder, would necessarily have caused discrimination. Indeed, such conclusion would overlook the possibility, particularly relevant in the case of a negotiated procedure, that a contracting entity may include in the contract documents a mechanism which provides for ongoing testing (for example to ensure that performance criteria remain appropriate and provide necessary incentives) or external factors (such as inflation) which allow changes to be made throughout the procedure. The Commission notes that the principle of changes being made was known to all tenderers in advance and considers that the introduction of changes was operated in an objective way. Thus, such

modifications cannot be considered to automatically constitute a form of discrimination even where they are introduced after appointment of the preferred bidders. This is all the more important in connection with particularly complex tenders which are negotiated over a long period of time (3 years in the case of PPP). An example of this type of modification is the PPP's Shadow Running where it was made known from the outset that the operation of "Shadow Infracos" could produce results which would, if necessary, be fed into the negotiation process even after the appointment of preferred bidders.

- (87) The Commission has further assessed the conduct of the tendering procedure as described by the UK government and the complainant. It reaches the conclusion that this conduct falls within the scope and nature of the tendering rules in the Directive and the underlying principles contained in the Treaty. The changes that were made have not changed the scope and characteristics of the PPP beyond what was contemplated by the OJEC Notices. This type of infrastructure contract requires a flexible approach. These particular contracts are unusually innovative and complex. Under these circumstances, it is compatible with Community legislation for contract details to be modified after the selection of preferred bidders without automatically vitiating the presumption that the final price is a market price.
- (88) After examination, the Commission considers that this point is further reinforced by the fact that many of the changes to the contracts made after the selection of preferred bidders derive from affordability constraints, shadow running, the development of an improved understanding of London Underground's own requirements, the passage of time, and changes in circumstances (i.e. events of the 11th September 2001) – all factors which would have had an impact not only on the bids of the preferred bidders, but also on the bids of the non-preferred bidders if those bids had remained in the competition.
- (89) Moreover, the Commission considers that the modifications after the selection of the bidders are of a degree which is acceptable under EC legislation, and that they are not so substantial, individually or collectively, as to be likely to have attracted prospective tenderers which did not consider tendering following publication of the original OJEC Notices. The Commission considers that in a complex and innovative infrastructure contract of this type, using the negotiated procedure under Directive 93/38/EEC, it was reasonable for the UK authorities to conclude that negotiation with single preferred bidders was an unavoidable part of the process of finalising a market price for the contracts.
- (90) The changes that were made fall into the following groups and are explained according to the following reasons:
- (a) Changes to the timing and sequencing of work, and in the amount of work to be done, as a result of affordability constraints, a more developed understanding of London Underground's requirements and the simple passage of time;

- (b) Changes to the performance regime and the methods of performance measurement, largely to resolve problems identified by Shadow Running;
 - (c) Changes to the asset management regime, reflecting concerns raised by bidders and the high cost of requiring them to take on risks which were not fully understood;
 - (d) Changes in risk allocation, to meet concerns raised by both London Underground and by bidders during negotiation and as a result of Shadow Running;
 - (e) Changes in the provisions of the Service Contracts concerning Periodic Review and, in particular, the funding of the Infracos' obligations following Periodic Review. The drafting originally issued did not deal comprehensively with the mechanics of Periodic Review and it became clear in negotiation that London Underground could have exercised its rights at Periodic Review in a way which made the existing transaction unfinanceable without taking responsibility for the consequences. Refinements were necessary to make clear that London Underground's ability to cause such an outcome were either limited or would result in London Underground taking responsibility for such an outcome;
 - (f) Changes in the calculation of payments on mandatory transfer of the Service Contracts, in order to increase and to bring certainty to the amounts repayable by London Underground in respect of the Infracos' debt, where a sale on the open market is not achievable within a specified time.
 - (g) Changes in the comfort letters issued by the UK Government in order to clarify their form. The drafting originally issued did not deal comprehensively with the need to deal with a newly established local authority body with no financial or other track record;
 - (h) changes in the amounts and timing of payments to Infracos, taking into account changes in financing requirements as a result of affordability constraints; the passage of time; and changes in the content of the contracts.
- (91) Finally, the Commission concludes that the final results of the process (including the elements negotiated after the selection of the bidders) would not have changed the outcome of the tendering procedure. . In relation to this point, the Commission refers to the review carried out by the British authorities and attached to the notification confirming that the preferred bidders remained the best value for money in light of the refinements made since the submission of the BAFOs (the last formal bids made before the selection of preferred bidders). The methodology employed for this review involved adjusting the offers of the other bidders to reflect the refinements made since announcement of preferred bidders, in order to estimate the likely financial impact of these changes.

- (92) In the absence of evidence indicating wrongdoing, it can therefore be concluded that the tendering process conducted by London Underground in respect of this PPP was open, transparent and non-discriminatory. On this basis, and according to the traditional practice of the Commission, it can therefore be concluded that the arrangements reflect a market price and therefore that the PPP arrangements do not constitute State aid.

4.1.2.2. Economic assessment of the changes in the contracts introduced after the selection of preferred bidders

- (93) In order to determine the conformity of the changes made after the selection of preferred bidders, in the context of a non discriminatory negotiated procedure, the Commission has examined the economic assessment provided by the UK authorities in the text of the notification.
- (94) The economic comments initially submitted by the UK Government focussed on whether the PPP represents value for money relative to the alternative of retaining the responsibilities within the public sector. They did not directly assess the value to the preferred bidders of the changes introduced in the contracts after the selection of preferred bidders.²⁶ For the sake of security, the UK authorities have therefore provided the Commission with an economic assessment on worst-case assumptions of the estimated value of these changes in order to determine whether the final results still represents a market price.
- (95) In examining the specific changes introduced in the contracts after the selection of preferred bidders, the Commission has concluded that:
- (a) in the following cases, the most reasonable analysis is that the volume of work within individual sections of the contract increased after the selection of preferred bidders, but the unit price of the work in question did not change significantly, and there are therefore no grounds for believing that there has been an increase in the rate of compensation:
 - removal of the cap on bonus payments for availability
 - snagging items
 - train declaration
 - (b) in the following cases, any change in the value of the contract for the preferred bidders is marginal in scale in relation to the overall value of the contract:

²⁶ Although these economic assessment did not initially assess the value to the preferred bidders of the changes introduced in the contract after the selection of preferred bidders, London Underground has since carried out such an assessment. In its view the most likely outcome is that any such changes have not added value to the preferred bidders.

- increased allowance for minor works;
 - introduction of the concept of intermediate works;
 - new penalties for engineering works that overrun into service hours;
 - grace periods before the application of certain penalties;
 - changes to the treatment of safety and law change costs;
 - requests for changes of customer information;
 - train ambience targets for individual lines;
 - changes in liabilities;
 - changes related to the PFI contracts;
 - changes in the arrangements for periodic review and contract termination;
 - comfort letters;
- (c) in the following cases, the changes are best assessed as measures to create outcomes intended in the original contract documents:
- graffiti clearing;
 - temporary speed restrictions;
 - change in how train ambience is measured;
 - limits on London Underground's use of contractual remedies;
 - capability penalties for factors outside Infracos' control;
 - insurance;
 - increased protection for contractors against the possibility of their strategic purchasing decisions being judged non-economic and efficient;
 - new system of penalties for too-slow fault rectification;
 - changes to the agreed rate of return.

Therefore, none of these changes can reasonably be considered as materially improving the value of the contracts for the preferred bidders relative to how the contracts stood at the point where preferred bidders were selected.

- (96) The UK authorities, however, do not completely exclude the possibility that certain other changes led to improvements in the value of the contracts for the preferred bidders.
- (97) In particular, the UK authorities consider that the maximum order of magnitude of any such improvement in the net present value of the JNP contract as presented in the submission, compared with the contract as it stood when preferred bidders were selected, is £140m over the 30 years. Compared to the total forecast ISC payments of £6378m, this would represent an improvement of 2.2%.²⁷
- (98) In the case of the BCV contract, the UK authorities consider that the maximum order of magnitude of any such improvement in net present value is £280m. Compared to the total CFO evaluation ISC of £4135m, this would represent an improvement of 6.8%.²⁸
- (99) In the case of the SSL contract, the UK authorities consider that the maximum order of magnitude of any improvement in net present value is £170m. Compared to the total CFO evaluation ISC of £4836m, this would represent an improvement of 3.5%.²⁹

²⁷ The factors that could lead to such an increase in the value of the JNP contract are: (a) a maximum increase of approximately £50m, if the an uplift for inflation of 2.85% were used ; (b) a maximum potential benefit of approximately £50m from the inclusion in the infraco's work programme of new items priced under non-competitive conditions (assuming a 5% increase in profitability under these conditions); (c) a maximum potential benefit of approximately £20m from the changes to the risks infracos carry for cost overruns and revenue shortfalls which even an efficient and economic contractor would have experienced; (d) a maximum potential benefit of approximately £20m from the revised treatment of the impact of delay events on capability targets.

²⁸ The factors that could lead to such an increase in the value of the BCV contract are: (a) a maximum increase of approximately £20m, if an uplift for inflation of 3.1% were used ; (b) a maximum potential benefit of approximately £50m from the inclusion in the infraco's work programme of new items priced under non-competitive conditions (assuming a 5% increase in profitability under these conditions); (c) a maximum potential benefit of approximately £40m from the changes to the risks infracos carry for cost overruns and revenue shortfalls which even an efficient and economic contractor would have experienced; (d) a maximum potential benefit of approximately £10m from the revised treatment of the impact of delay events on capability targets; (e) a maximum increase of £60m in the relative value of the contract at the point where preferred bidders were selected, in comparison with the contract as it now stands, to take into account possible consequences of changes in the definition of risks; (f) a "residual cost change" of approximately £100m .

²⁹ The factors that could lead to such an increase in the value of the SSL contract are: (a) a maximum increase of approximately £30m, if an uplift for inflation of 3.1% were used e (b) a maximum potential benefit of approximately £30m from the inclusion in the infraco's work programme of new items priced under non-competitive conditions (assuming a 5% increase in profitability under these conditions); (c) a maximum potential benefit of approximately £40m from the changes to the risks infracos carry for cost overruns and revenue shortfalls which even an efficient and economic contractor would have experienced; (d) a maximum potential benefit of approximately £10m from the revised treatment of the impact of delay events on capability targets; (e) a maximum increase of £60m in the relative value of the contract at the point where preferred bidders were selected, in

- (100) For all three contracts, it is possible that there has been no increase in value since the selection of preferred bidders. For two of the three (JNP and SSL), if there has been any increase in value, it can reasonably be estimated that this will have amounted to a maximum of 3.5% of the value of these contracts. For the third contract (BCV), it cannot be ruled out that there has been an increase in value which might have amounted to a maximum of approximately 6.8% of the value of the contract.
- (101) In assessing such potential increases in value, it is important to consider the nature of the contracts in question.
- (102) In this respect the Commission notes that the objective of the contracts (outsourcing responsibility for the provision of track, stations and trains while retaining operating responsibility in-house) is original. Their duration (30 years) is long. These factors unavoidably make the contracts complex and their value difficult to assess. The transaction and information gathering costs involved in preparing the contracts are high, for both clients and contractors. The gap between the selection of the preferred bidders and the conclusion of the contracts has been lengthy. These factors inevitably mean that unanticipated issues have emerged since the selection of preferred bidders and have had to be addressed under the non-competitive conditions then prevailing.
- (103) In the light of these factors, the Commission believes that even if the changes in the value of the contracts may, in practice, amount to the maximum estimated figures set out above, such degrees of increase would be reasonable in the context of contracts of this type awarded under a negotiated procedure. Therefore, the final results of the negotiations can be considered as representing a market price.

4.1.2.3. Assessment of the proportionality of the measures

- (104) The Commission needs to analyse at this stage whether the PPP arrangements chosen are both necessary and appropriate in the light of the objectives sought. In choosing the measures to be taken, a Member State must adopt those which cause the least possible disruption to the pursuit of an economic activity.
- (105) In this particular, the Commission notes that the duration of the contract (30 year period) is proportional in the light of the complexities of this project, which aims at developing a better London Underground through an efficient public sector operator working with an enhanced infrastructure managed by the private sector. This is particularly the case in order to ensure that the initial investment (quite significant) is paid off during the whole life of the contract.

comparison with the contract as it now stands, to take into account possible consequences of changes in the definition of risks. In addition there is room for doubt whether it is reasonable to suppose that the SSL contract became less favourable for the preferred bidder during the period after that bidder's selection.

The Commission notes that during this initial periods, regular payments (ISC) will not suffice to compensate the need for investment to face the modernisation of the Underground (i.e. stations, trains, etc) and consequently, the duration of 30 years appears necessary to reach the agreed rates of return.

- (106) The Commission further notes that three elements of the PPP arrangements will further guarantee its proportionality and in particular that no overcompensation creeps in during the 30 year period.
- (107) First, the procedure will be subject to a continuous review process (periodic and extraordinary reviews). This process allows for reconsideration of the regular payments (ISC) in the light of the changes in the scope of work or in light of the changes in the forecast of the level of cost which would be incurred by an Infraco acting in an economic and efficient manner. In considering these elements, an Arbiter is appointed to independently assess all these elements (i.e. proportionality of the payments, scope of work, the need for additional finance, etc). This arbiter will also assess the economy and the efficiency of the Infracos during the whole life contract. The Arbiter has wide-ranging powers to obtain information from all the participants in the PPP. In forming a conclusion, the Arbiter is entitled to consider practice in a wide range of other industries including, for example, regulated utilities. In essence, the PPP Arbiter acts as an economic regulator guaranteeing the equilibrium between the parties during the life of the contract.
- (108) Secondly, various measures in the PPP arrangements are aimed at avoiding non-proportional benefits in favour of the members of the Infraco. In this particular, there are strong legal guarantees and commercial incentives preventing the Infracos from awarding “soft” sub-contracts to their shareholders:
- *First*, the Infracos are responsible for procurement of sub-contracts. But then these, sub-contracts may only be awarded to the most economically advantageous bidder, following an open tender process. Failure to observe this contractual obligation will constitute a breach of contract.
 - *Second*, the fundamental legal basis of the PPP contract – that Infraco must act in an efficient and economic manner in accordance with Good Industry Practice - acts as a strong incentive on Infraco to let sub-contracts at the most efficient rates available in the market.
 - There are similarly strong de facto commercial incentives on Infracos not to award “soft” sub-contracts to their shareholders (see above in the description of the facts the members of the various winning consortia)
 - In particular, the Commission notes that the diverse nature of the shareholders of the two bidder consortia ensures that none of the shareholders have an incentive to cross-subsidise another shareholder’s contracting margin at the expense of dividend profits which would otherwise be earned as a result of Infraco performance. The idea is that the sort of communication

vessels which link each consortia' shareholders is kept at equilibrium.

- The lenders (financial institutions) will also have an incentive to exert strong pressure on the Infracos in order to avoid that operating expenditure of Infracos move away from certain reasonable limits because of the fact that Infraco award “soft sub-contracts” to its own detriment.

- In addition to these legal and de facto obligations and incentives, London Underground has extensive rights of audit over Infraco and its sub-contractors to ensure that sub-contracts are being let in an efficient and economic manner.
- Furthermore, the presence of the Partnership Director as an independent director on the Board of each Infraco, with the obligation to report to LUL should Infraco act in a manner inconsistent with the requirements of the PPP contract, provides a high level of monitoring of Infracos' compliance with its obligation.

(109) Finally, the Commission notes that there are strong limitations on Infracos to prevent the use of the assets to distort competition in other ancillary markets. The principle underlying the asset ownership regime of the PPP is that the Infracos will, with very limited exceptions, only be entitled to use PPP assets in order to provide services to London Underground under the terms of the PPP contract. Equally, London Underground should at all times be able to take back a fully functional business including all the assets required to continue to provide the infrastructure services currently provided by the Infracos. For the most part, Infracos are not entitled to undertake any business, operations or activity other than for the purpose of performing their obligations under the PPP contract. Even if there are exceptions to this prohibition, they are restricted to the following situations: (a) where reasonably required to perform an ancillary agreement or a centralised service agreement (in other words, subsidiary PPP agreements) or (b) where it consists of supplying services to other members of the Infraco's group, provided that certain conditions are met. As the UK authorities have confirmed, similar clauses already were foreseen in the draft contracts at the “invitation to tender” (ITT)-stage, so that all bidders could take account of this aspect when making their offer.

(110) On this basis, the Commission considers that the PPP arrangements are proportional to the aims pursued. Any risk of overcompensation creeping in during the life of the contract is substantially limited, if not eliminated, by the various safeguard measures examined and commercial incentives.

4.1.2.4. Conclusion on the existence of advantage

(111) On this basis, and according to the traditional practice of the Commission, it could therefore be concluded that the arrangements reflect a market price and that therefore that the PPP arrangements do not give rise to any advantage. In view of the open, transparent and non-discriminatory tendering process, the

Commission therefore understands that there is no need to examine in detail the various measures being part of the PPP arrangements (payments, ISC, guarantees, payments in case of breach of the contract, Government comfort letter to bidders' funders, etc). They are all part of the compensation "payable" for the carrying out of the tasks pursued under the PPP arrangements. [...]*. Thus, such negotiation does not give rise to any new advantage not already covered under the market price reflected in the results of the tendering procedure.

- (112) Furthermore, the Commission submits that any possible risk of overcompensation during the 30-year period is substantially reduced in light of the envisaged protective measures and commercial incentives.

4.1.3. Conclusion on the existence of State aid with regards to the PPP arrangements

- (113) In view of the fact that the PPP arrangements do not give rise to any advantage to the winning consortia, there is therefore no need to examine whether the measures at stake distort or threaten to distort competition and whether they may affect trade between the Member State.
- (114) The measures in question, and on the basis of the facts of the specific case, do not therefore constitute state aids.

4.2. Assessment of the existence of State aid with regards to the contractual arrangements ancillary to the PPP schemes

- (115) It is also necessary to examine whether the restructuring measures linked to the NLTS contract constitute state aids. In particular, it is necessary to assess whether Alstom and the Finance Parties, as well as any Infracos, have been put at an advantageous position pursuant to the London Underground PPP arrangements.
- (116) The Commission notes in this regard the existence of various measures that could potentially be construed as Government support, including a series of public guarantees granted in favour of Alstom and the Financial parties as well as additional security, step-in agreements and financial covenants pursuant to the PPP arrangements. These measures can all be regarded as constituting state resources imputable to the State. It is indeed the British Government which is in all cases behind all these measures. It is therefore necessary to examine whether any of these arrangements ancillary to the PPP contracts give rise to any advantage notably to Alstom and the Finance Parties (additional security, step in and other guarantees) and for Infraco JNP (financial covenants).

* Confidential information. It refers to the negotiations between the British Government and the EIB of various aspects in respect of loans to be granted to the London Underground PPP project

4.2.1. *Assessment on the existence of any advantage with regards to the NLTS Contract (the so-called additional security, step-in agreements and other guarantees)*

- (117) Many of the notified measures relate to the previously-signed Northern Lines Train Service (NLTS) contract involving London Underground and Alstom. The NLTS contracts were signed with Alstom and the FP for the provision and maintenance of new trains and related equipment for the Northern Line. The NLTS Contracts were awarded to Alstom and other Financial Parties after an open and transparent negotiated tendering process. Seven candidates responded to the Periodic Indicative Notices and all were invited to pre-qualify for the opportunity to submit tenders. Four of these parties sought to pre-qualify. The main criteria of evaluation were objective and were followed during the whole tendering procedure. Two tenderers were selected as short-listed bidders. Bids were assessed in terms of their net cost, the passenger benefits/operating cost, savings delivered and compliance with the terms of the Government's Private Finance Initiative. The preferred bidder was announced as Alstom on 7th December 1994.
- (118) In order to assess the guarantees awarded to Alstom and the Financial Parties (FP) pursuant to the PPP arrangement and in particular whether they give rise to any advantage, it is therefore necessary to examine their function in light of the NLTS Contract. According to the initial NLTS Contract, Alstom and the FP were entitled to require an additional security in the occurrence of certain events. These pre-existing rights could have been triggered in favour of Alstom and FP (i) upon a change of control of London Underground and (ii) on the transfer of the NLTS Contract to a private sector entity with inadequate financial standing and/or credit risk. Pursuant to the PPP contracts, the new arrangements in favour of Alstom and FP are aimed at restoring the situation as previously agreed pursuant to the NLTS Contract. They provide an alternative credit support structure in relation to their pre-existing rights which could have been triggered as a result of the changes originated from the PPP arrangements.³⁰ The PPP process would have potentially entitled Alstom/the FP to call for these guarantees. However, the FP and Alstom agreed not to call for these guarantees as a result of the PPP arrangements (transfer of London Underground to TfL or the transfer of London Underground's payment obligations to Infracore JNP). However, the FP and Alstom accepted this because other credit support structures had been put in place.
- (119) It is now worth regarding the aims of each of these new arrangements. In particular:

³⁰ In particular, the British authorities has assessed that in the event of a London Underground default under the original contract (occurrence of certain events), the additional security provided would be supporting the termination payments of London Underground to Alstom (which could amount to [...] in Net Present Value terms (€ [...])) if the NLTS Contract was terminated in the near future.

- (a) the *step-in agreements* ensure that, following the transfer of London Underground's obligations to a replacement Northern Line infrastructure provider in the private sector (Infraco JNP), there would still be a state entity performing the obligations in the event that Infraco JNP fails to do so;
- (b) the *London Regional Transport and TfL guarantees* of London Underground's obligations reflect the fact that control of London Underground is passing from central to local government (which has lesser revenue-raising powers). The British authorities have confirmed that this arrangement does not offer Alstom and/or the FP any greater protection from credit risk than they had previously;
- (c) The Commission also notes that the right of Alstom and the FP to call for *Additional Security* in certain circumstances, under the restructured arrangements, likewise confers no new benefits:
- Alstom and the FP had always been entitled to call for Additional Security in the event of London Underground transferring out of State ownership; the changes to the scope of the “supervening events” in the context of the restructuring gives the equivalent protection by allowing a call for Additional Security if London Underground, LRT or TfL were to pass out of State (whether central government or local government) control. Accordingly, in this respect the Additional Security merely gives substance to the basic protection which Alstom and the FP enjoy of their obligations being performed/guaranteed by a State entity, and provides alternative credit support in the event that the guarantor should cease to be a State entity;
 - Alstom and the FP had always been entitled to call for Additional Security in the event of a transfer of London Underground such that its assets fall below a certain level; the same effect is achieved under the restructured arrangements, but reflecting the fact that London Underground will no longer be owned by central government, by a provision that Additional Security may be called for if London Underground's assets were to fall below a certain level;
 - Alstom and the FP had always been entitled to call for Additional Security in the event of London Underground being unable to discharge financial indebtedness above a certain level to a third party. This provision remains essentially unchanged under the restructured arrangements;
 - in addition, under the restructured arrangements there will be a right to call for the Additional Security in the event that the step-in and guarantee arrangements were ever to be held illegal. This is no more than a consequence of the need for such step-in

and guarantee arrangements to put Alstom and the FP in the same position, in terms of credit support, as they had prior to the restructuring (see (a) above);

- following the transfer of London Underground to TfL, Alstom and the FP will have the right to call for Additional Security if TfL's credit rating were to fall below specified levels. This, again, simply reflects the fact that local government does not have equivalent revenue-raising powers to central government, and is therefore not of equivalent credit risk; the provision is designed to maintain for Alstom and the FP the credit protection it has enjoyed while London Underground was controlled by central government. It does not confer any new benefit;
- finally, the right to call for Additional Security in the event of the transfer of the NLTS Contract, and hence the obligations owed to Alstom and the FP, to Infraco JNP *prior to* the transfer of Infraco JNP to the private sector - which would have the effect that Infraco JNP would be performing the obligations before the FP and Alstom were entitled to the protection of the step-in agreements and the LRT/TfL guarantee - does no more than give Alstom and the FP equivalent protection to that which they would in any event have.

(120) On this basis, the Commission understands that the rationale was to award protection equivalent to the Additional Security that was previously required to be provided. These measures are necessary because they confer to the FP and Alstom an alternative credit support structure for their pre-existing rights. The Commission therefore considers that none of these arrangements in connection with the restructured NLTS Contract give rise to any advantage. They do not therefore constitute aid within the meaning of Article 87(1) EC, as they do not confer any new benefit on Alstom and/or the FP and do not place them in a better situation compared to the situation prior to the negotiations of the PPP arrangements.

(121) The Commission further notes that without these measures, the FP and Alstom would be entitled to re-assess their contractual position, which could lead to substantially increased costs being incurred by London Underground. These measures allow London Underground to ensure the continued provision of services on the Northern Line at the lowest cost to the London travelling public. The Commission therefore considers that none of these measures constitute aid.

4.2.2. *Assessment on the existence of any advantage with regards to the Financial covenants*

(122) London Underground is discussing with Alstom the possibility of making changes to certain financial agreements (covenants) between Alstom and London Underground. These covenants are contained in guarantees given by

Alstom to London Underground. As part of the NLTS Contract restructuring, these guarantees will be extended to Infraco JNP. Pursuant to the PPP arrangement, London Underground's interests under the NLTS Contract will be transferred to Infraco JNP (the Infraco responsible for the Northern Line).

- (123) The original covenants related to requirements on Alstom to maintain a minimum consolidated tangible net worth, a limit on its borrowings less cash, and a specified ratio of current assets to net sales, as well as requirements on Alstom to maintain certain gearing and interest cover ratios. The changes being discussed would have the effect that Alstom will be covenanting with London Underground (and thus Infraco JNP) to comply with the financial covenants given by Alstom to the FP, as such covenants are amended from time to time.
- (124) The financial covenants were originally given by Alstom to London Underground to match the covenants Alstom had given to the FP. The purpose under the proposed negotiations is that those agreements are extended also to the benefit of Infraco JNP. Since Infraco JNP will assume the responsibility over the Northern Line, the arrangements would simply extend those initial agreements in favour of London Underground in favour of the new responsible entity. The Commission notes that the arrangements also aim at making sure that any new position agreed between private investors (the FP) and Alstom from time to time is also extended to Infraco JNP, as it was previously done in favour of London Underground.
- (125) The Commission concludes that these amendments, if finally agreed, do not entail the giving of any gratuitous benefit in the benefit of Infraco JNP. They do not therefore constitute state aid.

4.2.3. Conclusion with regards to the existence of state aid with regards to the arrangements ancillary to the PPP contract

- (126) The foregoing assessment makes apparent that none of the arrangements contemplated by the British authorities ancillary to the PPP arrangements appear at this stage to result in any advantage and consequently, do not raise any State aid concern. Therefore, there is not need to examine whether the measures at stake distort or threaten to distort competition and whether they may affect trade between the Member State.
- (127) The measures in question do not therefore constitute state aids.

4.3. Assessment of the Government financing structure in favour of Transport for London

- (128) The concept of state aid applies to any advantage granted directly or indirectly, financed out of State resources, granted by the State itself or by an intermediary body acting by virtue of powers conferred on it.
- (129) So far, this decision has addressed the possibility of there being state aid for the three infrastructure managers (the infracos) and the parties associated with

them. It is also necessary to examine how the arrangements affect the operator of the Underground services (LUL).

- (130) The Commission first notes that if the charge paid by LUL for the use of the infrastructure is below a market price, this could in some circumstances indicate the presence of state aid. However, the conclusion above is that the price paid by the State/operator for the use of the infrastructure is a market price.
- (131) Furthermore, LUL will provide public transport services which would not be commercially viable without subsidy. LUL is the only operator using the London Underground network and it is the only one capable for paying for the infrastructure services it receives due to the State intervention resulting from the tendering procedure. To that extent, LUL will receive compensation and certain guarantees, including from TfL, to cover the infrastructure costs linked to the PPP arrangements. This compensation does not go beyond the minimum amounts needed to pay for the infrastructure services. The compensation cannot be used for other purposes than the payment of those infrastructure charges. According to the notification (annex 9) it cannot be diverted for aims other than those linked to the payment of the infrastructure services (within the context of the PPP arrangements). The Commission notes therefore that LUL is merely acting as an intermediary agent of the State or its “longa manu” for the purposes of the PPP arrangements.
- (132) The arrangements in favour of LUL in order to allow it to bridge the gap between LUL’s revenue and the cost of ensuring the provision of Underground services – including the infrastructure charges - are subject to the provisions of Regulation 1191/69/EEC, as last amended by Reg. 1893/91/EEC). The Regulation requires that the public funding is limited to the minimum necessary to compensate for the incremental costs caused by the provision of services in the general interest, and lays down specific rules for how this should be calculated. Under the terms of article 17(2) of that regulation, such compensation is subject to exemption from the preliminary notification procedure laid down in article 88(3) of the Treaty. Accordingly, the arrangements for the calculation of this compensation are not part of this notification and do not require the prior approval of the Commission.

4.4. Conclusion

- (133) In the light of these circumstances, the foregoing assessment makes apparent that none of the arrangements contemplated by the British authorities appear at this stage to result in State aid and consequently, do not raise any State aid concern. The Commission nevertheless reminds the British authorities that any modification of the notified measures has to be notified in advance to the European Commission. In this regard, the Commission draws the attention to the British authorities to the obligation to notify to the Commission in case the arrangements may further involve state resources in whatsoever form, which could be considered as state aid. Any deviation from such description would take the measures as eventually implemented outside the scope of this authorisation.

5. DECISION

It has decided, on the basis of the foregoing assessment and the commitments of the British State to consider that the arrangements linked to the London Underground PPP do not constitute state aid, in the light of its Article 87 EC Treaty.

If this letter contains confidential information which should not be disclosed to third parties, please inform the Commission within fifteen working days of the date of receipt. If the Commission does not receive a reasoned request by that deadline, you will be deemed to agree to the disclosure to third parties and to the publication of the full text of the letter in the authentic language on the Internet site: http://europa.eu.int/comm/secretariat_general/sgb/state_aids/. Your request should be sent by registered letter or fax to:

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Yours faithfully,

For the Commission

Loyola De Palacio
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