RMT **Policy Briefing**

22 May 2023

'A great sucking sound': Eversholt as a case study in the parasitism of the rolling stock companies

Introduction

In October 2012, Andrew Haldane, then an Executive Director at the Bank of England, described the way that the banking sector drew people into its activities and extracted wealth from the nation as 'a great sucking sound'.

This striking metaphor could be used aptly to describe the relationship between the companies that lease trains and the railway industry. While passengers face reduced services and staff endure pay cuts and attacks on their jobs, one thing has remained absolutely unchanged during the pandemic: the ongoing looting of the railways by the rolling stock companies (ROSCOs).

In this briefing we examine one of the three rolling stock companies, Eversholt, and look at how they are sweating the UK rail industry's asset base for eye-watering quantities of money with the protection of the government and almost no public scrutiny.

- Eversholt's latest accounts show that **last year it paid a dividend of £40,700,000** to its Luxembourg-based parent company.

- In the last **ten years, has paid £380 million in dividends** to its Luxembourg-based parent, with an average annual dividend payment of £35 million.

- These dividends represent, on average, between around 70% of the profits being made by the group of companies.

- In the last ten years, **Eversholt has also paid £520 million in interest payments on inter-company loans from its parent company**.

- Since 2017, this has been in the form of a Eurobond – a form of loan - of £340 million from its Luxembourg-based parent company. Under the terms of this loan Eversholt pays a coupon of £14.06% or £**47,891,000 every year**.

- Over the term of this loan these payments will amount to **£1.8 billion in interest payments** in addition to the loan principal. This is simply a way of extracting dividends by another name.

- As a result of this loan, Eversholt also avoids paying £9.5 million every year to the Exchequer, or £363 million over the term of the loan. Eversholt's decision to use a Eurobond means that it will **avoid paying £363 million in tax** to the UK Treasury that would otherwise be due in Withholding Tax on these interest payments to its overseas Luxembourg parent company.

- Eversholt consistently invests less in new rolling stock than it makes every year in revenue on operating leases. Last year, it spent **just £11 million** on new rolling stock, while making **dividend and interest payments of £89 million** to its parent company in Luxembourg.

Far from being innovative investors in new rolling stock, Eversholt, like the other ROSCOs, is a parasitic interest in the railways, enriching itself at public expense while the government shields it from public attention and directs austerity at the staff who work on the railways.

The growing cost of leasing trains

Eversholt is one of three Rolling Stock Leasing Companies that own around 87% of the UK's trains. They were handed British Rail's stock of trains on privatisation and have continued to dominate the train leasing market ever since.

Eversholt own 3,426 vehicles and they lease trains to Chiltern, East Midlands Railways, Greater Anglia, Great Western, Govia Thameslink, LNER, MTR, Arriva Rail London, Northern, Scotrail, Southeastern and Transpennine Express, as well as the freight companies Freightliner and GB Railfreight (See Table 2).

The cost of leasing these trains from the Rolling Stock companies has been growing markedly over the last few years. In 2013, rolling stock leasing represented 13% of TOC spending. Now it represents 24%.

As Table 1: Growth in rolling stock lease costs

£m	2013/14 expenditure	% of spending	2020/21	% of spending
Franchised train operator expenditure	10,143	100%	12,600	100%
Staff costs	2452	24%	3,600	29%
Rolling stock charges	1,268	13%	3,000	24%

Why rolling stock costs are rising

Rolling stock leases work in a similar way to PFIs. The government sets the requirement to build new trains, the ROSCOs raise money to buy them from train manufacturers and then the operating companies lease them back.

Rolling stock companies would have us believe that they are innovative investors in new trains. Yet left to their own devices, the ROSCOs presided over an ageing fleet and failed to invest in new rolling stock, preferring to sweat old assets.[1]

This failure is why, in recent years, the government stepped in to mandate new rolling stock through franchises and to commission bespoke projects like the InterCity programme. Government has effectively paid for these purchases either in the form of the InterCity PFI deals or through franchise payments to TOCs that pay for the ROSCOs' additional investment.

As the ORR noted in their financial analysis of 2018-19, the growth in rolling stock charges does not reflect the upfront costs of buying trains but is instead 'largely due to the increases in the on-going costs of rolling stock after the recent replacement of various trains'. These ongoing costs are 'the increased cost of leasing and maintaining trains'.[2]

The ROSCOs are able to keep their lease costs high because the three companies effectively monopolise a market in which there is little interchangeability between their products and so, little real competitive pressure. Between them, they still own 87% of the rolling stock on the network. This is why they were investigated by the Competition and Markets Authority in 2009. In April 2020, the ORR recently advised that the measures put in place (inadequate though they were) to offset this monopoly position, should be maintained because there had been no significant change in the period since 2009.

There is little incentive on the TOCs to negotiate lower lease costs either, as they are not really paying for the rolling stock.[3] As a consequence, as academic research has suggested, the public is likely to be paying the ROSCOs for years after the real cost of the trains has been paid off.[4]

This is one major reason why, under the old franchising system, franchise subsidies from government rose sharply. The rising cost of operating leases was effectively covered by franchise subsidies to Train Operating Companies. As the National Audit Office pointed out back in 2004, government pressure on the ROSCOs to buy new trains would simply generate more demands for subsidies as it was "unlikely that TOCs would accept stronger

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[1] Office of Rail Regulation, The leasing of rolling stock for franchised passenger services: ORR's reasons for making a market investigation reference to the competition commission, 26 April 2007, pp. 73-74.
[2] Office of Rail and Road, UK rail industry financial information 2018-19, 26 February 2020, pp. 8 and 14.
[3] Jean Shaoul, 'Leasing Passenger Trains: The British Experience', Transport Reviews Vol. 27, no 2, (March 2007), p. 200; S. McCartney and J. Stittle, 'Engines of Extravagance': the privatised British railway rolling stock industry', Critical Perspectives on Accounting 23 (2012), pp. 153-167.
[4] For more details see RMT's report 'Picking up the tab for trains: how the public is funding profiteering in railway rolling stock' (RMT, July 2020).

obligations in their franchise agreements for the delivery of new trains, unless the costs of such obligations were reflected in higher franchise subsidies." The NAO report went on to note that as TOCs' principal sources of income are subsidies … and fares, "ultimately taxpayers and passengers will pay for the work."[5] Now, under the ERMAs, and the National Contracts, the cost of these trains is being directly covered by the taxpayer.

Eversholt: a dividend generating machine

As the RMT has shown before, the three ROSCOs are complex networks of companies whose parent companies are based overseas in low tax regimes like Luxembourg and Jersey.

These companies are geared toward the production and extraction of dividends and they have been very successful at doing this both up to, and during the pandemic.

- Eversholt's latest published accounts show that Eversholt UK Rails (Holding) Limited and subsidiaries (Security Group) paid **a dividend of £40.7 million** to its top UK-based holding company Eversholt UK Rails Limited. This company then paid the same amount as a dividend to its Luxembourg-based parent company UK Rails S.a.r.l.[6]

- As Table 3 shows (Appendix), in the last ten years Eversholt, **has paid £380 million in dividends** to its Luxembourg-based parent, with an average annual dividend payment of £35 million.

- These dividends represent, on average, around 70% of the profits being made by the group of companies.

The ratio of dividend to group profits indicates clearly that this ROSCO, like the others, is basically a value extracting machine that sucks money out of the rail industry. Very little money appears to be being reinvested in rolling stock.

Eversholt's Eurobond: A dividend by any other name

But dividend payments are only part of the value-extraction story and possibly not even the biggest part.

In addition to paying out to its shareholders in the form of dividends, Eversholt's UK holding company pays out massive amounts in the form of interest payments on a loan from its Luxembourg parent company.

In 2017, UK Rails S.a.r.l. lent £340.6 million to the UK based parent company Eversholt UK Rails Limited in the form of a Eurobond. The bond has a maturity date of June 2055 and carries a coupon of 14.06% meaning that the UK company must pay an interest payment on the principal of £48 million every year to its Luxembourg parent company. On its maturity date, the principal must also be repaid. This loan is then 'cascaded' down to the group company in the form of a 'subordinated loan' from Eversholt UK Rails to Eversholt

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[5] https://www.nao.org.uk/wp-content/uploads/2004/02/0304263.pdf, p. 7
[6] https://eversholtrail.co.uk/investors/?date=2022#content

UK Rails (Holding) Ltd.

Since the loan was issued, Eversholt UK Rails Limited has paid **£286.7 million in interest payments on this bond**. Over the term of the loan it will pay £1.8 billion in interest payments on a loan principal of £340 million. In other words, this debt is simply another way of extracting dividends by another name.

Table 4: UK Rails S.a.r.l's Eurobond and interest payments made by Eversholt UK Rails Ltd

Eurobond principal	Annual coupon (14.06%)	Interest payments over 38 years	Interest payments since 2017
£340.6	£47.9	£1,819.9	£286.7

Added to its annual dividend payments, Eversholt's commitment to pay £48 million every year in interest means that **each year, the company is moving around £90 million overseas to its Luxembourg parent company.**

Tax avoidance

One major advantage of the form of loan that UK Rails S.a.r.l has issued is that it avoids normal taxation on international interest payments.

Ordinarily, interest payments from a UK company to its overseas parent would be subject to a 20% withholding tax. Eurobonds, however, are exempt from this withholding tax provided they are listed on an international stock exchange. Eversholt's Eurobond is listed on the International Stock Exchange and this allows it to avoid paying withholding tax on interest payments.

This withholding tax would be worth £9.5 million every year to the Exchequer and £363 million over the term of the loan. Eversholt's decision to use this Eurobond means that it will avoid paying £363 million in tax to the UK Treasury.

How the government has helped keep the capital flowing (out)

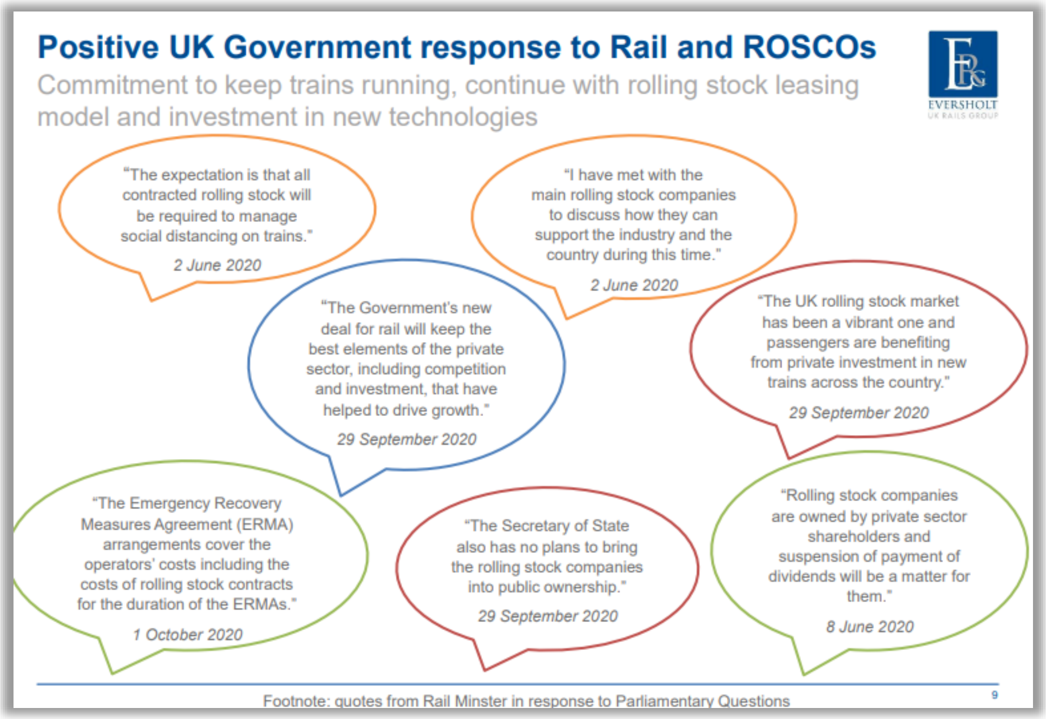
The government is intensely relaxed about the ROSCOs enriching themselves. As RMT has shown before, the government has stepped in and guaranteed that the ROSCOs' lease payments will continue to be paid in full and has made no attempt to control either lease charges or dividend payments.[7]

This support is very reassuring for the ROSCOs. As RMT revealed recently, Eversholt is using an infographic of Heaton Harris's answers to reassure investors that the dividend payment will keep flowing.

Figure 1: Extract from Eversholt Rails investor presentation, December 2020[8]

7 https://www.rmt.org.uk/news/minister-confirms-that-the-public-pay-for-railway-profiteering/

8 Investor Presentation - Dec 2020v.3.1 - Table of Ext v2 (eversholtrail.co.uk)



Eversholt's accounts show that the company had a good pandemic year, noting that because of the government support, "the Directors do not believe that COVID-19 presents any material risks to the Group".

This support is also vital for the ROSCOs' ability to raise bond finance.

Big investors?

The ROSCOs like to claim that they are big investors in the railways. In their promotional literature Eversholt say,

> *"We procure and finance new rolling stock and have invested more than £3 billion in new trains since privatisation."*[9]

But this would appear to be a major overstatement of their investment. As we saw above, Eversholt, like the other ROSCOs, typically remit almost the vast majority of their profits to their parent company in the form of dividends and interest payments which then disappear into Luxembourg.

This impression is reinforced when we look at their spending on assets. It would appear that very little is being spent on new trains.

As Table 5 (Appendix) and Figure 1 show, over the last 10 years Eversholt's rolling stock asset base has grown modestly, by around £400 million in value. Spending on rolling stock rose modestly from almost nothing in 2012, peaked in 2019 and has dropped to just 11 million over the last three years.

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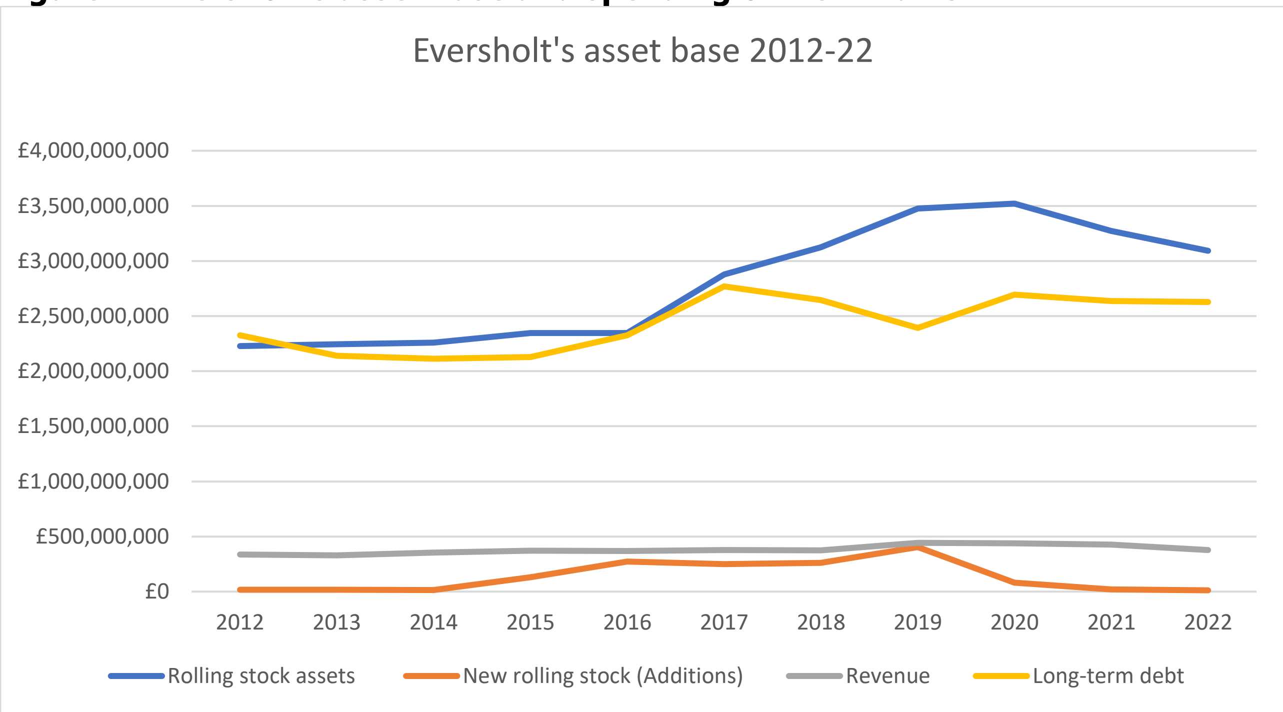
[9] https://eversholtrail.co.uk/

By contrast, their revenue has averaged £380 million each year and their long-term borrowing, which might be where we could see if Eversholt were borrowing to finance new rolling stock, has actually fallen slightly.

This is unsurprising from one perspective as the ROSCOe' bond covenants generally require them to maintain a certain ratio of Earnings Before Interest Taxation Depreciation and Amortisation (EBITDA) to their long-term debt.

So, like the other ROSCOs, Eversholt are consistently earning far more in revenue from leases than they spend on new trains and they don't appear to be engaging in long-term borrowing finance risk-taking. The small amount they are spending on trains is more than covered by their annual lease revenues, still enabling the extraction of around £90 million in dividends and interest payments each year. This is not innovative capitalism, it is rentier parasitism.

Figure 1: Eversholt's asset base and spending on new trains



The rolling stock racket

The rolling stock racket is a long-established scandal on the railways. In the last 10 years, the Rolling stock companies have paid out £2.7 billion in dividends to their owners. As we've seen, these dividends typically represent almost all their pre-tax profits. The average aggregate dividend payment is around £260 million each year. As RMT has previously shown, the cost of leasing rolling stock is growing faster than any other cost and now consumes almost a quarter of TOC spending.

Yet even as it attacks staff pay and jobs, the government maintains a deafening silence about the Rolling Stock companies and their grotesque profiteering.

RMT believes that this broken model of train procurement needs to be finally swept away.

The public should buy and own our trains directly, rather than paying extortionate rents to these three companies.

As an immediate step the pandemic profiteering must be curbed. The government could announce a windfall tax on profits of the Rolling Stock companies and use the proceeds to help fund a fare rebate for passengers and a fair pay deal for staff.

Table 2: The ROSCOs' overseas parent companies

ROSCO	Major shareholder	Registered	Ultimate Parent
Porterbrook	Allianz Infrastructure Luxembourg I	Luxembourg	Allianz Capital Partners, the investment of arm of Allianz Group, the German multinational insurance and financial services giant.
	PIP4 Thomas LP on behalf of AIMCo	Canada	AIMco is the Alberta Investment Management Corporation which is an investment vehicle for Alberta pension funds and endowments.
	Utilities Trust of Australia International Pty Ltd	Australia	Utilities Trust of Australia (UTA) was set up as an infrastructure investment fund by Hastings Funds Management, now Vantage Infrastructure. In 2018, UTA appointed New Zealand based infrastructure investment fund Morrison and Co to manage their investments, including Porterbrook.
Angel Trains (Willow Topco Ltd – registered in Jersey)	AMP Capital Investors (Angel Trains Topco) S.a.r.l	Luxembourg	AMP Capital Investors owns 65% of Angel Trains. AMP Capital Investors is part of AMP Capital, an investment arm of the Australian financial services firm AMP Group Ltd. AMP Capital also has a minority holding from the banking arm of Mitsubishi.
Eversholt Investment Ltd Security Group	UK Rails S.a.r.l.	Luxembourg	UK Rails S.a.r.l. was, until this year jointly owned by CK Infrastructure Holdings Limited and CK Hutchison Holdings Limited, which is registered in the Cayman Islands. UK Rails S.a.r.l. is now the controlling party.

Appendices:

Table 2: Who leases Eversholt's vehicles?

Train operating company	Vehicle type	Number of vehicles leased
Chiltern	Class 168	9
EMR	Class 170	15
EMR	Class 222	143
Freightliner	Class 66	56
GB Railfreight	Class 66	27
Greater Anglia	Class 321	400
Greater Anglia	Class 321 Renatus	120
GTR	Class 171	12
GTR	Class 455	185
GWR	Class 802	236
LNER	Class 91 Locomotives	24
LNER	Mark 4 Coaches	133
MTR/Arriva Rail London	Class 315	60
Northern	Class 158	20
Northern	Class 195	149
Northern	Class 322	20
Northern	Class 331	141
Scotrail	Class 318	63
Scotrail	Class 320	102
Scotrail	Class 334	120
Scotrail	Class 380	130
Southeastern	Class 375	438
Southeastern	Class 376	180
Southeastern	Class 395	170
Southeastern	Class 465	388
TPE	Class 185	153
TPE	Class 397	60

Table 3: Eversholt UK Rails (Holding) Limited and subsidiaries (Security Group) 2012-2022

(m)	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	TOTALs / AVE
Revenue	337.4	329.2	353.1	371.6	367.4	378.4	374.9	442.6	438.7	426.1	375.9	**4,195.3**
Cost of sales	197.5	180.9	193.6	171.4	163.2	170.6	185.8	223.2	228.8	195.5	169.8	**2,080.3**
Gross profit	139.9	148.3	159.5	200.1	204.1	207.8	189.2	219.3	209.9	230.7	206.1	**1,248.9**
Pre-tax profits	-45.9	12.6	-52.1	61.1	7.7	50.3	30.5	31.7	18.6	78.2	71.5	**264.1**
Gross profit rate	41%	45%	45%	54%	56%	55%	50%	50%	48%	54%	55%	**49%**
Pre-Tax profit rate	-14%	4%	-15%	16%	2%	13%	8%	7%	4%	18%	19%	**6%**
Dividends	40.0	0.0	50.0	20.8	14.8	43.0	40.1	41.6	46.5	41.8	40.7	**379.2**
Dividend as a % of profit	-87%	0%	-96%	34%	193%	86%	132%	131%	249%	53%	57%	**68%**
Interest on intergroup loan from parent company)	55.4	53.0	49.8	23.7	50.1	48.0	47.9	47.9	48.0	47.9	47.9	**519.7**

Table 5: Eversholt's asset base and spending on new rolling stock

	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Rolling stock assets	2,227.7	2,243.6	2,259.2	2,346.7	2,346.7	2,876.4	3,124.1	3,476.9	3,520.4	3,272.5	3,091.5
New rolling stock (Additions)	17.7	16.0	15.5	129.7	272.1	248.6	261.4	404.1	80.6	21.5	11.9
Revenue	337.4	329.2	353.1	371.6	367.4	378.4	374.9	442.6	438.7	426.1	375.9
Long-term debt	2,325.1	2,140.0	2,113.0	2,127.8	2,326.1	2,769.3	2,645.9	2,391.8	2,695.2	2,637.0	2,628.1

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