

Shaping Britain's railways: the periodic review



OFFICE OF RAIL REGULATION

May 2011



Why your views matter

This is a critical time for Britain's rail industry and it needs to demonstrate - to passengers, freight customers and taxpayers - that it is up to meeting the challenges and grasping the opportunities it faces.

- On many measures - including performance and safety - our railways have never been more successful
- They are carrying more passengers than ever before, with passenger demand forecast to continue to grow
- But this success has come at a high cost to passengers and taxpayers - with industry costs up to 30 per cent higher than other European railways
- In order to justify continuing public investment the industry needs to deliver a step change in efficiency and provide better value for money

Sir Roy McNulty's recent report calls for £1 billion of savings from the sector, with a significant improvement in Network Rail's efficiency.

It is therefore vital to have a wide-ranging debate to understand what we want from our railways and to enable informed choices as to how this can be best achieved with the money available.

Periodic review

A periodic review typically takes place every five years and provides a major opportunity to drive through a step change in industry performance and efficiency for the benefit of taxpayers and the passengers and freight customers who rely on Britain's railways.

At the heart of the review is our assessment of what Network Rail (who manages the rail infrastructure) must achieve from 2014, the money it needs to do so, and the incentives needed to encourage delivery and outperformance. But the review goes beyond Network Rail and looks at how it should work more closely with train operators, suppliers and others to reduce costs and deliver more for customers.

Our objective for the periodic review:



"To protect the interests of customers and taxpayers by ensuring our determination enables Network Rail and its industry partners to deliver or exceed all the specified outcome and output requirements safely and sustainably, at the most efficient levels possible comparable with the best railways in the world by the end of the control period.."

Key dates

May 2011
ORR initial PR13 consultation

♦
September 2011
Rail industry publishes its initial plan

♦
February 2012
ORR provides formal advice to Ministers on outputs and funding

♦
July 2012
DfT and Transport Scotland publish their output specifications and outline available funding

♦
August 2012
ORR consults on Network Rail's outputs

♦
January 2013
Network Rail publishes its strategic business plan

♦
June 2013
ORR publishes and consults on draft determination

♦
October 2013
ORR publishes final determination

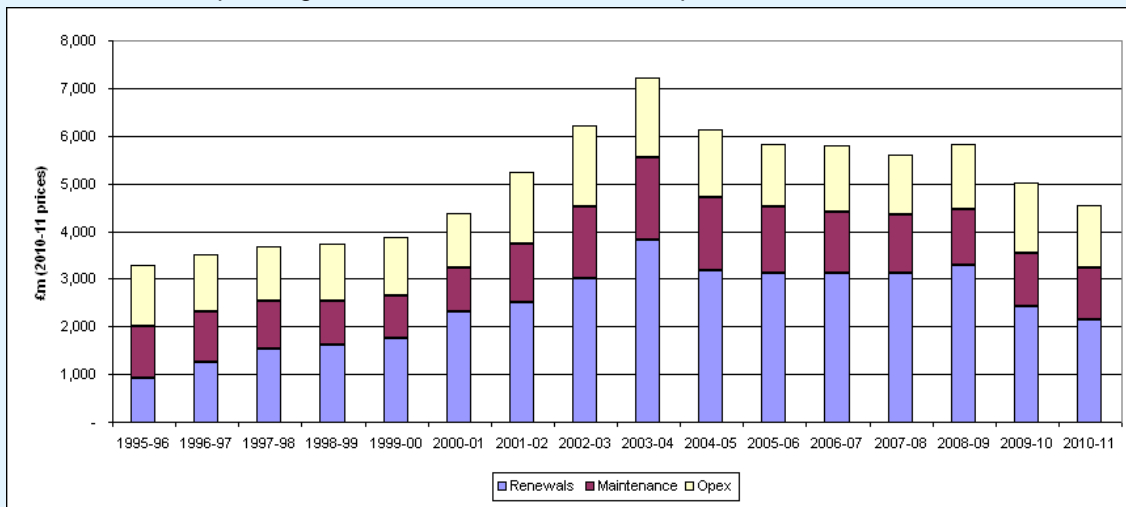
♦
November/December 2013
ORR issues list of access charges

♦
April 2014
The new control period begins

Rail industry costs

As the chart below shows Network Rail's costs are coming down. But they remain much higher than they should be. We expect the company to close the remaining efficiency gap with the best performing rail infrastructure managers by 2019.

Network Rail's operating, maintenance and renewals expenditure since 1995-96



Source: ORR

Sir Roy McNulty's recent rail value for money study took our analysis of Network Rail's costs and looked more broadly at the efficiency of the whole rail industry. His report highlighted that whole-industry costs are 30 per cent higher than comparable railways elsewhere in Europe. This is reflected in the high levels of fares and the need for continuing taxpayer support.

Key issues for consultation

✓ How best to improve efficiency and reduce costs to taxpayers and customers?

The work we will do to assess the scope for future efficiency improvements by Network Rail will be critical to reducing costs. So too will our work to incentivise Network Rail and train operators to work together to reduce costs and increase revenues.

✓ How best to improve the transparency of industry costs?

Better quality and more granular publicly available data will support improved benchmarking of Network Rail's costs; allow for efficiency benefit sharing between Network Rail and train operators; facilitate more local decision making; and provide better information to taxpayers and fare payers, including on where public subsidy is being spent.

✓ How to get the industry to play a bigger role in planning and delivering the railway?

The industry is closer to customers than government and better placed to respond to customer demand and expectations. We are encouraging the development of an industry plan to inform our periodic review and a clear delivery plan at the end of the review to ensure that it is implemented.

✓ How to get the best out of, and continue to develop, the rail network?

At a time of rising demand and concerns over costs we need to ensure that informed choices are made between capital enhancement and operational solutions (such as timetabling) to problems like congestion on the rail network. Questions also arise as to which projects should be supported in a cash strained environment. The periodic review will look at how incentives and access charges can be used to support this.

✓ How best to balance risk and reward across the industry?

Risks between Network Rail and its customers and funders should be allocated according to who is best placed to manage them to provide the best value for money overall. In line with this, the periodic review will look to balance risks and rewards for Network Rail.

✓ How best to deliver better value for money without compromising safety?

There can be no compromise on safety. Significant change will be required from the rail industry and it is essential that the way this change is planned and implemented does not jeopardise safety. We will ensure safety is integral to our approach to the review.

Key decisions we will be making

As part of the periodic review, we will be making a number of important decisions and providing advice to Ministers on matters such as public funding. The key issues are summarised below and set out in further detail in our consultation document <http://www.rail-reg.gov.uk/pr13/consultations/orr013.php>. Your views are welcome on all of these.

✓ How to enable more local decision making

The devolution of Network Rail decision-making from national to route level will provide greater focus on the local needs of the railway, train operators and their users, providing for better partnerships. We will undertake much of our analysis at the route level, for example working out how much Network Rail needs to spend. To allow this, we will require, and publish, more disaggregated financial information from Network Rail.

✓ How to improve incentives

We intend to improve the incentives on Network Rail and the industry to reduce costs and deliver more for customers by working together. For example, we plan a route-based efficiency benefit sharing mechanism for Network Rail and train operators to share the savings where outputs are delivered more efficiently than we assumed.

✓ How to establish what Network Rail should achieve

In setting Network Rail's outcome and output obligations, we need to decide how these can best be framed to ensure that they are delivered and represent value for money. We also need to consider which outputs should also involve train operating companies.

✓ How to set Network Rail's financial framework

We are consulting on a number of issues relating to the financial framework in which Network Rail will operate in the next control period. These include the length of the control period, how Network Rail is expected to manage risks, and the rate of return on the regulated asset base.

✓ How to set train operator charges

Train operators pay access charges to Network Rail. We are considering changes to how charges currently work, including moving to charges based on how congested the network is and measures to reduce the amount of electricity that trains use.

We are also considering changes to the basis by which open access passenger operators pay for track access and exploring how greater on-rail competition could work in practice. We will be publishing a study on on-rail competition in July.



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Key stages of the review process

✓ **Stage one** - from May 2011 until February 2012 focuses on consultation on a number of key issues in preparation for the latter stages. It culminates in our advice to the Secretary of State and Scottish Ministers on how they should develop their **high-level output specification (HLOS)** and a **statement on funding available (SoFA)**. These set out what they want to be achieved by the railways from 2014 and the public financial resources that are, or are likely to be, available for this.

✓ **Stage two** - from February 2012 to October 2013. During this phase we will consult on more detailed issues relating to the regulatory framework and how access charges should be set. The Secretary of State and Scottish Ministers must also issue their HLOSs and SoFAs to us.

This is a key stage of the review and it is important for stakeholders to make their views known to the relevant government in relation to the issues and priorities that they consider are most important. It ends with the publication of our determinations.

✓ **Stage three** - from October 2013 to April 2014 sees the detailed planning by Network Rail and its partners for the implementation of our determinations.

Your views are important

Our initial consultation closes on **2 September 2011** and we encourage you to respond to the questions set out in our consultation document <http://www.rail-reg.gov.uk/pr13/consultations/orr013.php>.

As part of the consultation process we will be inviting stakeholders to a series of workshops on the following dates:

- 5 July - Edinburgh
- 11 July - Cardiff
- 12 July - London
- 21 July - Manchester

Summaries of the discussion at these workshops will be published on our PR13 website. We are also willing to meet with, and run workshops for, interested stakeholders.

Stay up to date

- Visit our PR13 website at <http://www.rail-reg.gov.uk/pr13/>.
- Register for news by email updates <http://eepurl.com/KAKd>

About the ORR

As **national safety authority** we regulate health and safety for the entire mainline rail network in Britain as well as London Underground, light rail, trams and heritage sector.

Our functions as **economic regulator** of the mainline railway include setting Network Rail's funding to enable it to carry out its work efficiently, ensuring that it delivers the agreed outputs whilst improving its own efficiency.

As a **competition and consumer authority** we use our powers to ensure that users and funders of railway services benefit from competitive railway markets and that passengers are treated fairly.

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