

Commercial Ferry Service - between Gourock harbour, Inverclyde and Dunoon pier, Cowal.

The Scottish Executive is seeking to facilitate the introduction of a fully commercial ferry service on the Clyde Estuary between Gourock harbour, Inverclyde and Dunoon pier, Cowal. Currently the route is served by Caledonian MacBrayne under payment of subsidy from the Scottish Executive. If a suitable operator is identified then the current subsidised service would be withdrawn. The proposed service will be run on a commercial basis with no operating or timetable restrictions. No subsidy will be made available for this new arrangement. The Scottish Executive is seeking to enter into an arrangement that will require the operator to ensure certain minimum standards.

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Dunoon Observer, February 4th 2005

Western Ferries plans new linkspans

Western Ferries has put in a planning application this week for a replacement linkspan at Hunters Quay.

When asked how that fitted in with any plans to move the company's services to Dunoon, Gordon Ross, Managing Director of Western Ferries said that it was too early to be specific as they were still waiting for the fine details with regard to the proposed commercial invitation for the Dunoon crossing.

However, he said that irrespective of any decision to move some or all of the company's services to Dunoon, they would still need a fully operational facility at Hunters Quay. This would provide an alternative facility for bad weather, improved overnight docking and a berth for refueling and scheduled maintenance.

Mr Ross went on: "The company is looking forward to testing the new facilities in Dunoon when they are completed and having two local berthing options offers us greater operational flexibility and the ability to enhance our current level of services".

Mr Ross is also bullish about the timetable for the proposed replacement linkspan: "Assuming planning permission is granted it may be possible to have the new linkspan and berthing structure in place by the end of this year."

Mr Ross stated that the Company had also submitted plans for an additional linkspan at McInroys Point.

“This will offer us alternative berthing, meaning we could offer a more flexible service at peak times. At the moment we run four ferries an hour, and this is an ideal timetable for one boat arriving, disembarking and then loading up for the return journey. However, with two linkspans on each side, it would mean that as one ferry is loading cars the other can be discharging.

These planned improvements are the company’s next steps in its efforts to improve the current service levels and follow quite naturally the introduction of two new vessels over the next three years. It is hoped that these improvements will enable the company to provide additional sailings and an enhanced level of service to our customers whether they are traveling by car or on foot.

Dunoon Observer, Friday 4th February 2005, pp.1-2

Gourock-Dunoon, 23 Questions, 23 Answers and a Conclusion

The Executive's announcement (8th December, 2004) of its plans for the Gourock-Dunoon ferry service raises a number of questions. I have tried to do an analysis below on the questions that have been asked or are likely to be asked. I will modify and update the questions and answers on a continuing basis as events unfold over the next few weeks and months.

I will start with the announcement, list the questions, go on to offer some answers, and suggest some conclusions. Clearly there are aspects of answers given here that interested parties might wish to confirm independently (such as the potential role of EC law). However, if all parties are aware of both the possibilities opened up by the announcement and how the law is designed to help the public interest in this context, then the very real opportunities that now exist may be achievable.

The Executive's Announcement: Gourock-Dunoon ferry route

08/12/2004

The Gourock to Dunoon ferry service will be advertised for operators to run on a commercial basis with no operating or timetable restrictions on the vehicle service, Transport Minister Nicol Stephen announced today.

If a suitable operator is identified, the present service, provided under subsidy arrangements by Caledonian MacBrayne, would be replaced.

However, if no suitable operator is found then the Executive will bring forward proposals to tender a subsidised service.

The decision was taken in response to representation from the local community to secure the long term future of the service.

In the Parliament, Mr Stephen said:

"The Gourock to Dunoon service is of huge concern to the local community. This new approach involves advertising for a commercial service and responds directly to the proposals put forward by local people and interested parties.

"We expect to advertise the opportunity extensively in the New Year to attract the widest possible interest. Depending on the outcome, a new operator could appear on the route within a year or so.

"It is important to emphasise that if a commercial operator does not come forward all our options for delivering a subsidised service remain open."

The Questions

There are a number of questions that have been and/or will be asked in relation to the implications of this announcement:

Question 1: Western in a briefing paper to MSPs for the Transport Debate said it believed that CalMac was being given unfair (subsidy) advantages on the Gourock-Dunoon market. Is Western's point fair?

Question 2: Is all this anti-Western?

Question 3: Is all this anti-CalMac?

Question 4: What was wrong with the proposed passenger-only PSO for the Gourock-Dunoon route?

Question 5: Can we expect CalMac to offer to run an unrestricted unsubsidised vehicle carrying service Gourock-Dunoon?

Question 6: What is to stop the new operator pushing up passenger fares and/or otherwise degrading the level of service on the CalMac route?

Question 7: What is to stop the new operator pushing up vehicle fares and/or otherwise degrading the level of service on the CalMac route?

Question 8: What is an "essential facility" in EC law?

Question 9: The Deloitte Touche report suggested that route liberalisation would lead to a price war with one operator being eventually driven out or being made insolvent. Is this likely?

Question 10: What are examples of essential facilities in EC law?

Question 11: The essential facilities doctrine has been mostly applied in cases where those who owned the "essential facility" were also operators. In this case, CalMac or Vesco and Argyll and Bute Council would own but not operate the facilities. Does that make a difference?

Question 12: Suppose Western and CalMac or a potential entrant into the Gourock-Dunoon market wished access to the public linkspans?

Question 13: What if more than one operator wished to compete in the Gourock-Dunoon market and claimed access on the basis of "essential facilities"?

Question 14: The value to Western of controlling access to the public linkspans at Dunoon and Gourock could be the difference between the value of facing genuine competition and being a monopoly. This would be a considerable sum. So what is to stop it outbidding potential entrants for access to these linkspans?

Question 15: CalMac can take advantage of network links in the case of Gourock-Dunoon, for example relief vessels in the case on annual maintenance or breakdowns, shared with usage on other routes such as Bute and Skye. How could an entrant compensate for not being part of that network?

Question 16: What if one of Western's linkspans was out of operation and it claimed access to the public linkspans on the basis of "essential facilities"?

Question 17: If Western has been able to successfully claim that it should be able to bid for the PSO for the CalMac passenger service on the basis that it was a different market from their present one, could they not also argue that the CalMac vehicle-carrying service is in a different market serving different customers from their present market and so the public linkspans are "essential facilities" for them also in that market?

Question 18: Apart from finding a suitable operator, what are the main remaining problems?

Question 19: What will Western do now?

Question 20: Could these actions by Western create barriers to entry in the Gourock-Dunoon market?

Question 21: What will be the EC's attitude to all this?

Question 22: What if there is no serious interest from potential operators?

Question 23: Who stands to benefit from all this?

Questions and Answers

Question 1: Western in a briefing paper to MSPs for the Transport Debate said it believed that CalMac was being given unfair (subsidy) advantages on the Gourock-Dunoon market. Is Western's point fair?

In its Briefing Paper Western said, “we need to ensure that our operation at Gourock to Dunoon is based on a level playing field with Calmac” but failed to mention that for 22 years Western has benefited from CalMac’s service being limited to a basic hourly service. This frequency limitation was imposed by the Scottish Office explicitly to protect and benefit Western’s own service. But frequent travellers are more likely to buy books of frequent traveller tickets from the frequent travel service. Frequency of service is the oxygen that underpins competitive advantage and profits on this market. For Western to complain that CalMac’s subsidy is too high is like cutting off someone’s oxygen supply and then complaining that their hospital bills are too high.

Question 2: Is all this anti-Western?

No. All this is pro-competition, not anti-Western

Question 3: Is all this anti-CalMac?

No. It is important to separate out the genuine and justified public outrage over the current public relations debacle following CalMac’s adoption of shore-based ticketing on the route from the broader issue of longstanding public support for CalMac as a company with a long and fine tradition of public service in the Clyde and Hebrides. In my case, along with many others, I argued both to the Executive and in public the need to keep the CalMac network together and the lack of logic in tendering out its operations – and I also argued that the Altmark judgment supported this point of view.

Question 4: What was wrong with the proposed passenger-only PSO for the Gourock-Dunoon route?

Two main problems. The proposed restriction in the PSO on vehicle carrying would continue to distort competition in this market to Western’s advantage. But even if this was removed, it would not solve the problems.

The PSO for the passenger market for Gourock-Dunoon could have been argued to be for a different market than the one which Western currently is in (which is essentially for vehicle-carrying). In any event, Western successfully argued to the European Commission and the Executive that they should be allowed to bid for the PSO for the foot passenger service between Gourock-Dunoon. Had they won the PSO, they would have secured control over the ferry services out of both sets of linkspans, their own and the public linkspans between Gourock and Dunoon, whether or not they ran a vehicle carrying service along with the passenger PSO. Western would have had a strong financial incentive to outbid other potential operators for the PSO because it would

secure their monopoly control over the Gourock-Dunoon market. So although the PSO was oriented to passengers, its biggest economic and commercial impact would have been on the vehicle carrying market. That is why Western was preparing the public for their becoming the monopoly provider with promises of a “users charter” or “users contract” to supposedly protect customers interests in the event of their becoming sole provider, the notion of such a “charter” being no more legally binding than a “shoppers’ charter” offered by a supermarket and in no way indicative of how monopolies behave in practice.

Question 5: Can we expect CalMac to offer to run an unrestricted unsubsidised vehicle carrying service Gourock-Dunoon?

In his statement in the public debate on transport in Parliament on 8th December, the minister said that was possible but hinted that it is unlikely. The reasons are obvious from the energetic briefing campaign carried out by Western to try to influence that debate. In his Briefing Paper noted above, Mr Gordon Ross argued that CalMac was being given unfair (subsidy) advantages and, more broadly, asked how the Executive could prevent CalMac abusing its status as the incumbent operator and/or a publicly owned company.

If an operator was to enter the Gourock-Dunoon market on a commercial basis, they would have to incur investment and other startup costs before they would make a profit from route operations. That is normal and to be expected from any market entry and startup venture and does not of itself raise competition issues. But if that operator was *CalMac*, Western could be expected to immediately make representations that it was using its advantageous position as public company and/or public money and/or incumbency advantages to compete unfairly it.

I, and many others, would dearly like to see CalMac as one of the companies bidding to take advantage of the new opportunities offered by the announcement of 8th December. However, the attacks that Western are already making on CalMac’s operations and status means that these obstacles would have to be overcome if the Executive was to give the go-ahead (and the funding or access to funding) for CalMac to sail into these waters.

Question 6: What is to stop the new operator pushing up passenger fares and/or otherwise degrading the level of service on the CalMac route?

The Executive could now effectively lock in the present passenger fares levels (inflation-adjusted) - as maximum targets - and levels of service (e.g. timetable and frequency) – as minimum targets - in the form of a shadow PSO. The attention of potentially interested operators could be drawn to these current levels of fares and services as measures of economic and social targets the Executive wish on the route. If these targets are not met, the Executive could and should reserve the right to trigger a proper PSO and put the service out to tender. The operator would have every incentive to meet these targets because otherwise it could lose its right to compete on the lucrative vehicle-carrying market.

However, there should still be allowances for flexibility and innovation, for example, the entrant might decide that it would be worthwhile running a service every 20 minutes instead of every half-hour. This might have knock-on implications for connections with public transport, but the economic and social gains might be deemed to outweigh any potential costs. This is something for which there should be a basis for consultation and discussion between the operator and interested parties, including the Executive on a continuing basis, or as and when necessary.

Question 7: What is to stop the new operator pushing up vehicle fares and/or otherwise degrading the level of service on the CalMac route?

These fares and levels of service are already outside the subsidised (passenger) service. The introduction of proper unrestricted competition should be expected to have major user benefits ranging through fares and levels of service.

Question 8: What is an “essential facility” in EC law?

An essential facility has been defined by the European Commission as: "a facility or infrastructure without access to which competitors cannot provide services to their customers". It refers to potential entrants into a market as well as existing competitors.

Question 9: The Deloitte Touche report suggested that route liberalisation would lead to a price war with one operator being eventually driven out or being made insolvent. Is this likely?

Deloitte Touche are accountants, and their analysis of the route was an accountants' analysis commissioned by the two incumbent operators (Western and CalMac) and the Scottish Office / Executive. Deloitte Touche said "the likely consequence of complete liberalisation would be an intense competitive war between the two operators to gain dominance on the route. Our route analysis suggests that the market is not big enough to support two operators, so eventually one of them would be driven out or become insolvent." (Section 10.2).

Deloitte Touche's financial and accounting analysis is unproblematic, however, speaking as an economist, I would say the economics of the route is actually quite different from that suggested by Deloitte Touche.

Firstly, looking at it from an economics perspective and based on (while updating) the accounting figures and assumptions supplied by Deloitte Touche, the report prepared by Kay, Ferguson and Smith for DGFG and FSB reinforced the common sense conclusion that the market was already more than big enough to support two profitable commercial operators, including Western, and that natural growth of the market would only increase market room for operators in the future. I would also expect there to be an element of suppressed demand that competition will help trigger, with businesses and individuals

being more willing to locate and invest with the increased benefits and choice and reduced uncertainty that genuine competition will bring with it.

Secondly, even though the routes are close substitutes for many vehicle users (which is where the competition element comes in), both routes have natural advantages and are likely to have a core base of users. The Western route is shorter and has a cost advantage, and is particularly convenient for vehicles traveling North Cowal - Ayrshire directions. The CalMac route is a particularly convenient for foot passengers, for those who wish to travel on in the direction of the conurbations at Inverclyde and Strathclyde (possibly the bulk of travellers on the market) and the vessels on the CalMac route can also offer catering facilities, which can attract the many users for which the ferry journey is only part of a longer journey. Western also has a frequency advantage, this can be expected to be partially or totally offset by a commercial operation on the present CalMac route.

Thirdly, if one operator begins to dominate (as in the case of Western at the moment), success will bring congestion and queueing problems (also as in the case of Western at the moment) and this can serve as a natural control mechanism encouraging some switching to the other operator as long as they have spare capacity and can also offer a reasonable service (including on frequency grounds, which the CalMac service does not have at the moment).

Fourthly, if one operator does indulge in pricing below cost to push out the other, this would be regarded as predatory pricing and a breach of EC and UK law.

Fifthly, suppose after all this, one operator did push out the other, say in a price war, whether it was Western pushing out the entrant or vice versa. The essential facilities doctrine would still hold and facilitate subsequent entry by third parties. So any monopoly position gained through a price war could be temporary, achieved at great cost and weaken the incumbent financially. The incumbents would be aware of this and this should be a deterrent to trying to achieve monopoly control through a costly price war.

For these reasons, bearing in mind that these are not guarantees, at least the combination of market, competitive and legal factors should help encourage sustain and protect competition in this market.

Question 10: What are examples of essential facilities in EC law?

“Two Commission decisions from the early 1990s provide a good example of the development of a specific doctrine relating to essential facilities rather than refusal to supply.

Both decisions concerned Holyhead Harbor, a focal point for ferry services between Britain and Ireland. The harbor was managed by Sealink, a company which also operated ferries from the harbor. A rival ferry company which also operated at Holyhead, B&I, complained that Sealink, as manager of the harbor, modified the sailing schedule of its own ferry operator in such a way that it interfered with B&I's loading and unloading of ferries. The Commission concluded that Sealink's behavior breached Article 82, and it granted B&I interim measures. The Commission considered the harbor to be an essential facility, which it defined, for the first time, as "*a facility or infrastructure without access to which competitors cannot provide services to their customers.*"

In the Commission's view, Sealink's provision of access to the harbor to B&I on less favorable terms than those accorded to Sealink's own ferry service was a breach of Article 82. Sealink owed a duty not to manage the harbor in such a way as to favor its own ferry services over those of a rival operator. It should be noted that the Commission did not require B&I to be eliminated from the market as such, and there was no evidence that B&I withdrew from it. Rather, what was condemned was Sealink's placing of B&I at a competitive disadvantage by discriminating in favor of Sealink's own ferry service.

In its second decision concerning the harbor, the Commission imposed interim measures against Sealink in order to ensure that it provided reasonable, non-discriminatory access to the harbor to Sea Containers, which sought to introduce a new ferry service at the harbor. The Commission held that the essential facilities doctrine applied equally to established competitors and new entrants to the market.”

<http://www.ftc.gov/os/comments/intelpropertycomments/finefrank.pdf> page 6

Question 11: The essential facilities doctrine has been mostly applied in cases where those who owned the “essential facility” were also operators. In this case, CalMac or Vesco and Argyll and Bute Council would own but not operate the facilities. Does that make a difference?

No.

“It is conceivable that cases could arise in which the person owning the facility (and therefore having the only right to license access to it) and the person having a dominant position in the "downstream" market are two different legal entities. Under EC precedent, if the owner of the facility refused to provide access to it to a third party entrant, there would be discriminatory access in favor of the dominant incumbent, which is forbidden under Article 82.

The underlying considerations would be virtually the same as when the owner of the facility favored its own operations in the relevant "downstream" market. In either event, the Commission would apply Article 82 in order to prevent consolidation of the relevant market by excluding third party access to an essential facility. Whether the third party is owned or controlled by the owner of the essential facility is actually incidental to this analysis.”

<http://www.ftc.gov/os/comments/intelpropertycomments/finefrank.pdf> page 8

Question 12: Suppose Western and CalMac or a potential entrant into the Gourock-Dunoon market wished access to the public linkspans?

In that case, CalMac and/or the potential entrant would be able to argue that the facilities represented “essential facilities” for them in order to compete in that market. Since Western already has its own facilities at Hunters Quay and McInroys Point they would not be able to claim access to these facilities on an “essential facilities” basis. Not only could the authorities be entitled to award to those for whom the facilities are essential facilities instead of Western, if instead they awarded access to Western this could be subject to challenge under the EC’s Article 82 and the essential facilities doctrine. The operators wishing access under “essential facilities” would be fully entitled to have any access given to Western that could block their own access thrown out under EC law.

Question 13: What if more than one operator wished to compete in the Gourock-Dunoon market and claimed access on the basis of “essential facilities”?

The first thing to note is that, while this is a problem, in public terms it is not a bad problem to be faced with since it is indicative of potential demand for the facilities from

interested operators. In fact, if there are problems of access due to lack of spare capacity, this would be one of the few grounds on which refusal to access could be made:

“an essential facility is “a facility or infrastructure without access to which competitors cannot provide services to their customers”¹[4]. That qualification has important competition law consequences, because an undertaking (or group of undertakings) holding such a facility must allow access thereto, at a cost-oriented price, unless there is an objective justification for that refusal, such as lack of capacity of the infrastructure in question. Any decision to the contrary could actually allow the facility owner to block the emergence of a potential new service or product, or impede competition on a (existing or potential) product or service market.”

http://www.twobirds.com/english/publications/articles/banking_confronted_by_new_com_p_law_issues.cfm?RenderForPrint=1

Question 14: The value to Western of controlling access to the public linkspans at Dunoon and Gourock could be the difference between the value of facing genuine competition and being a monopoly. This would be a considerable sum. So what is to stop it outbidding potential entrants for access to these linkspans?

The holders of the essential facility must make it available at “reasonable” charges to those for which it is an essential facility. See the answer above to Question 13; “an undertaking (or group of undertakings) holding such a facility must allow access thereto, at a cost-oriented price”. Clearly the question of what is reasonable would have to be established, but since there are a number of facilities (and potential comparators) in the Highland and Island region (including some owned by both CalMac and Argyll and Bute Council) it should not be difficult to establish what would be standard charges for access to such facilities. So the option of Western outbidding a potential entrant into this market should not be available.

Question 15: CalMac can take advantage of network links in the case of Gourock-Dunoon, for example relief vessels in the case on annual maintenance or breakdowns, shared with usage on other routes such as Bute and Skye. How could an entrant compensate for not being part of that network?

If the main CalMac network goes out to tender, its vessels will be made available to OpsCo (the winning bidder) through VesCo at normal commercial rates (it is the operations which will be subsidised, under EC rules the vessels must be made available to OpsCo at normal commercial rates). The opportunity would exist to write a contract that would make current and future relief main-network vessels available for duties such as annual maintenance for the commercial Gourock-Dunoon operator. Since the contract would have “normal commercial rates” already specified for the main network operations, this could be used as the basis for the contract for the Gourock-Dunoon route and Western would have no grounds for complaint since this contract was clearly not being subsidised by the Executive.

This would be helped by the fact that it would be the Executive (through VesCo) who would still own the vessels and could write the contract. It could be written in such a way that OpsCo would not be financially disadvantaged by any such deal.

If, or for as long as, Calmac does not go out to tender, it would still be possible to identify shadow prices for such vessels to make them available to the Gourock-Dunoon commercial operator at commercial rates. There may be other sources of relief vessels, for example the operator may have its own resources.

The case of breakdowns would be less clear, though it should be possible to write contingent contracts that would make back-up available from the main network (and VesCo) on a commercial basis if needed.

This does not necessarily solve all the problems especially if VesCo/OpsCo has no spare and suitable capacity to give the Gourock-Dunoon operator in the case of breakdown. But it is important to note that these same problems exist just now, and at least at a technical level there should be more choice of relief/replacement for the operator with the adoption of conventional bow and stern loading technology, and away from the route-specific side-loading streakers.

At the end of the day it would be in the interests and mutual advantage of both the Executive (as owners of CalMac or VesCo and through them as its agents) and the commercial Gourock-Dunoon operator to make any such arrangement work. As such, it should have less potential problems than if such deals were being negotiated between direct rivals.

Question 16: What if one of Western's linkspans was out of operation and it claimed access to the public linkspans on the basis of "essential facilities"?

The proper public policy response, after expressing sympathy, would be "hard luck". The care, maintenance and protection of these facilities are Western's responsibility and it is up to it to make sure this just does not happen. Western would not expect to be asked to offer up access to its own linkspans if a council or CalMac linkspan went down, as indeed happened for several weeks in 2003 when the linkspan at Dunoon Pier went out of action.

Question 17: If Western has been able to successfully claim that it should be able to bid for the PSO for the CalMac passenger service on the basis that it was a different market from their present one, could they not also argue that the CalMac vehicle-carrying service is in a different market serving different customers from their present market and so the public linkspans are "essential facilities" for them also in that market?

Not really, because they have spent more than two decades arguing the opposite, i.e. that the CalMac vehicle-carrying service and their own service are in the same market. That is why restrictions were imposed on the CalMac service in the first place, and it also

underlies its arguments that the subsidy to the CalMac service is excessive, for example in their Briefing Paper they sent to MSPs prior to the Transport Debate in Parliament, 8th December. In the Herald article (11th December, p.6) on the announcement, Western's MD Gordon Ross said: "there actually is a commercial operator already on that route. It is called Western Ferries". So that settles that.

Question 18: Apart from finding a suitable operator, what are the main remaining problems?

Finding suitable vessels. The second hand market may be a thin one and even if vessels are available, work may have to be done on them to bring them up to EC standards. New build takes time, depends on spare capacity in shipyards, and involves a bigger financial commitment and risks by the potential operator. But Western's operating profit of £1.4mill on a turnover of £4.2mil (year ended 2003) should go a long way to convincing financial directors of other ferry companies that this is a market worth looking seriously at. The time horizon in the Scottish Executive announcement should certainly be long enough to identify if there is serious interest, though it may take longer to get an actual new service up and running if newbuild is involved.

Question 19: What will Western do now?

The initial response by the company was "surprise that the vote which sent the Executive back to the drawing board on the tendering issue did not affect the Dunoon Gourock route". When it became that the vote did not affect the Gourock-Dunoon announcement, Mr Gordon Ross, the company's MD said "there is no question that if the route comes up to tender we would certainly be interested." (both quotes Dunoon Observer, 10th December).

We would expect that Western will negotiate options on those second-hand vessels presently on the market that might be suitable for the CalMac route.

But that could also deplete what is already could be a very thin market and put obstacles in the way of potential entrants finding suitable vessels.

Western are also about to start trials at the new linkspan facility this month. We would expect them to propose to Argyll and Bute Council that they move part of the operations to the new linkspan, running over to their present facility at McInroys Point, and push for options to extend the service in the future should they so wish.

But that could siphon off more of CalMacs traffic at Dunoon and also be seen as putting obstacles in the way of another bow-and-stern loading service using that facility for the CalMac route, especially if the access times used by Western at Dunoon overlapped with access times to that linkspan that a commercial operator (or CalMac) would want if they were to fulfill CalMac's present timetable (CalMac will still be using the sideloading streakers and the other linkspan at Dunoon Pier at present).

Western can also be expected to bid to be the operator that runs the present CalMac service under the non-subsidised terms consistent with the announcement of 8th December.

Western might also step up its campaign against CalMac present subsidy (and its service) on the route. It might consider or threaten a possible complaint to the EC on these grounds, but it would be ill-advised to do so, both because of potential public reaction and the dangers of a closer investigation of how the past and present restrictions on the CalMac service have benefited Western for more than 20 years.

Western can be expected to criticize the Kay/Ferguson/Smith report to DGF/FSB arguing the economic case for a commercially viable ferry service on the CalMac route. They did so when the summary of results was released earlier this year. However, it would be difficult for them to do credibly because the basic data and assumptions used in the Kay/Ferguson/Smith report is that set out in Western Ferries own report into the Gourock-Dunoon ferries (co-sponsored by them along with CalMac and the Scottish Executive, and carried out by Deloitte Touche). Any significant changes we have made to the data and assumptions underlying the Deloitte Touche report are based on objectively observable events, and are independently verifiable as such.

Western will also step up its public relations activities at local level based on its representing itself as a community-based firm which has benefited local interests for many years. It will argue that it should have equal access to the new facilities that are being created with any other operator.

Question 20: Could these actions by Western create barriers to entry in the Gourock-Dunoon market?

Not if interested parties such as the owners of the linkspans (and support infrastructure) and potential operators are aware of their rights and obligations under EC law, for example any agreement Western might try to make for access to the public linkspans would be trumped by an operator wishing access on an essential facilities basis. Western's actions should at best have nuisance value if the letter and the spirit of EC law such as the essential facilities doctrine are adhered to. This is a case where transparency, communication and knowledge would be the best defence against any competitive distortions.

Question 21: What will be the EC's attitude to all this?

Its direct interest would be if a PSO (Public Service Obligation) was to be awarded. "A Public Service Obligation is, any obligation imposed upon a carrier to ensure the provision of a service satisfying fixed standards of continuity, regularity, capacity and pricing, which standards the carrier would not assume if it were solely considering economic interest" <http://www.scotland.gov.uk/news/2000/04/se01183.asp>

The Executive may be regarded as going beyond the minimum required by the EC in that it is market testing whether a PSO is required, and reserving the right to pursue a PSO if necessary. While the EC will not be directly involved in the process at this stage, the Commission should be very positive and welcome the market testing process which will generate valuable information and is very much in the spirit of EC legislation in this area.

Question 22: What if there is no serious interest from potential operators?

In that case, we are back to where we were at the beginning of December, though at least the market test process will have helped to justify a PSO. If any PSO was then set up it could lead to the certainty of a Western monopoly since it would have a strong incentive to outbid any other tenderers for the PSO unless safeguards were built into the PSO to prevent this happening. If there were no changes to the PSO that was previously on offer, the Executive could expect to face legal challenges from interested parties wishing to defend their communities and the public interest.

So it is in the interests of everybody, including the Executive, local councils, local businesses and other interested parties to do everything in their power to make sure this does not happen and that a second commercial operation is created, Gourock-Dunoon.

Question 23: Who stands to benefit from all this?

If genuine commercially-based competition was injected into the cross-Clyde Gourock-Dunoon with a second frequent vehicle-carrying service using the publicly funded linkspans, it could be expected to:

- (a) Benefit users by improving choice, fares and quality of service
- (b) Boost local economic growth and benefit dependent communities on both sides of the Clyde
- (c) Eliminate a considerable and unnecessary subsidy burden on the taxpayer on the current CalMac service
- (d) Significantly increase council revenues from ferry charges and dues at Dunoon compared to what would be obtained under any other scenario (such as a foot passenger service that Western might put on under a PSO)

These would all be recurring benefits accruing annually to the users, dependent communities, and the taxpayer at both national and local level. The net public economic benefit would be worth many millions in terms of combined gains and savings.

It could also be argued that Western would ultimately gain from the benefits of genuine competition on the market and help create sharpen its skills and competitiveness for when it finally does pursue its expressed aim of moving into other markets (Western Briefing Paper 8th December), and possibly competing against private commercial ferry operators that have not face the restrictions and controls that CalMac has faced on this market for more than two decades. However, it is appreciated that this is a point of view which might not be shared by Western at the moment.

Conclusions

The Executive's announcement of 8th December offers real hope that at last there will be a positive solution to the Gourock-Dunoon problem that has bedeviled successive governments for more than two decades. This is a possible solution where the commercial interest may be made to coincide with the public interest. There were other possible outcomes where commercial interest and the public interest may not have been so closely aligned.

The Executive have said they "expect to advertise the opportunity extensively in the New Year to attract the widest possible interest." Amongst other matters, if they have a shadow PSO available at that point (see answer to Question 6 above) for information to potentially interested operators, it will facilitate discussions with potentially interested operators and help reduce or avoid any subsequent confusion and problem relating to what might be expected of a commercial operation. The Executive have listened to the communities involved and responded. It is absolutely crucial that they continue to do so and work with the communities in a continuing basis as far as commercial and government confidentially allows. We hope that the individual or team involved in this process will come to Dunoon and Gourock at the earliest opportunity to discuss matters with local interested parties. In this respect, it would also greatly help matters if a contact person was designated in the Executive on this issue for local groups and individuals, just as there is for the consultation process on the proposed tendering of the main network

The owners of the public linkspans (Argyll and Bute Council and CalMac) should welcome any interest from ferry operators who might wish to use these facilities. However, any arrangements that are made should be made in full awareness of the implications of the Executive's announcement and the implications of the essential facilities doctrine under EC law (see especially answers to Questions 19 and 20 above).

Apart from that, it is essential that local groups and individuals work as energetically as possible to both attract welcome interest in the possibilities that the new linkspan and the Executive's announcement opens up. It is absolutely essential that the real opportunities this affords are seized and not wasted. The door that has been opened will not stay open for ever.

ENDS