

What future for Britain's railways?

Pull it out and pass it on!

Ten years after rail privatisation, the Government is considering how the industry should be organised in future. Here, Railfuture sets out its views on the way forward

1 Basic approach

1.1 Railfuture does not seek change for change's sake, mindful that any reorganisation distracts from running the system. But whilst the railways need stability, they also desperately need the right structure. We therefore propose some moves which we believe can be achieved without drastic upheaval.

1.2 One general point: we strongly urge the Government to listen to all views from all parts of the industry, stakeholders, consumers, academic and other external commentators, to consider objectively all comments and to seek a consensus before acting, notwithstanding the need to act with due speed. In 1993 the then government acted in haste on dogmatic, ideological imperatives and disregarded almost all advice they received. The consequences of this are with us still. We must not make the same mistake again. Rumours that the Government has already taken a view on several key aspects of its Railway Review are therefore alarming and we hope they are unfounded.

2 Privatisation versus renationalisation

2.1 Privatisation has solved some problems, but created others. Most of us were against it, at least in the form proposed in 1993, and with the benefit of hindsight, on balance we still are. But we have to start from here. Much as some might wish it, we do not believe that renationalisation as such is practical or even desirable, less still that it would solve everything. Indeed it would be a major distraction to management. We do not therefore support it at this time.

2.2 We believe that the key issue is not ownership, but (re)integration, and in some respects, control. The big mistake made in 1993 was fragmentation, not privatisation as such. The industry was broken into too many pieces and mistakes were also made in the regulation and control structure, which was not based on sound business principles, created a myriad of interfaces and inevitably led to increased costs. We recognise that progress has already been made under both these headings since 1997, and we propose further moves in this direction.

3 Changes since privatisation: The SRA

3.1 The first major change was the creation of the Strategic Rail Authority in the 2000 Act. We campaigned for the creation of the SRA, as we saw the need for a body to give guidance, direction and voice to the industry as a whole, and to look beyond the limited horizon of finite franchises. We do not always agree with their decisions (notably on some aspects of refranchising – see below), nor do we feel that they have yet found their real role. Under the first chairman they eschewed "command and control" in favour of a light touch, arguably too light, whereas under the present chairman they have engaged in detail to the exclusion of the bigger long-term view. We believe it is the job of the SRA to focus on long-term strategy.



NEW TRACK: Track workers prepare London St Pancras station to receive Eurostar trains in three years time. Work is under way on Britain's first high-speed railway from the Channel Tunnel to St Pancras which will be a hub for the international trains and inter-city trains to the English Midlands. Although a new Thameslink station box is being provided underground adjoining St Pancras, there is now no way that Thameslink 2000 can be implemented in time for the first international arrivals. Without Thameslink 2000, travellers from Europe are likely to find it much more difficult to find connections to their final destinations.

Picture: RAIL LINK ENGINEERING

So while we have our criticisms of them, we remain convinced of the need for a Strategic Rail Authority within the present structure. Among functions it might take on are responsibility for the National Rail Enquiry Service and publication of the National Rail Timetable. We will return to issues of their relations with other regulatory bodies, but we would be firmly opposed to a return to a purely franchising body (OPRAF), or to merging a rump SRA into the Department for Transport.

4 Changes since privatisation: Network Rail

4.1 The other major change was the replacement of Railtrack by Network Rail. Whilst the manner of this change in the aftermath of Hatfield was open to criticism, there is little doubt that the effect has been a positive one, bringing the infrastructure side under a proper degree of public control once more. The original sell-off of Railtrack was one of the main mistakes of the previous administration, and was not even provided for under the 1993 Act. Alongside the effective return of Railtrack to the public sector, an even greater benefit has been gained from bringing maintenance back in-house (from this year). This has cut out a layer of subcontracting, a major source of cost-escalation, and is a significant step towards reintegration. It is to be hoped that this process might continue with at least minor renewals, possibly some major

renewals, going down the same road. All these processes we support.

5 Ongoing organic change: Franchises

5.1 If there has been progress on the infrastructure side, the picture on the operational side is more mixed. Some have seen the taking of the southeast franchise temporarily in-house as the way to bring all operations back into the public sector in the same way as Network Rail did with infrastructure. Suffice it to note that this option exists, at least in principle, and is beginning to look increasingly attractive.

5.2 Refranchising offers some opportunities for change, and the SRA has sought to exploit these, primarily to create larger franchise units. This we support, although the policy has not always been applied consistently and we have severe reservations about the approach adopted in the North of England in particular. The most important consideration has to be quality of management. Nevertheless the objective of reducing the number of franchises to about a third of the present number is another welcome move in the direction of a less fragmented industry. (It should be noted that this does not preclude microfranchising in appropriate circumstances.)

5.3 Another aspect of franchising on which policy seems to have oscillated from one extreme to the other is the length of franchises. While

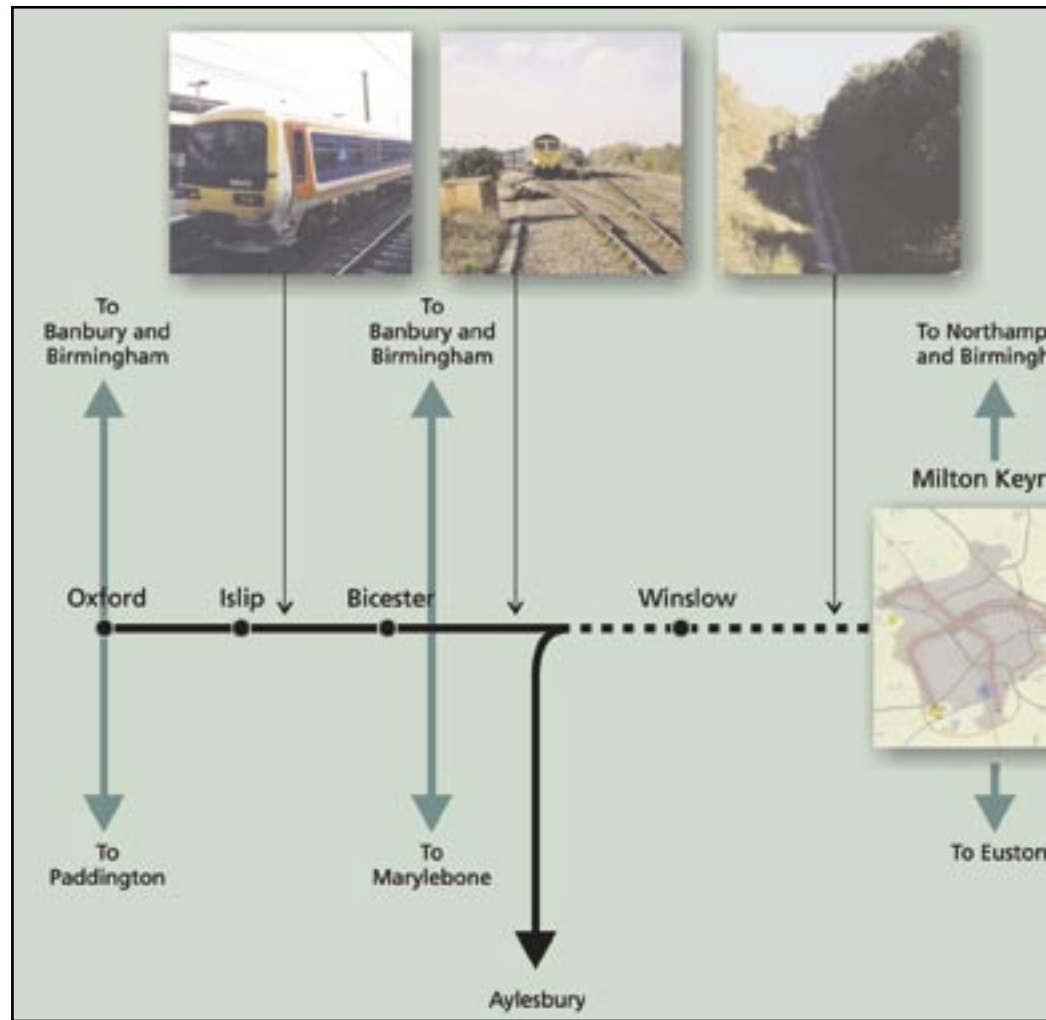
there are arguments for and against both long and short terms, it is clear is that short franchises effectively prevent any major investment which involves the franchise holder. This might not matter if the SRA were more pro-active on long-term investment. Unfortunately this is not happening. Franchise bidders are told to concentrate on running the specified service and leave the long-term visionary plans to the SRA, yet in the next breath the SRA announce that they are doing no long-term planning because the funds are not there, despite several prospective franchisees having offered funding for just such schemes. This is unacceptable. Of course we must get the existing system right first, but if we do not start planning for the long-term we will never achieve real development of the system to cope with exploding demand. We believe this is the job of the SRA.

5.4 If short franchises are problematic, a policy of rolling two-year extensions (which seems to be the current SRA preference) is even more fraught with difficulty. Given that the process of specification, bid preparation, submission, evaluation and implementation itself takes the best part of two years, and that all but one bid will be abortive, this means that a fair chunk of resources not only of the SRA but of TOC managements is tied up almost permanently on tendering, much of it abortive. This has to be an inefficient use of resources which should be devoted to running the service. In summary, the shorter the franchises, the more the system operates in a permanent state of uncertainty and absence of essential long-term planning. For this and other reasons, the time may have come for a long hard look at the suitability of franchising for rail operations in principle. It may not be practical to do this within the ambit of the present Review, and in any event the earliest practical date for implementing any non-franchise alternative might be as far away as 2010-12, as only three of the current franchises run beyond that date. That gives ample time for some objective expert studies. In the meantime it may be no bad thing if a few more franchises reverted to direct SRA management.

6 Vertical integration

6.1 Almost from day one of separation in 1994 there has been pressure to restore vertical integration between track and trains, and on practical operational grounds there is much to be said for this. But it is worth recalling the thinking behind separation. European Commission Directive 91/440 is widely believed to require separation, but in reality it requires only separate accounting, to facilitate open access (especially for freight). The model was the earlier Swedish reforms which were part of a wide-ranging reform of finance and taxation of both road and rail with a view to placing the two modes on an equal footing. There is thus a respectable case to be made for separation, but not only did the 1994 UK legislation not include the parallel reforms needed to achieve it, it actually went further than the EC Directive required in separating railway infrastructure and operations. In other words, given that separation has clear costs in everyday operations, we have ended up with the worst of both worlds – the costs without the benefits. Since more radical reform of transport funding seems unlikely, it would make sense to restore as much vertical integration as is compatible with the Commission Directive.

6.2 Two alternative approaches are on the table. One has been called “virtual integration”, and consists of aligning franchise areas and infrastructure zones as closely as possible, with a view to introducing closer



day-to-day cooperation and joint working on the ground, as has been the case in Scotland. This is hardly rocket science, and ought to be good practice anyway. The second option, promoted by Stagecoach in 2002, takes this a stage further, to create joint operating and infrastructure franchises, with the franchisee looking after the infrastructure in their area. Stagecoach believe this would be compatible with the EC Directive, and proposed trial franchises which might include not only the easy cases (Merseyrail and Island Line effectively are already, LTS/C2C and Chiltern south of Aynho could follow), but also more complex systems like Anglia, Great Western, Scotrail or Stagecoach's South West Trains franchise. This is an attractive idea and merits careful examination and testing. It might imply infrastructure maintenance returning to the private sector, or some operations to the public sector. The question is not so much should vertical integration happen but rather how it should happen and with what degree of management risk, but in either case even if we assume a pattern of regional franchises, the operations and infrastructure maps are never going to match precisely.

6.3 There will be a need for safeguards for long-haul intercity operators (east and west coast and especially cross-country) as well as open-access operators such as Hull Trains, and above all for freight operators. Indeed in the absence of anything other than a fully integrated railway, there will continue to be a need for a Rail Regulator to govern settlement arrangements in overlap areas and for non-regional operators.

7 The regional dimension

7.1 Scotland and Wales are already benefiting from involvement of their devolved bodies in rail and other transport policy. This is a development which could be extended to the English regions especially if elected bodies are introduced to these areas. Ideally

this would take the form of regional PTAs/PTEs covering rural as well as urban areas. We have long pressed for the established and highly successful PTA/PTE model to be extended to non-metropolitan areas. Whilst this could be done at shire county level, the spread of unitary authorities mean that a plethora of joint boards would be necessary unless the regional tier can take it on. Bus services may require to be handled at county level by delegated powers, but for rail a regional pattern of franchises and infrastructure areas would fit well with this approach, although it is clear that in much of the country the administrative map will never match closely the railway operations or infrastructure maps. Among other things, it would also be necessary to consider with which pattern the structure of Rail Passenger Committee areas should be aligned.

7.2 Assurances would be needed that the regional dimension would be an additional source of funding, rather than a replacement for present funding streams, and that the regional network remains part of the national rail fares and ticketing system, especially in rural areas. (These considerations also apply to microfranchising and Community Railways.) There may also be scope for joint funding arrangements such as Private-Public partnerships, although the record of these in other areas (including London Underground) is not exactly one of universal glory, and the ease with which the SRA has turned off the tap of Rail Passenger Partnership and rail freight grants is not an encouraging precedent.

8 Regulatory bodies: SRA and Regulator

8.1 Much attention has focused on the relationship between the several regulatory bodies – the SRA, ORR and HSE, and their relationships with each other. Whilst we



East West Rail

The run-up to privatisation killed off British Rail plans to reopen the line from Bletchley to Oxford, and run through trains to Bedford.

As reopenings go, it would have been one of the most simple to implement and one of the most popular.

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Politicians and civil servants should use the east-West project as a litmus test.

Any new structure must be capable of delivering projects like this.

They are an alternative to a future of poisonous road building.

understand the urge to eliminate overlap and simplify controls, we see difficulties with many of the proposals being floated. In particular, despite its faults, we see the SRA as an absolutely key body in the rail industry, and would be strongly opposed to any proposal to reduce it to its previous purely franchising role and/or absorb functions into the Department for Transport. This would be a retrograde step and place the rail industry too firmly under government control especially regarding funding.

8.2 Proposals were made at the time of the 2000 Act, that the Regulator's office be merged into the SRA. We were unconvinced of this idea then and remain unconvinced now, not least (as the present Regulator has pointed out) because the status of the bodies is different, one being a government agency and the other an independent body. The nature of the Regulator's remit and relations with both government and bodies such as the SRA will no doubt change when the new Board takes over in July, and some reallocation of responsibilities could well take place then.

8.3 A more interesting proposal for the SRA, which would fit well with moving towards vertical reintegration (or virtual integration), is for a parallel merger between the SRA and Network Rail, now that the latter is in the semi-public sector. This has attractions, as it would bring the driving and controlling forces at national level on both infrastructure and operations under one roof and really begin to look like an integrated railway once more. It is certainly worthy of consideration. The new not-for-dividend status of Network Rail ought to make this a more practical and attractive proposition. An independent regulator would of course be even more essential in the event of this merger.

9 Regulatory bodies: HSE and Railway Inspectorate

9.1 When it comes to the Health & Safety Executive and the status of the Railway Inspectorate however, there is a clear and widely recognised case for change. HM Railway Inspectorate had a long tradition of expertise on railway safety as an independent agency under the Department of Transport. Merger with the HSE was ill-advised and has not been a success. The HSE philosophy is fine for the workplace or factory, but a different approach is needed on a transport system where safety has to be balanced against performance, sheer practicality and (above all) cost. The old Inspectorate understood this, but the HSE seemingly does not. The need to restore the independence of the Inspectorate was recognised by Lord Cullen following Ladbroke Grove, but the Government sought instead to reform the HSE from within. This strategy has failed, and it is imperative that HM Railway Inspectorate is now restored to independence from the HSE.

9.2 In the longer term it has been suggested that the Inspectorate be merged with the Regulator's office or the SRA. The need to retain independence from the industry should preclude merger with the SRA. The option of a merger of the railway Inspectorate and the Regulator's office, on the model of the Civil Aviation Authority which regulates economics and safety in aviation, is a possibility, but we are not convinced that the model is right for rail and we note that it is not favoured by the Regulator.

9.3 A far better option is offered by the once-promised Transport Safety Authority of a few years ago. This would be modelled on the American National Transportation safety Board, and cover safety in all modes of transport. It would encompass existing agencies such as the air, maritime and rail accident investigation branches, the Railway Inspectorate and perhaps elements of the Civil Aviation Authority and/or the Traffic Commissioners. This would not only enable

a realistic approach to be taken to balancing safety against cost, but also bring some sanity to the approaches to safety among different modes of transport. No longer would rail be urged to become ever safer at prohibitive cost while business is constantly lost or priced off to less safe modes. We recognise that this would need legislation, but we see this as an absolutely essential and urgent reform. It is a great pity it was omitted from the 2000 legislation. That omission should be rectified forthwith.

10 Regulatory bodies: The Commission for Integrated Transport

10.1 Before leaving regulatory bodies, mention must be made of another key player – the Commission for Integrated Transport. This body is one of the most valuable innovations of the 1997-2001 government. It is the only trans-modal body created during that period. Some had called for the creation of a Strategic Transport Authority. We did not subscribe to this view, fearing that such a body would be unwieldy and reminiscent of the postwar British Transport Commission. The essential multi-modal overview is provided by the CfIT, and that is as it should be. There have been suggestions that the Commission might be reduced in its role or even abolished. We would strongly oppose this, and indeed see a case for strengthening it and widening its role. It is perhaps regrettable that the job of monitoring the Ten-Year Plan reverted to Government (seemingly by common consent), as this smacks a little of the government "marking their own homework". Be that as it may, there is plenty of scope for the Commission to promote integrated transport and interchange facilities at local level, by urging local (and in time regional) transport authorities to follow examples of best practice elsewhere. It may well be that there is a role for the CfIT and/or the Regulator to take over regulation of the bus industry from the Office of Fair Trading, thereby giving integration priority over competition in the bus industry. Like the HSE, the OFT has failed to adapt their preconceived ideas to the practical requirements of transport systems. It must always be remembered that the real competition for any form of public transport comes from the private car.

11 Rolling stock companies (ROSCOs)

11.1 As many of the other elements of the alphabet soup created in 1994 are reviewed, merged, taken back in-house or abolished, the one element that has been left alone quietly making money is the ROSCOs. Indeed they have been making some very large profits from leasing charges, little of which has been reinvested in the railway industry.

This contrasts with profitable Train Operating Companies, which have to make franchise payments to the SRA and these are in principle at least available for investment in the network. But profits from leasing are lost to the industry, and leasing charges, unlike access charges, are wholly unregulated (on the theory that competition between the three ROSCOs will keep them down) and of course are reflected in franchise subsidy demands which come ultimately from the public purse.

If these profits had been devoted say to speculative rolling stock construction, this might matter less, but by and large this has not happened. We therefore feel that in order to ensure that public subsidy does not feed unreasonable private profit and that subsidy to the railways is spent on the railways, roll-

ing stock leasing charges ought to come within the remit of the Rail Regulator. Lower leasing costs would in turn be reflected in lower franchising costs and thus in more cost-effective use of public funding on the railways. We recognise that this is likely to require legislation.

12 Access charges

12.1 A related point which should be considered if vertical integration is not pursued, is the possibility of paying more of the government support direct to Network Rail rather than through the current "money go round" of franchise support payments to TOCs and access charges from them to Network Rail. This would not only enable access charges to be reduced and thus encourage less profitable services, but it would also bring the railways more into line with roads, where the infrastructure is provided by government, and operations left to the private sector. Another possibility is relating access charges more closely to revenue, which would give Network Rail a more direct link to the real customers. If vertical (or virtual) integration goes ahead, access charges become academic for most passenger operators but remain relevant to open access operators and to freight operators.

13 Cost control

13.1 Everyone with any interest in the railway industry is painfully aware that the curse of cost escalation is currently undermining virtually any attempt to make even modest improvements to the network. No progress in developing the system to accommodate growing demand is going to be possible until this problem is solved.

In this context we note an excellent study undertaken recently by Roger Ford for Transport 2000 on Rising Costs of Britain's Railways. We commend this study, and quote his conclusion that current spending is buying perhaps a third of the value that one might expect, based on historic trends and comparable overseas experience.

In particular, mainline maintenance and renewal is costing more than three times the European average and twice the highest figure on mainland Europe. Ford identifies Hatfield as the turning point at which this trend took off exponentially. Whilst he is not specific as to causes, he does mention fragmentation, "margins on margins", subcontracting chains, safety legislation, the regulatory environment, and bureaucracy in general, much of it dating from privatisation.

13.2 We have already referred to two areas which need to be addressed with legislation, which would begin to deal with some of the causes of cost escalation: the HSE/HMRI relationship, and leasing charges. Other areas are not hard to find. For exam-

ple, the Treasury requires an allowance to be made in all cost-benefit analyses, which it refers to as "optimism bias". This is in effect an allowance for errors in forecasting factors on both sides of the equation. But in recent years, based on our experience on the West Coast Main Line upgrade, a figure of 30% is now required. This is notwithstanding that many earlier rail schemes, including line and station reopenings, have turned out far more successful than forecast. With a handicap of this size, it is a wonder that anything ever gets approved.

Clearly there is something of a vicious circle here, in that until better results can again be demonstrated, the Treasury are unlikely to relent, but until schemes are approved the opportunity to demonstrate progress will be denied. The Department needs to tackle the Treasury on this issue.

13.3 Another cause of cost escalation can be traced to insurance costs. These days the private sector is even more risk averse than government it seems, and insurance costs are escalating in all fields fuelled by the increasingly litigious "blame culture" that is now prevalent and seems to have been given added impetus by the high-profile rail accidents of recent years.

Undoubtedly fragmentation, combined with chains of subcontracting, has exacerbated this problem in the rail industry, as each player is obliged to secure his own cover on the open market.

This contrasts starkly with the pre-privatisation situation where British Rail were their own insurers, accepting all risks corporately themselves. Clearly this was an extremely efficient arrangement financially. Now the process of reintegration and taking functions back in-house will no doubt reduce this problem somewhat, but it will come nowhere near restoring the pre-1994 situation. We propose that Government should open discussions with the insurance industry, the SRA and all other key players, with a view to determining how best this situation can be improved and insurance arranged on a joint industry-wide basis as economically as possible.

Even if it is not possible to restore the pre-1994 situation in the absence of an

integrated industry, it ought to be possible to replicate the sort of arrangement whereby anyone hiring a car pays the rental company a charge to cover his share of the company's insurance cover.

14 Summary of recommendations

14.1 To conclude, our "dream scenario" might look something like this: First, deal with the urgent issues of the Railway Inspectorate and ROSCOs, even if this requires legislation to set up a Transport Safety Authority and regulate leasing charges. Second, tackle some of the root causes of cost escalation by opening discussions with the Treasury on Treasury rules and with the insurance industry on insurance options. Third, encourage the continuing process of reintegration not only on the infrastructure side but also on the operational side, for example with larger franchises. At the same time the future or otherwise of franchising should be examined, more franchises taken back in-house and vertical reintegration encouraged, starting with some trial areas. Ideally this could lead to the gradual ending of franchising, combined with a return to vertical integration on a mainly regional basis, and in due course the merger of the SRA and Network Rail, to re-establish in effect a not-for dividend BR, not fully state-owned but reintegrated, at arms length from government and regionally organised in parallel with Regional Transport Authorities with PTE-type powers. Freight and some others might remain separate "open access" operations with safeguards. The railways will never be free of the need for state financial support, but they must be efficient and should have as much independence as possible.

Mike Crowhurst
chairman

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