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FirstGroup chief Tim O'Toole offered to quit with chairman over £2bn debt

Transport firm CEO, who was told by Martin Gilbert to carry on, spearheading courtship of big investors over £615m rights issue

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Despite the west coast mainline fiasco, it is the bus rather than the train that is to blame for Tim O'Toole having to head FirstGroup's rights issue. Photograph: FirstGroup

FirstGroup's chief executive, Tim O'Toole, will this week visit its biggest institutional investors to secure backing for the troubled transport operator's £615m rights issue, as it emerged that he offered to quit instead of the chairman.

Martin Gilbert announced his resignation last week after the group concluded it could no longer continue struggling with its £2bn debt. Sources close to the company said O'Toole had, in a private conversation, told the chairman he would also consider his position, but Gilbert said he should carry on.

O'Toole will steer First through a £1.6bn programme of investment over the next four years – primarily in renewing its ageing bus fleet. After the west coast mainline fiasco, in which it missed out on the lucrative railway linking Britain's biggest cities, it would be natural to blame rail for its troubles. But the malady that has forced the firm's rights issue was incubated in the mode of transport it knew best: the bus.

The company, which bills itself the "world's largest public transport operator in private hands", began with a small municipally owned bus company in a far corner of Scotland. Formed from a management buyout under privatisation and a merger with south-west England's Badgerline, the new FirstGroup plc was little more than a decade later striking a deal that would make it the biggest player in key US markets – but at a cost that it is finally having to address.

Borrowing billions, First acquired US transport firm Laidlaw in 2007, and now provided 40% of school bus services across the States. But the takeover did not go to plan: attempts to reduce the debt to a manageable sum by hiving off the newly acquired Greyhound coach service to another buyer fell through. The school runs on a 54,000-strong fleet of the yellow buses did not generate the anticipated profits, and First's share price fell while the group's debt burden made the ensuing bumps in the road ever harder to absorb.

The services it runs in about 40 towns and cities in Britain also began to run into trouble. Passengers were deserting deteriorating, clumsily managed services, with routes slashed and fares pushed up, to the point that there were campaigns and protests against the operator in cities such as Bristol. Changes in government grants and support for concessions exacerbated problems in a bus business that had been generally regarded as a safe cash cow, leading to a profits warning last year.

These headwinds and growing questions over the group's debt partly explain why First bid so keenly for the west coast mainline – a bid so high that rival Sir Richard Branson, the Virgin boss, branded it "insanity", though O'Toole has consistently defended it since. Instead of securing the bandage of a lucrative rail franchise, First licked its wounds as the government paused the entire rail franchising programme, a delay that diminished options beyond the long-resisted rights issue – one being considered even when US railwayman O'Toole joined the board four years ago.

What First now describes as an "albatross" was debt that peaked at £2.6bn after the acquisition of Laidlaw. While the debt was being eroded – partly through selling assets – fears that rating agencies would downgrade First's creditworthiness to junk status, piling on financing costs, forced the group's hand.

Douglas McNeill, a director at investment firm Charles Stanley, said: "Pressing on without a rights issue wasn't doomed to failure, but it was risky: when you have a lot of debt you need everything to go well. You're vulnerable to events.

"Had they done it earlier when the share price was higher it would have been less painful, less dilutive for shareholders."

Those shareholders include at least 8,000 FirstGroup staff who have been part of a long-term share buying scheme, and would likewise have seen their nest eggs slashed by a third last week as the share price nose-dived for the second time in seven months. The RMT union said: "Low-paid guards and platform staff have been propping up the share price with a scheme that might see them losing all their money – and now potentially their jobs because of the chaos at the company." First dismissed the union's claims that the schemes had been closed or that jobs were at risk.

The one man who did lose his job, Gilbert, was a director of First running buses in Aberdeen when Sir Alex Ferguson was still managing the local football club, and has overseen a similar transformation in the scope and scale of the business as Fergie at Manchester United. Analysts believe one sacrificial lamb will be enough to appease shareholders, and O'Toole will have some breathing space.

A First spokesman insisted the rights issue, which should be ratified by shareholders on 10 June, is "good news: we can pay down debt, this is a licence to invest and grow, even if the share graph over 24 hours looks terrible – it's what analysts were expecting". McNeill concurs: on First's prospects, he is "optimistic – for the first time in a while".