



House of Commons
Transport Committee

The Future of the Railway

Seventh Report of Session 2003–04

Volume I



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Report, together with formal minutes

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The Transport Committee

The Transport Committee is appointed by the House of Commons to examine the expenditure, administration, and policy of the Department for Transport and its associated public bodies.

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Summary

Our deep concerns about the spiralling costs and poor performance of railways in Great Britain led us to announce an inquiry into the future of the railway last year. We received a strong response which raised a large number of further fundamental issues, including the effect on railway regulation, performance and growth of the industry's present highly fragmented state. Our report addresses this, and identifies extremely serious systemic flaws in the present organisation of the railway.

The main problems we uncovered were:

- The Rail Regulator is solely responsible for determining the amount of funding Network Rail receives. His decision is binding upon the Government. In addition, although Network Rail is a private company it requires to be guaranteed by the Government. However, as a private company it is denied access to the cheapest forms of Government loans. Consequently, Network Rail's borrowing is more expensive than if it were in the public sector.
- The Rail Regulator has prescribed the level of maintenance and renewals funding that Network Rail requires to undertake over the next five years from April, thereby duplicating the work of the company's management. The present regulatory arrangements did not prevent the disaster of Railtrack; and in a number of important respects, such as Network Rail's asset control, they have not performed well. Costs have still not been brought under control.
- Network Rail's ownership structure is unacceptably weak, and its ability to forecast accurately future funding requirements has been demonstrably poor.
- The Strategic Rail Authority (SRA) is expected to set targets, determine outputs, grow and lead the industry as a whole, yet it has no control over the infrastructure which largely determines overall rail performance. There is therefore a serious mismatch between the SRA's objectives, powers and responsibilities.
- The regulation of rail safety is undertaken by the Health and Safety Executive. We found that the industry believes that the HSE has failed to take fully into account the industry's present record when assessing risk; that this may have led to higher safety costs than necessary; and that, as a consequence, the HSE has lost the trust of the industry.

We have concluded that the industry is not fit for purpose, and that if these major problems are to be solved, the railway's present inability to deliver key projects effectively corrected, and its focus on excellent service delivery to the travelling public strengthened, as it must be, a fundamental reorganisation of the railway is required. While reorganisation will entail disruption, the railway is unlikely to perform significantly better unless the existing bodies are replaced.

Our main recommendations are:

- A public sector Railway Agency is needed. This new executive body would combine the strategy and output delivery functions of the SRA with control of the infrastructure, and must be given all the powers required to manage the entire rail system and to deliver excellent services for the travelling public. Combining these functions will permit the body responsible for growth and targets also to manage the means of achieving improvements, and to receive funding at the cheapest level. However, this body must demonstrate a much greater creativity and vigour than its predecessors if these new arrangements are to have a chance of working. The travelling public do not care who runs railway services; their concern, quite properly, is with efficiency and value for money. While the private sector may therefore continue to provide some train and infrastructure services, where that clearly provides the best option, the Government needs to keep an open mind on the provision of these services directly by the public sector.
- Economic regulation of the railway, as presently organised, has largely failed. However, if the private sector continues to be involved, there will be a role in future for a measure of independent economic regulation to 'hold the ring' between the infrastructure provider and the private sector companies. But the Government must take back into its own hands decisions about the sums which will be spent on the railway. This will correct the present absurd position in which the Government simply underwrites the Regulator's funding decisions. Economic regulation should be removed from functions which are properly those of Government.
- All parts of the industry and the safety regulator need to work co-operatively to provide a progressively safer, effective and efficient environment for those who work on, and travel by, rail. Our evidence suggested strongly that the HSE's relationships with important parts of the industry have broken down. In these circumstances, there cannot be full public confidence in the present regulatory arrangements for rail safety. Consideration should be given, therefore, to removing the regulation of rail safety from the HSE, and for Her Majesty's Railway Inspectorate either to be made a free standing Agency of the Department for Transport or merged with the new Railway Agency.

Demand for rail is strong, and it is impossible to imagine that the railway will not continue to be required. It is essential, therefore, that costs are controlled and performance improves. In January the Government announced a review of the structure of the railway. We welcome this review. A new beginning for the railway is needed. The mistakes and 'drift' of the last ten years need to be corrected. We do not underestimate the size of this task. We have mapped out in this report what steps for organisational change will be required to assure the future of the railway. We hope that the Government will accept the real challenges of railway restructuring.

1 Introduction

1. The rail industry is at a critical point of its development. Since our predecessor Committee's report in 2002 on the structure of the rail industry¹ a new private rail infrastructure provider, Network Rail, has replaced Railtrack. In December, the Rail Regulator determined the sums of money he considers the company will require for 5 years from April 2004.² In April 2003, the Rail Safety and Standards Board (RSSB) replaced Railway Safety as the rail industry's lead body on safety and standards matters. The Government's Spending Review decisions in the summer will determine industry funding to 2008.³

2. As part of our remit to monitor the performance of the Department for Transport and its associated public bodies, we took evidence last session from leading figures in the industry including the Rail Regulator and the Chairman and Chief Executive of the Strategic Rail Authority (SRA).⁴ That preliminary work left us sufficiently concerned over the state of the industry to announce in July 2003 an inquiry into the "future of the railway".

3. **The Government and Mr Bowker, Chief Executive and Chairman of the SRA, assured us that the structure of the industry was not going to be changed, and that the industry's focus should be on making the existing arrangements work properly. Nevertheless, we felt it was important to look at fundamental issues. To this end, we posed four questions:**

is rail an outmoded form of transport?

is the present network the right one, and if not, will it have to be changed?

what sort of traffic is the network best used for?

how does our network compare with other railways and what lessons can we learn from other countries?

4. These simple questions provoked evidence raising a number of fundamental issues, including the role of the Rail Regulator, the capacity of the SRA to lead the industry, its relationship with the Government, the Government's capacity to direct the policy of rail in the current structure; and the effectiveness of Network Rail. **The constant theme throughout our work was the complaint that the current structure of the industry is too**

1 Transport, Local Government and the Regions Committee, First Report of Session 2001-02, *Passenger Rail Franchising and the Future of Railway Infrastructure*, HC 239-I

2 The sum is determined by the Rail Regulator after an *access charges review*, also called a *periodic review*. This is the process in which the Regulator determines the income which the infrastructure operator – now Network Rail; Railtrack prior to 2002 - needs to earn mainly from train operators in the form of *track access charges*, and from certain other sources. Mr Winsor announced the access charges review which concluded in December 2003, in 2002. Further details may be obtained from the website of the Office of the Rail Regulator (ORR)

3 HC Deb 19 January 2004, col 1076

4 We produced two rail related reports in the last Session, Transport Committee, Fourth Report of Session 2002-03, *Railways in the North of England*, HC 782-I; and, Seventh Report of Session 2002-03, *Overcrowding on Public Transport*, HC 201-I. These reports, and in particular HC 239-I, are highly relevant to this work, and our present conclusions should be read in conjunction with them.

fragmented to provide clear lines of responsibility and leadership and a satisfactory basis for improved rail performance.

5. The Secretary of State's *Directions and Guidance* to the SRA make clear that rail privatisation was "seriously flawed" in "many respects";⁵ and that "The Authority will...need to address the problems caused by fragmentation of the railway industry's structure...". Our predecessor Committee highlighted the dangers of fragmentation in 2002, when it warned starkly that:

"The fragmentation brought about by privatisation contributed to the chaos and delay that paralysed the industry. It is essential that fragmentation is significantly reduced."⁶

6. Mr Bowker has sought to achieve a measure of industry co-ordination through regional "joint boards" involving Network Rail, the SRA and the train operating companies.⁷ We also heard about the so-called "Group of 6" key industry leaders who have met regularly since 2002.⁸ However, there is no evidence that this effort of co-operation is mitigating industry fragmentation, or improving service performance.

7. We have seen no evidence, since our predecessors reported two years ago, that fragmentation in the rail industry has reduced. Indeed, our evidence has suggested that it is getting worse. In addition, industry costs are increasing; performance remains in the doldrums; and the SRA appears utterly incapable of managing significant improvements. The evidence of the Rail Regulator's Interim Review of track access charges is that the Regulator and the SRA are not co-operating well.

8. The evidence of Dr Dieter Helm, Fellow in Economics, New College, Oxford, illustrates the appalling extent of the present confusion of responsibilities in the railway:

"the Department for Transport's role is subsidiary to that of the Treasury and spending review, leaving the status of the 10 Year Plan ambiguous;

the SRA's role depends on the Department for Transport's priorities, and the guidance provided to it;

the SRA's budget is notionally outside the main government borrowing calculations, but in reality is determined by the Treasury;

the Rail Regulator decides the track access charges which, in practice, are paid by the SRA at the margin;

thus, the Rail Regulator determined how much money the SRA pays Network Rail and the TOCs [train operating companies], and therefore how much money the Treasury pays the SRA via the Department for Transport;

5 *Directions and Guidance*, para 5.3

6 HC 239-I, para 53

7 Q 247

8 SRA, Rail Regulator, HSE, Network Rail, and representatives of the train operating and freight operating train companies, *SRA Strategic Plan 2003*, p 21. Engineering contractors and rolling stock manufacturers are not represented.

the outputs are, however, determined by the SRA, which effectively carries out the capital planning function (which Railtrack previously did);

Network Rail therefore is largely responsible for the operations of the railways, and the SRA for its capital development, confusing the roles of management and responsibility;

the Rail Regulator and the SRA have a concordat which cements this confusion of roles between them.

As a result, it is not surprising that there are often sharp differences of opinion between all the main parties: the Treasury, the Department for Transport, the SRA, the ORR and Network Rail. Tom Winsor, Rail Regulator, sees himself as the ‘referee’, but one who has to take into account the aims of the SRA, and whose decisions ultimately determine public expenditure on the railways.”⁹

However, even this picture does not represent the extent of the confusion, and lack of co-ordination between the main bodies, which we found.

9. It became clear that, as the railway system is currently governed, there is no one organisation capable of properly addressing the four questions with which we started. In our view, until there is a single body with the authority to deal with these questions, Government and the rail industry are condemned to spending energy debating structural issues rather than getting on and running the railway for the benefit of the travelling public and the country. This report addresses the fundamental questions: who does, and who should, run the railway?

The Government’s Failure

10. Much of this report analyses in detail the flaws in the main pillars of railway governance: the SRA, Rail Regulator and Network Rail. However, responsibility for the railway rests ultimately with the Government. It has had six years to construct a policy and structure for the railway that works well, but our report shows that it has failed to do so.

11. The first missed opportunity was when the SRA was established by the Transport Act 2000. The purpose of the SRA, set out in the Government’s White Paper in July 1998, was to provide a “clear, coherent and strategic programme for the development of our railways.”¹⁰ The SRA has not come close to achieving this, as we demonstrate later in this report.

12. The failure to address properly the effects of the establishment of the SRA on the Rail Regulator is a further, serious, example of Government policy failure. The SRA and the Rail Regulator were left with overlapping duties and powers which later led to a struggle to determine which of them ran the railway. In addition, the Rail Regulator is independent of the Government in regulating Network Rail but is also under a duty to “have regard” to the budget of the SRA in setting Network Rail’s funding levels. He must also have regard to

9 FOR 94

10 Department of the Environment, Transport and the Regions, *A New Deal For Transport: Better For Everyone*, Cm 3950, July 1998, p 94

guidance from the Secretary of State, a policy stressed in the Government's 1998 White Paper.¹¹ It is no wonder that in a recent publication explaining the difficulties of reconciling these and other duties he said that "the Regulator's duties do not always point in the same direction and may conflict".¹² The Government appears to have assumed that the Regulator's duty to have regard to guidance would ensure that the Regulator considered the financial needs of the railway in the overriding context of Government and SRA policy and budgets. This has not happened.

13. The collapse of Railtrack gave the Government a further opportunity to address these problems. Instead, it added another fudge by creating Network Rail, a private company without any private sector disciplines, seemingly set up simply to keep the enormous costs of the railway infrastructure away from the Government's balance sheet. In addition, we have found that the Health and Safety Executive is regulating railway safety without full regard for the improving safety record of the industry or its ability to fund improvements. The result is that spending in this area is a major contribution to soaring costs but with progressively less safety gain.

14. Directly or indirectly, the effects of this failure of Government rail policy are evident in the huge rise in costs of the industry since 1990. In 2002, 6% of passenger kilometres were made by train in Great Britain; rail represented 47% of public passenger travel excluding cars, vans, and taxis; and approximately one third of total planned (public and private) expenditure on transport in the period 2001/02 to 2010/11 – £64.9 billion out of £181.9 billion – is allocated to the railway in the Government's Ten Year Plan.¹³ The taxpayer is making a very substantial investment in the railway and it is therefore essential that the railway provides excellent value for money not only to the fare payer, but as importantly for the tax payer. Roger Ford provided the Committee with the following information:¹⁴

11 Ibid, p 97

12 *ORR Interim Review of Track Access Charges: Draft Conclusions*, p 10

13 *Transport Statistics 2003*, pp 14, 25; and Specialist Advisor

14 FOR 88

Table 1

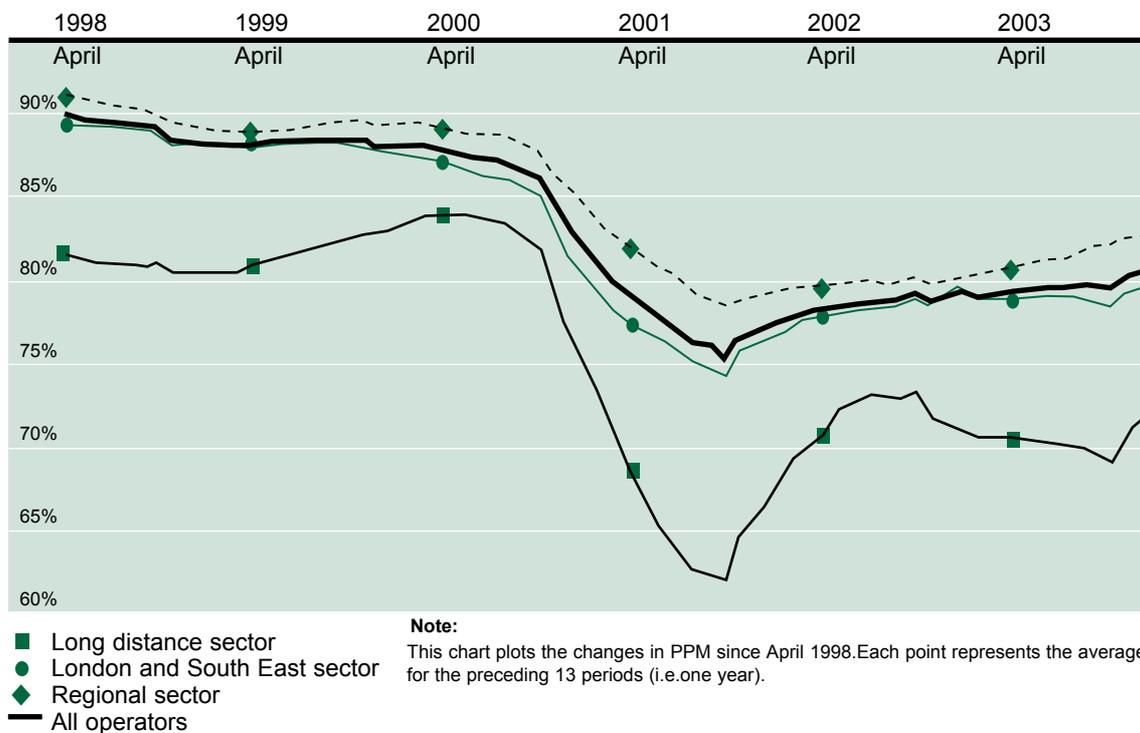
	Industry wide operating spend and revenue pressures 1989/90, 1999/00 & 2002/03 (2003 prices) (£m)			
		1989/90	1999/00	2002/03
Infrastructure OMR (1)		1856	2800	5000
Franchised train operation (2)			2800	3600
Freight train provision			500	400
Total train provision		3182	3300	4000
Underlying spend		5038	6100	9000
Passenger and freight revenue		4942	4400	4800
Network Rail open access/rental			100	200
Total revenue		4942	4500	5000
Public sector support		889	1400	2500
Total income		5832	5900	7500
Surplus/deficit			-200	-1500

(1) Includes joint industry costs (2) Includes rolling stock leases but not track access charges

In addition, as the graph below demonstrates, the performance of the industry has become highly unsatisfactory over exactly the period when Mr Ford calculates that the industry operating spend was in deficit:

Chart 1

Public Performance Measure: moving annual average percentage of trains arriving on time 1998/9-2003/4



Source: SRA, *National Rail Trends, 2003-2004 quarter three, Table 2.1 Public Performance Measure*

15. As public sector support for the railway has tripled, underlying spend has doubled and revenue has remained static; while the SRA's graph reveals the industry's inability to sustain and improve its performance. The taxpayer has paid progressively more in this period for a declining service. Mr Ford points out that the enormous increase in the cost of the railway places its future in grave serious doubt.¹⁵ **It is essential that costs are brought under control for the future of the railway.** Professor Roderick Smith of Imperial College gave evidence to us that the cost of one entirely new railway system was in the range £11 – 27 billion.¹⁶ The sums which have been used ineffectively by the Government's railway structure in propping up the present, poorly performing system, could have paid for a large proportion of a new railway network.

16. The enormous public sector costs of the industry have been camouflaged. Network Rail's borrowing appears in the UK National Accounts as private sector borrowing owing to its classification there as a private non-financial corporation even though the Government, through the SRA, guarantees much of the company's borrowing. While the Comptroller and Auditor General has concluded that Network Rail should be accounted a subsidiary of the SRA, the National Statistician, relying on accounting advice from the Department for Transport, considered the present classification of the company was

¹⁵ Ibid

¹⁶ Professor Roderick A. Smith, "High-speed Railways for the UK", *The Utilities Journal*, April 2003, pp 36-38

satisfactory.¹⁷ This means that the Government does not have to account for the enormous debts of Network Rail - which we detail later in this report - despite guaranteeing them.

17. **The damaging consequences of these and other failures for the sound regulation and governance of the railway are the subject of the remainder of this report. However, the fundamental failure of the railway is one of Government policy. The Government has not been able to exert control on the extra costs of the railway system, identify clearly the root causes of the extra costs, nor has it after two attempts produced a governance structure that has clear lines of accountability for public money and ensures appropriate transfer of risk to the private sector.**

18. **It is vital that the recent surge in costs for the railway is checked. The Government has told us that it is in control of the industry. But the swelling subsidy figures of recent years tell the real story of an industry that is out of effective control. The siren song of the SRA is that a “gradualist”, evolutionary approach based on intra-industry co-operation will enable costs to be reduced and performance to improve. Others we heard from were in favour of restructuring. We publish the evidence of both with this report. Relying on incremental improvements may take many years to produce results; ill judged restructuring will damage the industry further. However the Government chooses to reverse the present position of the railway, it will be essential that in future it ensures proper control over the money it provides. The Government must ensure that the private sector assumes real risk where it is involved in providing railway services in future. The Government also needs to ensure that the funding of the railway is properly integrated with other transport modes. The Government has the responsibility to sort out the current mess; it needs to make sure that it has the powers required to do so, and that the powers and responsibilities of all the bodies involved in the railway industry are appropriately structured.**

Secretary of State for Transport’s statement of 19 January 2004

19. We were heartened that as our inquiry was in its final stage, the Secretary of State for Transport announced on 19 January 2004 an immediate review of the structure of the rail industry with “fundamental reform” in mind.¹⁸ In a striking departure of tone and approach, Mr Darling referred to a fragmented, excessively complicated and dysfunctional industry with “too many organisations, some with overlapping responsibilities”.¹⁹

20. The Government’s proposed examination of the industry structure represents a welcome, if belated, reversal of its position as set out by the Secretary of State as recently as 10 September 2003 when he told us that he was “loathe to start spending overmuch time on structural changes when I really want everybody in the industry to concentrate on delivery”²⁰ and that “It is not so much the structures that are important; it is making sure that you have got the right relationships...”.²¹ **We are delighted that the Secretary of**

17 Treasury Committee, First Report of Session 2002-03, *National Statistics: The Classification of Network Rail*, HC 154, para 9

18 HC Deb 19 January 2004, col 1077

19 Ibid

20 Transport Committee, Second Report of Session 2003-04, *The Departmental Annual Report 2003*, HC 249, Ev 9

21 HC (2003-04) 249, Ev 17

State has changed his mind over the four months since he gave evidence to us and has also decided to review the structure of the railway.

21. In the course of this inquiry we received 126 memoranda from individuals and organisations and held five evidence sessions from October 2003 to January 2004, in addition to evidence sessions dealing with rail related issues. The volume of the evidence we received demonstrates the extremely high degree of current concern about the railways, and confirms our original view of the timeliness of this work.

22. Evidence was taken from Dr Kim Howells, Minister of Transport, Mr Richard Bowker, Chairman and Chief Executive of the Strategic Rail Authority (SRA), Mr Tom Winsor, Rail Regulator, Mr Len Porter, Chief Executive of the Rail Safety and Standards Board (RSSB), Mr Alan Osborne, Dr Allan Sefton, Director of Rail Safety, Health and Safety Executive (HSE), Mr Ian McAllister, Chairman, Network Rail, Mr John Armit, Chief Executive, Network Rail, Mr Stewart Francis, Rail Passengers Council (RPC), Mr Christopher Garnett, Association of Train Operating Companies (ATOC) and Chief Executive, GNER, Mr Olivier Brousse, Chief Executive, Connex South Eastern, Mr Mark Beckett, Business Development Director, Chiltern Railways, Mr Patrick Verwer, Managing Director, Merseyrail Electrics, Mr Roy Wicks, Director-General, South Yorkshire PTE, Mr Neil Scales, Director-General Merseytravel, Mr Robert Crow, General Secretary, National Union of Rail, Maritime, and Transport Workers, Richard Rosser, General Secretary of the Transport Salaried Staffs' Association, Mr Mick Rix, Associated Society of Locomotive Engineers, Mr David Clarke, Strategy Director, Jarvis Rail, Mr Colin Carr, Engineering Director, Amey Rail, Mr Andrew Rose, Chief Operating Officer, Balfour Beatty Rail, Dr Keith Lloyd, Representative of Alstom Transport UK, Mr Per Staehr, Chief Country Representative, Bombardier Transport UK Ltd, Mr Anton Valk, Managing Director, NedRailways B.V., Mr Gerlof Den Buurman, Project Manager, ProRail, Mr Shaun Markham, English Nature, Mr Michael Hughes, Chairman, Railfreight Interchange Investment Group, Ms Philippa Edmonds, Freight on Rail, Mr Stephen Joseph, Executive Director, Transport 2000, Mr Robert Goundry, Director of Strategy, Freightliner Group, Mr Neil McNicholas, Managing Director, Direct Rail Services, Mr Michael Schabas, Director, GB Railfreight, Mr Graham Smith, Planning Director, English Welsh and Scottish Railway, Mr Paul Wright, Head of Logistics, ASDA-Walmart, Mr Allan Leighton, Chairman, Royal Mail, Professor Sir Frederick Holliday, Professor Roderick Smith, Imperial College, London, Professor Chris Nash, Institute for Transport Studies, University of Leeds, and Rail Research UK, Professor Mark Casson, University of Reading, Professor Stephen Glaister, Imperial College, London, Professor David Newbery, University of Cambridge, Dr Tim Leunig, London School of Economics, Mr Jonathan Tyler, Principal, Passenger Transport Networks. We are grateful to these witnesses and all those who contributed to our inquiry.

23. A Clerk and the Specialist Advisor made a brief study trip to the headquarters of NedRailways B.V., a subsidiary of Nederlandse Spoorwegen, in Utrecht. We are grateful

for the highly informative briefing they received there.²² We wish to thank Dr Terry Gourvish, Director of the Business History Unit of the London School of Economics, our Specialist Advisor.

24. Regulation of the Railway is undertaken by three bodies: the Rail Regulator, the Strategic Rail Authority, and the Health and Safety Executive. The railway infrastructure is owned and run by Network Rail, a private company. In the following chapters we examine the roles of these bodies to highlight operational inadequacies in each, and their chronically poor co-ordination, which are rooted in the present deeply flawed structure of the industry.

22 Dr John Patterson, Clerk, and Dr Terry Gourvish, Specialist Advisor, visited the headquarters of NedRailways in Utrecht on 25 and 26 November 2003. Their study programme extended over one full day and a quarter and covered the following aspects of the Dutch railway and transport structure: transport integration, electronic ticketing and gateing, staff training centre, long term vision, timetabling, rolling stock and maintenance, company culture change, regulatory and industry structure, human resources policy, aggression training centre, station visit – Den Bosch.

2 Rail Regulator

25. The Rail Regulator, who leads the Office of the Rail Regulator (ORR), was established by the Railways Act 1993 to provide for economic regulation of the monopoly and dominant elements of the rail industry. The Regulator enforces the terms of the network licence of Network Rail, the owner of the national rail network; sets the company's contractual and financial framework; approves agreements between the company and train operators; and, in particular, determines the track access charges levied by Network Rail on users of the railway infrastructure, effectively deciding upon major industry costs. The Regulator is independent of Government though he receives general guidance from the Secretary of State under section 4(5)(a) of the Railways Act 1993 as amended by section 224 of the Transport Act 2000.²³ Mr Tom Winsor, the current Rail Regulator, will be replaced by the Office of Rail Regulation in July 2004.²⁴

26. The Rail Regulator was initially intended to hold the ring between the Government, the private sector infrastructure provider, and private sector operating companies.²⁵ However, changes in the structure of the industry mean that the Regulator is no longer determining the relationship between conventional private sector bodies, since Railtrack has been replaced by Network Rail which, though a private company, has no shareholders and is funded wholly by debt. The introduction of the SRA produced a significant new complication, which was recognised by a "Concordat" drawn up between the two organisations, designed to clarify their respective responsibilities.²⁶

27. In the remainder of this chapter we briefly summarise four key problems with the Regulator's present functions; in Chapter 3 we explore some effects of economic regulation on Network Rail.

28. It is unfortunate that the Regulator has chosen not to reply to our letter of 10 December 2003 where he was asked a number of important questions including: why he thought the railway was excessively fragmented; how his incentive regime for Network Rail would work; and his projections for Network Rail's profitability. His failure to respond, despite prompting, has prevented us from gaining as complete a picture of his view of these matters as we would have liked.

Asset register – indicator of regulatory failure

29. In its 2001 report, *Rail Investment: Renewal, Maintenance and Development of the National Rail Network*,²⁷ the Environment, Transport and Regional Affairs Committee considered that the regulatory regime set up at rail privatisation had failed, in the

23 The Secretary of State issued *Guidance to the Rail Regulator* on 26 September 2002. The Guidance includes, the context in which the Regulator works, his relations with the HSE and the SRA, the requirement for the Regulator to work to a 'common agenda' with the other railway regulators, and to have regard to the SRA's policies and budget. The Guidance may be found on the website of the Office of the Rail Regulator.

24 For 77B

25 The present main functions of the Rail Regulator are described in the letter from David Rowlands, Permanent Secretary of the Department for Transport to Tom Winsor, 16 December 2003, FOR 99B and FOR 77A. Full details of the Rail Regulator's functions may be found on the website of the Office of the Rail Regulator.

26 *Concordat Between the Strategic Rail Authority and the Office of the Rail Regulator*, 25 February 2002

27 HC 18-I

context of a growing railway, to ensure that the infrastructure operator had delivered what was required of it by train operators, passengers and the wider public.²⁸ A similar complaint was made by our predecessor Committee in 2002.²⁹ Mr Winsor's subsequent regime has been no more successful in ensuring that the infrastructure operator has complete knowledge of its assets. When Mr Coucher, Deputy Chief Executive of Network Rail, saw us in June 2003, MIMS (Maintenance Information Management System), a key part of the company's Asset register, was due for completion in "late summer" 2003;³⁰ in October the Rail Regulator told us that full completion was due "by 31 January 2004".³¹ In January 2004 Network Rail told us MIMS was to be "reliant across the network" by March 2004.³²

30. However, MIMS is only a part of Network Rail's Asset register databases. In October Mr Winsor told us those were 80% complete. Two years have passed since he had made their compilation a licence condition in April 2001. **Network Rail has now indicated that 'a baseline asset register providing an inventory of the assets and their key attributes' will not be ready until mid-2005.**³³

31. **It is utterly astonishing to learn that Network Rail's Asset register, a fundamental management tool, will now be available only in 2005, four years after a Select Committee of this House drew attention to its absence. The Regulator has clearly failed to ensure that first Railtrack and now Network Rail, have produced information needed to assess performance of the system. This is not an academic exercise. If the state of the infrastructure is not thoroughly known then reliable decisions about the levels of maintenance and renewals are simply not possible and the basis of the Regulator's *Interim Review* is placed in doubt. This episode demonstrates graphically how the Regulator has failed in his core function of effectively regulating the "stewardship of the national rail network".**³⁴

Regulation and investment

32. A key part of the stated "Aim" of the Office of the Rail Regulator is to:

"...facilitate investment in capacity to satisfy the demands of growth in passenger and freight traffic at the time it is needed."³⁵

The Regulator clearly failed to achieve this when Railtrack, a private company with shareholders, was the infrastructure provider. It is not clear that he has been any more successful in the new structure.³⁶

28 HC 18-I, para 32

29 HC 239-I, para 52

30 Q25

31 Q1290

32 FOR 57B

33 Ibid

34 *Guidance to the Rail Regulator*, 26 September 2002

35 *ORR Business Plan 2003-2004*, p 5

36 'More than 70% of City analysts believe rail regulator Tom Winsor has failed to bring clarity to investors in the industry, a survey commissioned by the Strategic Rail Authority has found.' in, 'Results of survey leave rail regulator steaming', *The Daily Telegraph*, 16th March 2004

33. Mr Winsor has stated his belief that “independent economic regulation is necessary if you are going to have private investment in the railway.”³⁷ In addition to attracting private investment, the Regulator sees his role as protecting it:

“There is only one Network Rail. Therefore, train operators, passenger and freight, and those who stand behind them and invest in them need to know that Network Rail will not be permitted to abuse its monopoly.... The industry also needs to know that the finances of the industry will not be arbitrarily altered by political intervention.”³⁸

34. We asked Mr Winsor to quantify the investment that has been made in the railway industry as a result of his function. We were astonished that, despite his bold claims, all he offered to us by way of reply was that “It is extremely difficult to do that.”³⁹

35. Mr Winsor's defence of regulation fails to address the shift of emphasis away from the original vision of a privatised railway in which private sector franchisees would have significant freedom to extend and enhance their service, and to take commercial risks, to the present, highly subsidised and much more strictly delineated franchises. It does not take full account of the SRA's role as a significant industry ‘customer’ whose requirements may conflict with those of the Regulator. Nor does it take account of the fact that although the infrastructure provider is technically a private company, it has no shareholders and its debt funding is effectively guaranteed by the Government.

36. The Government has made clear its role in guaranteeing investment, as in the case of the securitisation to refinance Network Rail's short to medium term borrowing.⁴⁰ Mr Darling said in a recent answer to a written parliamentary question in the House of Commons:

“Railways are essential to the economy of Britain. Whatever the institutional structure, the Government will need to be at least as closely involved as it currently is in expenditure decisions and in making financial commitments to the industry and those who finance it; so that lenders to the industry enjoy at least the same strength of financial support from the government as they do today.”⁴¹

It is the Government, not the Rail Regulator, which guarantees private investment in the railway.

Conflict of responsibilities – who runs the infrastructure?

37. Mr Winsor has been conducting an interim review of passenger track access charges which will provide Network Rail with a proportion of its funding for 5 years from April 2004. The funding allowed by the Rail Regulator was £22.2 billion,⁴² an increase of £7.2

37 Q1253

38 Q1263

39 Q1262

40 FOR 77B

41 HC Deb, 9 February 2004, cols 1237-1238W

42 *ORR Access Charges Review 2003: Final Conclusions*, 12 December 2003, p 6

billion over the settlement made in 2000.⁴³ Mr Winsor calculates that train operating companies will pay £18.892 billion in track access charges over the same period.⁴⁴

38. Mr Winsor is prepared to seek the detailed outputs he wants. For example, when announcing his final conclusions on the Review on 12 December he put forward significant changes to the terms of the West Coast Main Line (WCML) upgrade project:

“Substantial savings, amounting to 22% of the estimates made by Network Rail in September 2003, can be achieved by extending the timescale for delivering certain other elements of the project which will provide a greater certainty of those outputs being delivered on time and on budget.”⁴⁵

We explore the WCML project in more detail in Chapter 4.

39. The SRA responded sharply to what it saw as an attack on its WCML enhancement strategy,⁴⁶ while Mr John Armitt, Chief Executive of Network Rail, told us:

“The Rail Regulator decides the *broad* costs that he expects to be initially required by an efficient rail maintenance organisation for renewals and maintenance. *In terms of where we spend it that is our decision at the end of the day* (emphasis added).”⁴⁷

On 7 January he repeated:

“At the end of the day, we have to decide how to spend and where to spend the £22.2 billion.”⁴⁸

40. But there is nothing “broad brush” about the Review’s conclusions. Funding is parcelled by activity heading on an annual basis reflecting the nature of the railway operations, maintenance and renewals work the Regulator has concluded is required.⁴⁹ The Regulator’s Review findings give a clear blueprint for operational, maintenance and renewals activity on the national rail network over the next 5 years. In a Press Release, the ORR stated “Network Rail is now equipped with a *very clear specification* of how much money it is entitled to receive, what it must do for that money and where the necessary outputs are to be delivered (emphasis added).”⁵⁰

41. The Regulator, Network Rail and the SRA clearly differ about who exactly runs the railway infrastructure in the UK. Although we understand the need for a measure of regulation to prevent a monopoly company abusing its position, the Regulator is not the customer, and should not specify what the customer should be buying. It seems that the Regulator cannot do the job of economic regulation without effectively acting as the

43 ‘£15 billion to deliver a modern, safe railway with greater public accountability – Rail Regulator’, ORR Press Release, 23 October 2000

44 ORR Press Release 12 December 2003

45 Ibid

46 SRA Press Release, 19 December 2003

47 Q1417

48 Q1730

49 ORR Access Charges Review 2003: Final Conclusions, Annex D, p 267

50 ORR Press Release, 23 December 2003

informed customer. This is to confuse the roles of economic regulation with the SRA's job of purchasing services. In those circumstances, it is clear that the railway structure must be fundamentally changed.

Financial impact of the Regulator's settlement on the SRA

42. Section 224(6)(a) of the Transport Act 2000 imposed on the Regulator a duty to have regard to 'any general guidance from the Secretary of State about railway services or other matters relating to the railways'. Such guidance was issued on 26 September 2002 and stated that:

"It is particularly important that the Rail Regulator should be mindful of SRA strategies and financial position in the context of the review of access charges..."⁵¹

The Department wrote to Mr Winsor on 16 December 2003. That letter contained a reminder of "his duty to have regard to the SRA's budget".⁵² The Minister of Transport wrote to us prior to giving evidence on 5 November repeating the same point.⁵³

43. When he appeared before us on 29 October, Mr Winsor, emphasised that the private sector train operators enjoyed an open-ended indemnity from the SRA covering increases in the level of track access charges which might occur as a result of the Rail Regulator's decisions.⁵⁴ Mr Winsor explained the consequences of any refusal to honour this:

"If the Strategic Rail Authority does not pay up, the passenger train operators will of course sue the Government, the Strategic Rail Authority, and they will win. That is how it works."⁵⁵

44. The position was confirmed at our request by the Minister who responded in rather more nuanced terms "If we want to continue to achieve the outputs that the Office of the Rail Regulator has itemised and costed we will have to pick it up and pay for it and that has been the case ever since the railways were privatised and, by the way, it was the case when it was in public ownership."⁵⁶ We pressed the Minister on this vital point:

"Clive Efford: I just want to be clear about the Government's role in it because these are decisions that are being made outside Treasury and everywhere else in effect by the Rail Regulator, but the taxpayer is basically just going to sign the cheque?

Dr Howells: Oh, if only. The Treasury will have a to-do on this....*there are no assumptions we can make about the taxpayer and taxpayer's money paying for these costs.* It may well be the case that at some stage in the future, and there has been a lot of discussion about it in this afternoon's session, we will have to decide whether we

51 *Guidance to the Rail Regulator*, 26 September 2002

52 Letter of 16 December 2003 from David Rowlands, Permanent Secretary, Department for Transport to Tom Winsor, Rail Regulator

53 FOR 77A

54 Q 1257

55 Q 1257

56 Q 1609

can go on subsidising the railway in the way we have been and are doing at the moment and are likely to go on subsidising it for the next five years.

Clive Efford: ‘... Mr Winsor... was quite clear that he had the power to impose these increased charges and that those charges would be passed on to the Government and that the Government had no choice but to pass them on to the taxpayer.

Dr Howells: *The Government always has a choice* (emphasis added).⁵⁷

45. However, Mr Winsor characterised the position as follows:

“there is a contract between the state and the private sector. It says that every five years or so there is a question to be arbitrated. The question is how much money does the network properly require and what should the charges be. It has very properly put that question into the hands of an arbitrator - in this case the Regulator.... there are no grounds, it seems to me, for the Government later to complain that they wish they had not done it and they have chosen not to pay.”⁵⁸

Nevertheless, Mr Winsor failed to square this position with his other clear responsibility to “have regard to the budget of the SRA”.

46. The ORR’s *Track Access Charges Review 2003: Final Conclusions*, published on 12 December 2003, notes:

“Ten days before the publication of this document, the DfT and the SRA made a joint submission to the Regulator in which they explained that for accounting reasons it would be desirable for the SRA in future to increase the amount of money it pays in grant to Network Rail, allowing access charges to be set at a lower level than [proposed] in Table 3.”⁵⁹

47. The Review states that the Regulator considered it “regrettable that such fundamental issues should be raised at such a late stage in the review, given the considerable efforts he has made to establish the SRA’s financial position, in accordance with the statutory duties.”⁶⁰

48. Our inquiry exposed an astonishing and fundamental disagreement between the Government and the Regulator about the extent of the latter’s powers. According to the Minister, the Government had a choice about whether to accept the Regulator’s access charges settlement; but the Regulator considered that the Government had no option but to accept his decision. This is a prime example of the confusion which lies at the heart of the present structure of the railway and why it is essential that this structure must be streamlined. Since we took this evidence, the Secretary of State has made clear, in answer to a parliamentary question, that the Government is committed to the Regulator’s access charges settlement. We were pleased to note that in the same answer

57 Q 1611

58 Q 1261

59 *ORR Access Charges Review 2003: Final Conclusions*, p 11

60 *ORR Access Charges Review 2003: Final Conclusions*, p 12. The Committee asked the Regulator and Mr Bowker about the provision of SRA financial information to the Regulator late last year when it was clear that there had been a partial break-down in communication. QQ 1286, 1577

the Secretary of State indicated that the Government would need to consider “whether options for changes to the industry structure might imply consequential changes to the details of economic regulation.”⁶¹

49. It appears that both the Government and the SRA were unprepared for the result of the Rail Regulator’s Interim Review of track access charges and that a last minute panic took place about how the financial implications of the Regulator’s settlement for the SRA were to be met. The SRA and the Government should not have been surprised that the Regulator was proposing to set aside his duty to have regard to the SRA’s budget because Mr Winsor said so specifically in his *Draft Conclusions* document published in October 2003.⁶² The Regulator chose not to give appropriate weight to his statutory duty by ignoring the SRA’s budget; and the Government and the SRA failed to challenge this decision.

50. This whole episode is not only an example of the high handed manner in which the Regulator approaches his role; it is an example of a deep failure in the structure of rail governance which has allowed the Regulator to act as a “Rail Czar”, something that was never intended and which must be corrected.

Conclusion

51. The private sector needs appropriate protection from arbitrary Government decisions. But the current power of the Regulator goes far beyond reasonable bounds and must be reined back. The enormous sums of public money directed to the railways by the Regulator are ones over which, astonishingly, neither the Government, nor the SRA, have any practical control. The Government has little choice but to honour the cheques which the Regulator writes for it.

52. The present situation is an intolerable restriction on the Government. The sums of money decided by the Rail Regulator are so large, and the issues for the transport infrastructure of the country so important, that the Government needs to take back from the Regulator decisions over the level of infrastructure funding.

61 HC Deb 9 February 2004, Col 1237W

62 Para 2.8

3 Network Rail

53. Network Rail Infrastructure Limited acquired Railtrack PLC on 3 October 2002 and assumed the business of operating, maintaining and renewing the national railway infrastructure network on that date. The company is the monopoly owner of the national rail network and operates under a network licence issued by the Secretary of State and, as explained in Chapter 2, is regulated by the Rail Regulator.

54. We asked ourselves in what respects Network Rail appeared to be fulfilling its remit of operating, maintaining and renewing the infrastructure, and have identified a number of serious problems.

Ownership and accountability

55. Network Rail has no shareholders, but instead has members who own the company and to whom it is accountable. However, the members have no financial or economic interest in the company and receive neither dividends nor share capital.⁶³ The *Annual Report and Accounts 2003* nevertheless states that “members of Network Rail will have an important role in ensuring that Network Rail is managed in line with high standards of corporate governance.”⁶⁴

56. Industry stakeholders are eligible for membership on the basis of specific criteria including franchise holders, railway undertakings, and operators of railway assets. Public Members are appointed on the recommendation of a “Membership Selection Panel” which is chaired and contains up to three independent members but is appointed by the Board of Network Rail.⁶⁵ The decision on who to appoint is that of the Board of the company, not the Panel.⁶⁶

57. There are 116 members whose main roles are to:⁶⁷

receive the accounts of the company;

approve changes to the constitution;

approve the appointment and re-appointment of directors (except the SRA director);

approve the appointment and re-appointment of the company auditors.⁶⁸

58. We asked Mr Armitt, Chief Executive of Network Rail, how the members influenced the company’s decisions. He instanced two formal annual meetings and informal

63 *Policy and Procedure for the Selection and Appointment of the members of Network Rail* is available on the company’s website.

64 *Network Rail Annual Report and Accounts 2003*, p 10

65 *Policy and Procedure for the selection and Appointment of the Members of Network Rail*, para 28

66 *Ibid*, para 35

67 *Network Rail Annual Report and Accounts 2003*, p 11

68 *Policy and Procedure for the Selection and Appointment of the Members of Network Rail*, para 13

meetings.⁶⁹ He considered the accountability exercised by members was effective,⁷⁰ and reminded us of the many other accountabilities owed by the company:

“we are also accountable to HMRI for our safe conduct of the network. We are accountable to the Rail Regulator to a greater degree than Railtrack was. We are accountable to our customers. There are a lot of people with a lot of interest in the performance of Network Rail who do not hold back at all in pointing out where they think we are going wrong. I can assure you that we feel very accountable to a large number of people who do not hesitate to publicly express their disquiet, in a way in which in the private sector it would not happen.”⁷¹

59. However, accountability is not the same as people “publicly expressing disquiet”, and it is arguable that the accountability of Network Rail is less than Railtrack which had shareholders. **Network Rail did not convince us that the members of the company were exercising an effective control of the company. We were also concerned that industry members were virtually self appointing. These members include contractors,⁷² and while members have a duty to the company, there was always some possibility of the appearance of a conflict of interest. Finally, the public members are appointed by the Board of the company and represent no-one but themselves.**

60. While Mr Winsor was reported widely in the press as being critical of the company’s structure,⁷³ he thought that the compensating measures he had taken to strengthen the network licence would correct the “accountability deficit”:⁷⁴

“I have made up the accountability deficit with the increased licence conditions, the stronger, streamlined and simplified access contracts and many other things... I would just summarise the accountabilities. The network licence is now the strongest that it has ever been. All the defects of privatisation have now been put right...The membership of the company is not without influence. They can question the board and they can fire the board.”⁷⁵

61. The actions of the Rail Regulator to strengthen the terms of Network Rail’s network licence may be welcome in themselves, but are no substitute for sound day to day management and powerful managerial accountability to the owner. We do not believe that appropriate accountability is demonstrated at present by the company.

Business planning and performance

62. Network Rail states that it has developed a “clear plan” for “transforming the business to meet the requirements of our stakeholders”.⁷⁶ But the delivery of the plan

69 Q76

70 Q78

71 Q79. See also, *Network Rail Business Plan Summary 2003*, p 13

72 Q75. A list of Network Rail members may be found on the company’s website

73 For example, *BBC News Online*, 3 June 2003; ‘Network Rail ‘out of control’’, *The Guardian*, 7 June 2003

74 Q140

75 Q140

76 *Network Rail Business Plan Summary 2003*, p 10

depends upon a number of assumptions, for example: asset knowledge; greater engineering access to the network; an increase in supply chain capacity; the introduction of high-output machinery; and the estimated cost of the West Coast Route Modernisation remaining stable.⁷⁷

63. Network Rail readily acknowledges that it does not have complete control over the factors that contribute to industry-wide objectives for safety, performance, capability and relationships.⁷⁸ Mr Armitt admitted “It is not only our own performance, it is that of the train operators in operating the trains that has to improve equally ...”.⁷⁹

64. When the Regulator gave evidence to this Committee in October he castigated the performance of Network Rail for being “92 per cent worse than before Hatfield...”.⁸⁰ When he asked himself why it was so bad, he thought that this was due to Railtrack’s legacy and the period of administration, but also because ‘the company still has to regain operational competence in terms of the management of delay.’⁸¹ **That the performance of the infrastructure provider should have plummeted on the railway in the period since Hatfield by 92%, and from 70% to 92% between June and October 2003 alone is scandalous, and demonstrates the utter inability of the industry as presently structured to improve its performance.**

65. The performance of the infrastructure is a key determinant of the performance of the railways as a whole. 54% of the delays attributable to trains overall arises from operational inefficiencies on the infrastructure.⁸² In October 2000, immediately before the Hatfield accident, the total delay on the railway attributable to inefficient infrastructure work was 7.7 million minutes; last year the total was 14.7 million minutes, figures Network Rail does not dispute.⁸³ The Regulator has set what appear to be testing, year-on-year, improvement targets for the company expressed as “delay minutes affecting all operators” as follows:

77 Ibid, pp 48-50

78 *Network Rail Business Plan Summary 2003*, p 13

79 Q56

80 Q1269

81 Q1269

82 FOR 97B

83 FOR 57B

Table 2

Year	Delay minutes affecting all operators	Year on year reduction
2004/05	12,300,000	-
2005/06	11,300,000	8.1%
2006/07	10,600,000	6.2%
2007/08	9,800,000	7.5%
2008/09	9,100,000	7.1%

ORR, *Access charges Review 2003: Final Conclusions Table1: Network Rail's performance trajectory, para 13.*

66. While Network Rail has a leading role to play in improving performance, achieving those improvements depends on train operators and other industry players working co-operatively. It appears clear from the evidence we took from the company that it recognises the importance of the issue, is taking the problem seriously and is making efforts to address it. But the company's attribution of the increased delays to a wide variety of factors, such as safety standards, contractor response times, and poor cross-industry co-ordination following disruption and even a much higher level of track renewals is reasonable. Network Rail told us "...we will ultimately carry some risk that our industry partners will not be able to achieve the profile of improvements which would enable us to meet the regulator's targets."⁸⁴ In view of the number of contributors whose performance will be required to achieve these targets, it is hardly surprising that Network Rail describes the targets for future years set by the Regulator as "extremely challenging".⁸⁵

67. **The fact that Network Rail has to assume for business planning purposes that industry partners will make improvements in step with its own, is a further example of the extreme difficulties caused by the structure of the industry. In the present circumstances of extreme industry fragmentation the company's key main performance indicators – improved safety, higher performance, increased system capability, improved customer and stakeholder relationships, improved financial control, improved asset stewardship, improved business performance⁸⁶ - can never be measured and scrutinised to any satisfactory degree against the company's own activities alone.**

68. **That overall railway performance depends on such a large number of companies is not just a problem for Network Rail. The problem is that while it is possible, for example, to collect statistics on the number of trains running, or the number of**

84 FOR 57B

85 FOR 57B

86 *Network Rail Business Plan Summary 2003, p 46*

minutes of delay, and who is responsible for them, unless there is a body empowered to direct performance, companies blame one another for poor performance, rather than working together for improvements. One result is that the responsibility for train service interruptions is not transparent: the fault may lie with Network Rail, the train operating company, a train operating company elsewhere which has caused a ‘knock on’ delay, or a combination of these. That train passengers often do not know who is responsible for delays under the current system is a further, major, frustration for those using the service.

69. It appears most unlikely that the targets for reducing delays set by the Rail Regulator for Network Rail will be met fully, if at all. The cause is, in large part, the result of the fragmented state of the railways and the enormous, wasted effort required to co-ordinate effort between a wide range of parties. Network Rail alone has over 10,000 suppliers of goods and services and approximately 200 main contractors on the infrastructure.⁸⁷ Many delays will arise from events beyond its control. For the Regulator to place ever more challenging targets on a structure which is incapable of meeting them fully is nonsensical.

Incentives

70. In the absence of shareholders, the sole lever of improved infrastructure performance is the Regulator’s incentives regime. He stated in his *Interim Review of Track Access Charges: Draft Conclusions* document published on 17th October 2003, that he was relying on it to improve Network Rail’s efficiency by 8% per annum during the next 3 years and by 6% thereafter.⁸⁸ There is, however, some underlying uncertainty in the projections. For example, in the *Final Conclusions* document published on 12 December 2003 “spending [by Network Rail] *should* fall below approximately £4 billion per annum within five years (emphasis added).”⁸⁹ When we asked Mr Winsor what confidence could be placed in the incentives he has for the company, we were not particularly impressed to hear him rely on the “professionalism and integrity of my office.”⁹⁰

71. We were concerned by one measure that the Regulator presented as an ‘incentive’, namely, the SRA’s “step-in” right.⁹¹ Where Network Rail is unable to meet its interest payments the SRA is able to “step in” with a £4 billion credit facility (“Facility A”). This is embodied in an 2002 agreement between the SRA and Network Rail which also gives the SRA the right to determine whether the Network Rail Chairman and Chief Executive should keep their positions if more than 5% of “Facility A” is drawn down. The Regulator presents these arrangements for an SRA credit facility for Network Rail as a protection for any company investor. This is surely correct. But he also considers it to be a discipline upon the company.

87 FOR 57B

88 *ORR Interim Review of Track Access Charges: Draft Conclusions*, p 2

89 *ORR Access Charges Review 2003: Final Conclusions*, p 6

90 Q1329

91 *ORR Access Charges Review 2003: Final Conclusions*, p 226

72. Although the Chairman and Chief Executive may be deterred from breaching 5% of “Facility A” by the threat to their positions, in the final analysis, “Facility A” is a Government guarantee for Network Rail. It appears to us that such a “Facility” has little to do with a sound mechanism to force the company to live within its means and perform to agreed targets. Indeed, it could be argued that such a cushion acts as a *disincentive* to maintaining budgetary controls. **We are utterly unconvinced that “step in” rights for the SRA provide an effective incentive for Network Rail to improve its performance and live within its means. This is an example of the Rail Regulator “dressing up” Government financial support as a regulatory “incentive” to defend the present regulatory regime.**

Profits, losses and debts

Profits and losses

73. One of the main claims for Network Rail by the Government is that it will be “run along commercial lines to make surpluses from its operations, which will be re-invested in the network.”⁹² Mr McAllister, Chairman of Network Rail, told us, both, that ‘We are expected to make profits’,⁹³ and that “We do not expect to make a profit in the foreseeable future.... because with the level of debt our interest payments are very considerable and will be very considerable....”⁹⁴

74. **Network Rail is far from profitable.** In 2002-03 Network Rail’s preliminary figures indicated a loss of £290 million.⁹⁵ This has since been adjusted to £255 million in the audited accounts for the year.⁹⁶ Had the company not moved from historic cost accounting to depreciated replacement cost accounting for valuing the railway’s fixed assets, Mr Armitt confirmed the £290 million loss would have been much higher, £1.8 billion.⁹⁷

75. In exploring why the company had made a loss, and why the company apparently had spent at levels in excess of those allowed in the Rail Regulator’s Periodic Review of 2000, we were astonished to be told by Mr Armitt:

“When I arrived in Railtrack in December 2001, they were three-quarters of the way through a business planning exercise... we made the details of that business plan available to the Department for Transport, and the SRA were informed. The Regulator would also have been informed. You have to recognise that the company was in essentially a very difficult position, and *we were allowed to expend at the levels of expenditure that we had indicated were necessary* (emphasis added).”⁹⁸

92 Department for Transport, *Delivering Better Transport: Progress Report*, para 3.13

93 Q 1434

94 QQ 1436, 1435

95 Network Rail Press Release, 28 March 2003

96 *Network Rail Infrastructure Limited: interim financial statements six months ended 30 September 2003*, p 8

97 Q 33

98 Q 98

76. Mr Armitt indicated that the Regulator had agreed “in that period” to add the overspend to the company’s “regulated asset base”.⁹⁹ However, Mr Winsor told us “I was not consulted about the levels or the efficiency or the extent of overspending because Ernst & Young, as the administrators of Railtrack had a direct line to the Strategic Rail Authority...The Government took the decision to put the company into administration... and in that time the efficiency of the company and the spending was out of control.”¹⁰⁰

77. The outcome of this overspend was that the Regulator:

“made additions to the regulatory asset base which for April 2004 was expected to be in the region of £6.8 billion, and is now likely to be £17 billion. This is approximately £11 billion in excess. *The increase in the regulatory asset base is the result of a number of additions to the regulatory asset base which were not scheduled in the periodic review. The major contributor, accounting for around 50% of the increase, is the expected overspend during the current control period, during the period of administration mainly. The overspend in 2001-02 and 2002-03 is about £2.5 billion. The overspend in 2003-04 is £2.9 billion.* The addition of £11 billion to the regulatory asset base has been made for two reasons: to ensure that Network Rail was not handicapped by the overspending of its predecessor, and it was Railtrack in administration that overspent as it did and Railtrack before it went into administration as a result of the panic after Hatfield, but also it is in respect of *an agreement between the Strategic Rail Authority and Network Rail made prior to Network Rail’s takeover of Railtrack which stated that the Strategic Rail Authority would compensate Network Rail for overspending up to April 2004.* (emphases added).”¹⁰¹

78. **We understand the arguments in favour for adding overspend to the Regulatory Asset Base (RAB), but it might be thought that this seems rather like increasing someone’s credit limit on the grounds that the goods they have bought by overspending increase their real wealth. The huge sum of £5.5 billion was overspent in the period 2001-2004. The addition of this amount to the ‘regulatory asset base’ of Network Rail – apparently a decision for the Rail Regulator alone- is the equivalent of a massive, one-off subsidy to the rail infrastructure. Yet, even so, Network Rail has posted a loss of £290 million.**

79. **This episode demonstrates the extent of the power which the present structure has allowed the Regulator to accumulate at the expense of all the other parts of the railway, and of the Government. The Regulator is meant to be restraining costs and seeking value for money. Instead, the present structure has permitted him to write off astonishingly large sums of public money, apparently on his own authority. One highly significant aspect of the overspending during the period in which Railtrack was in administration is that, in the middle of the most severe crisis for the industry in the last 10 years, the SRA, which must have been backed by the Government, bypassed the**

99 Q 99. The *regulatory asset base*, also called *regulated asset base* (RAB), is the Rail Regulator’s valuation of Network Rail’s physical assets, such as track, signalling equipment and stations, FOR 99A

100 Q138

101 Q137

Regulator. The system was not flexible enough for all parties to join together in finding the best solution in extreme circumstances.

Debts

80. **Network Rail's debt is soaring.** In 2002-03 Network Rail's net debt increased from £6.3 billion to over £9 billion.¹⁰² In Network Rail's interim financial statements for the 6 months to 30 September 2003 the debt is stated as £10.3 billion against a forecast of £10.7 billion.¹⁰³ The company gave evidence to us that the forecast for the year to 31 March 2004 was for debt of between £13 and £13.5 billion.¹⁰⁴ However, additional debt of around £4.4 billion is expected over the next 12-24 months as a result of the *Regulator's Interim Review of Track Charges*.¹⁰⁵ Reprofiting revenue streams as borrowing could result in the company incurring further debt of up to £2.8 billion over the same period.¹⁰⁶

81. As a private sector company, Network Rail has no access to Government funding for borrowing purposes.¹⁰⁷ It estimates the annual cost of borrowing to be approximately £39 million for each £1 billion.¹⁰⁸ The company might therefore eventually incur debt repayments in the region of £800 million annually were it to have to borrow to the extent it believes possible as outlined above. Lord Oakeshott of Seagrove Bay was reported in May 2003 as believing that the company would have saved £80 million in interest payments if it had been financed by Government gilts rather than private finance.¹⁰⁹ Evidence received by this Committee has suggested that Network Rail's borrowing would cost less if raised by the Government.¹¹⁰

82. The argument for private financing might be that this transfers the risk to the private sector, but Network Rail's borrowing has been possible because the SRA has supported it with £21 billion of standby support loans,¹¹¹ thereby transferring the risk back to the Government.

83. However, such Government support does not mean that the company has access to the cheapest borrowing:

“as a private sector company, Network Rail (NR) does not have access to Government gilts to meet its borrowing requirements....through SRA support for NR's income requirement, either through support for Track Access Charges or

102 *Network Rail Infrastructure Limited: Preliminary Results for the Twelve Months ended 31 March 2003*, p 7 and *Network Rail Annual Report and Accounts 2003*, p 2

103 *Network Rail Infrastructure Limited: Interim Financial Statements Six Months ended 30 September 2003*, p 4

104 FOR 57B

105 FOR 57B

106 FOR 57B

107 FOR 57B

108 FOR 57B

109 'Ministers wasted £80 million on Network Rail', *The Times*, 29 May 2003

110 FOR 79

111 *Network Rail Business Plan Summary 2003*, p 44

payments of Network Grant, Government does indirectly meet the cost of NR's borrowing."¹¹²

although "The SRA facilities allow NR to borrow for the short and medium term at very low rates, with a margin of around 35 basis points above gilts. (100 basis points being equal to 1 percentage point)".¹¹³

84. Further Government support is to be provided for by a securitisation of the company's income:

"To provide comfort to investors about policy and related risks of investing in NR, Government intends to provide an indemnity to the company to meet a shortfall in its ability to meet debt service costs of the securitisation under certain circumstances."¹¹⁴

85. The role of the Government in guaranteeing the entire financing of Network Rail, and in providing comfort to private investors, is clear from this evidence. The private status of the company means that the company's borrowing is more expensive than would be the case were it to be Government owned, despite the Government's crucial role as guarantor. **In effect, what has happened is that the Government has accepted the risk of the Network Rail operation, but on more expensive terms than it need have had it direct ownership of the company.**

86. **We are deeply concerned that the cost of servicing Network Rail's considerable debt is higher than it need be because of the company's private status which means that the cheapest Government borrowing is unavailable to it. We can see little prospect of the company becoming profitable and able to feed funds back into the rail industry under present circumstances. This makes it all the more important for borrowing to be done as cheaply as possible.**

87. **The present Network Rail ownership arrangements do not make sense. The company is not expected to make a profit for the foreseeable future; the cost of funding it as a private sector company is higher than it need be; and its governance arrangements are weak. We consider that it is time for the Government to cut through this tangle of responsibilities and take direct ownership of Network Rail on the grounds that a Railways Agency, incorporating the rail infrastructure, will ensure both the lowest borrowing costs to meet the necessary funding requirements and direct, democratic accountability.**

Driving costs down

88. In its Strategic Plan 2003, the SRA expresses great concern about the escalating cost of operating, maintaining and renewing the rail infrastructure.¹¹⁵ The SRA notes that Railtrack had indicated that the cost for this was 40% higher than allowed for by the Regulator in his Periodic Review for 2000. Network Rail considers that "targeted and

112 FOR 77B

113 FOR 77B

114 FOR 77B

115 *SRA Strategic Plan 2003*, p 38. This strategic plan is the last published by the SRA to date

incremental savings” are unlikely to effect the desired cost reductions but that a “step change” will be required and has set itself a target of achieving efficiencies equivalent to 20% of costs by 2006 (estimated at almost £1 billion of additional savings). Mr Coucher told us that he estimated that £1.1 billion of savings had been identified already out of an annual target of £1.3 billion.¹¹⁶

Maintenance and track renewals

89. £5 billion of Network Rail’s £6 billion annual cost base was spent on external contractors.¹¹⁷ In June Mr Coucher, Deputy Chief Executive of Network Rail, said that the company was removing three maintenance areas from the private sector to take the work directly under its control “to understand how our cost base moves, and what working practices and standards we put on areas that drive up cost.”¹¹⁸ However, there was no intention by the company to take all maintenance “in-house” at that stage.¹¹⁹

90. On 24th October, shortly after the rail maintenance firm Jarvis relinquished its three rail maintenance contracts,¹²⁰ Network Rail announced that it was taking all remaining rail maintenance on the national network away from the private sector taken after “a fundamental review of rail maintenance that has been carried out over the last six months.”¹²¹ Renewals work would remain with the private sector with the transfer to be complete by summer 2004.

91. Mr Coucher said that savings of “around £170 to £250 million” annually could be expected from bringing the contracts in-house.¹²² Mr McAllister estimated the savings to be a little higher at £300 million.¹²³ These would arise from reduced overheads such as the commercial profit margin - which Mr David Clarke, Strategy Director at Jarvis Rail, estimated was in the “range” of 4% for maintenance and 6% for renewals¹²⁴ - and efficiencies, such as removing duplication of systems to manage staff and programmes within contractors and within Network Rail itself, and economies of scale.¹²⁵

92. The company would need to compensate the private sector for early termination of maintenance contracts, but we were told that the level of compensation was commercially sensitive and could not be divulged.¹²⁶ It appeared that the earlier worries about absorbing large numbers of employees had been dispelled,¹²⁷ even though Mr

116 QQ12, 9

117 Q12

118 Q21

119 Q24

120 Jarvis Press Release, 10 October 2003

121 Network Rail Press Release, 24 October 2003

122 Q1405

123 Q1476

124 QQ 721, 729. Mr Andrew Rose, Chief Operating Officer of Balfour Beatty Rail thought profits on maintenance for the private sector under Network Rail’s ‘new maintenance contract’ (since set aside when the company took direct control of maintenance) would be ‘4.7% of sales value’, Q798

125 FOR 57B

126 Q1405; FOR 57B

127 Q24

Armitt told us that the company will now grow from 16,000 to “about 34,000” as a result of taking maintenance in-house as staff transfer from the private sector.¹²⁸ The company did not consider this to be a “strategic” decision but, in Mr McAllister’s words, an “operational” one for the company alone.¹²⁹

93. We think that the company’s decision to take all infrastructure maintenance in-house is a move in the right direction, though we had expected to be given a rather more exact estimate for the likely savings than the range of figures presented to us. It appears obvious that overheads associated with contracting for such work with the private sector do swell overall costs, and that in the absence of private sector profit margins the cost of maintenance should fall. However, the company will need to manage the costs of increasing its own workforce to cope with this work carefully to preserve potential savings. It will also be particularly important that the company attracts the appropriate mix of engineering expertise from the private sector.

94. However, the company intends to continue to contract with the private sector for track, telecommunications and signalling renewals. In his Statement to the House of Commons on the 28th October 2003, the Secretary of State said that this was because that market was well suited to competitive tendering and that such work could be carried out on a project basis.¹³⁰ The company told us that it had tightened its renewal contracts and that the new contracts “will deliver further efficiencies” and “value for money”.¹³¹ Mr Armitt considers that out-sourcing infrastructure renewals work is effective,¹³² and has “targeted” a 20% saving in the contracts for renewals over the next three years.¹³³ However, Mr Bob Crow, General Secretary of the National Union of Rail, Maritime and Transport Workers, considered that there was no fundamental difference between railway maintenance and renewals work and saw no reason why the latter should not be brought “in-house” by Network Rail.¹³⁴

95. Network Rail’s decision to retain the private sector for track renewals could be problematic. While inefficiencies may, or may not, be driven down to the level the company is seeking by this decision, there will remain a contract profit margin cost to the company which will be absent from the rail maintenance side of the business. The efficiency gains will need to be demonstrably significant for National Rail’s present renewals’ policy to be persuasive. Taking more work “in-house” would also be an opportunity to reduce the number of company “interfaces” and contracts which currently burden the industry. In the longer term, Network Rail should reconsider its decision to retain private sector contracts for track renewals. It should also review now what other services it currently purchases and which might be more economically provided under direct management control.

128 Q1471

129 Q1424

130 HC Deb 28 October 2003, col 162

131 FOR 57; Q1431

132 Q1414

133 Q1445

134 Q1200

Estimating funding requirements

Headline figures

96. Network Rail has revised its estimates of the funding it will require over the “control period”, 2004-2009, three times since March 2003. In March 2003 the company estimated its requirements at £35 billion; in June 2003 at £29.5 billion; and in September 2003 at £24.5 billion, a reduction of nearly a third from its first estimate.¹³⁵ On 7 January, Mr Armitt denied that the company had inflated its original estimate of its requirements in order to attempt to set a high benchmark for the final settlement “Absolutely not”.¹³⁶

97. Mr McAllister, Chairman of Network Rail, explained:

“When the first estimate was published in March we did indicate to all concerned that we felt that we were not ready at that stage to formalise the numbers. We did say that we would continue to work on these to improve efficiencies. We would rather not have published the March numbers but we were required to do so under the terms of our licence....”¹³⁷

98. On 17th October 2003 the Regulator published *Draft Conclusions* which suggested that the amount required by the company was £22.7 billion¹³⁸ (since revised down to £22.2 billion when he published his *Final Conclusions* on 12 December).¹³⁹ Network Rail accepted the Regulator’s final settlement on 5 February 2004.¹⁴⁰ However, the difference between the company’s last published estimate of requirements and the Regulator’s still represented £2.5 billion.

Renewals

99. Such headline variations may arise because of disputes between Network Rail and the Regulator over the levels of activity. In this case, the Regulator considered that Network Rail should do less renewals work than it had planned.

100. Consultants LEK Consulting, Halcrow Group, and Transportation Technology Centre Inc., retained by the Rail Regulator to study the current expenditure of maintenance and renewals as set out in Network Rail’s Business Plan, considered that of 798 track renewals reviewed only 57% of “plain line track” renewals were “fully justified”; of the remainder, 16% were “not justified”. Renewals, and other work, were sometimes not justified in the consultants’ view because there was insufficient information available in Network Rail to make a judgement.¹⁴¹

135 Press Release , 23 September 2003

136 Q1721

137 Q1390

138 ORR Press Release, 17 October 2003

139 ORR Press Release, 12 December 2003

140 Network Rail Press Release, 5 February 2004

141 *Bottom-Up Review of Network Rail’s Business Plan: 2003/04-2005/06*, 8 August 2003, Report to ORR, paras 5.3.10, 1.4.2, Fig. 1.4, and 1.2.4, Fig 1.3

101. In his *Draft Conclusions* published in October, the Regulator concluded that Network Rail should spend 20% less on renewals in 2004/05 and 2005/06 –equivalent to savings of £360 million- than budgeted for in the company’s March 2003 Business Plan.¹⁴² He noted there that Network Rail disputed the consultants’ work,¹⁴³ but that he was not persuaded by Network Rail.¹⁴⁴ The view of the Regulator was shared by Roger Ford, the railway journalist, in evidence to this Committee: “Network Rail’s projected maintenance costs are broadly in line with historic figures. However renewals are so high as to be ludicrous.”¹⁴⁵

102. The Regulator paraphrased the company’s argument in his *Final Conclusions* document published in December: “Network Rail asserted that the replacement of additional track components in conjunction with a necessary renewal job is often justified by reductions in overall costs.”¹⁴⁶

103. We asked Mr Armit about this and he told us:

“We clearly had justification [for the renewals]. What they were looking for was detailed calculations which they could find for the bulk of it. On some we had placed our assumptions on fairly straightforward age of the infrastructure, renewal rates on a broad scale and therefore we knew that we were going to have to carry out those broad levels of renewal. I would still advocate those broad parameters for carrying out renewals are a good guidance for what needs to be done, when you are looking five years out you have to rely on broad parameters, you do not rely on detailed calculation for what you are going to do five years hence.”¹⁴⁷

104. Probed about whether Network Rail’s figures for overall budget requirements might not be more accurate than his own, the Regulator said “It is conceptually possible but let us remember they are the monopoly provider of an essential service. They are hardly likely to ask for less.”¹⁴⁸ This seems to be something of a caricature of the Network Rail’s position, which was clearly based on professional estimation, even if the company was culpable in not having provided supporting documentation of sufficient and persuasive detail in the case of some renewals.

105. Network Rail’s approach to renewals appears to be in line with Government policy, which is that one advantage of the company’s commercial structure over Railtrack’s equity basis was “decision-making based on long-term analysis of whole-life asset costs- not deferring much-needed investment expenditure for short-term economic gain.”¹⁴⁹ This has been Network Rail’s position in the Interim Review process. But it is evidently not the Regulator’s, and the Government itself may have underestimated the short term costs of such a policy when applied to the run down UK infrastructure. **We are**

142 *ORR Interim Review of Track Access Charges*, para 5.27

143 *Ibid*, para 5.25

144 *ORR Interim Review of Track Access Charges*, para 5.26

145 For 88

146 *ORR Access Charges Review 2003: Final Conclusions*, p 55

147 Q1415

148 Q1324

149 Department for Transport, *Delivering Better Transport: Progress Report*, December 2002, para 3.13

concerned that the drive to reduce costs appears in conflict with long term investment in the infrastructure. Balancing costs and investment needs to be undertaken on the basis of solid data and agreed targets, both of which appear to be in short supply. The company needs to get a better grip on the level of renewals required so that there can be confidence that cost and investment are in reasonable balance.

106. The Regulator was entitled to challenge Network Rail's estimates of work required where these appeared to him to be in excess of necessity. We are nevertheless astonished at the spectacle of two bodies – Network Rail and the Rail Regulator - in dispute in this manner. This is not an outside body (the Regulator) undertaking a straightforward check of the operator's documentation, but appearing to undertake a root and branch parallel exercise by consultants of renewals' estimation. Either the renewals documentation of Network Rail is grossly deficient – as the Rail Regulator appears to believe – or the Regulator undertook too detailed an examination, at a considerable consultancy cost.¹⁵⁰

107. It was inefficient and highly expensive for Network Rail and the Rail Regulator to undertake parallel exercises assessing renewals' requirements of the rail infrastructure. It should be a firm objective for the future economic regulatory authority and the infrastructure provider to ensure that the quality of the latter's estimation processes and records is sufficient to provide a very high degree of confidence in what is being proposed, allowing there to be much less parallel checking and micro-management in future.

108. It is also unacceptable that Network Rail did not have its estimates of overall funding requirements under control. We accept that the original estimate in March 2003 may have been inaccurate owing to the requirement to publish and the relative shortness of preparation time. However, even after an element of joint working with the Regulator and his consultants, the company's final requirements estimates vary by an excess of £2.5 billion from those of the Regulator.

109. In these circumstances it is difficult to understand why the company has now agreed to a settlement which its own estimated figure appears to suggest is too low for the work it considers necessary without complaint. It had options to ask the Regulator either to issue a new review notice, or refer his determination to the Competition Commission, but chose not to do so.¹⁵¹ This suggests that the company's estimates of funding requirements cannot be relied upon. The company needs to take urgent steps to demonstrate that it has adequate systems in place to ensure future funding forecasting is accurate to establish credibility.

Conclusion

110. Taking the company into direct ownership together with removing the Regulator's present role of determining the level of the company's funding, as discussed in Chapter 2, would enable the Government to ensure cheaper funding for, and more effective

150 Q1306

151 On 7 January, Mr Armitth indicated his belief that the company would accept the settlement, Q1720; which it duly did, Network Rail Press Release, 5 February 2004. See, Q1257 and, *ORR Access Charges Review 2003: Final Conclusions*, pp 17-18 for reference to the Competition Commission.

overall control over, the railway infrastructure, particularly maintenance, renewals and enhancements. It is likely that there will continue to be a role for the private sector in aspects of infrastructure provision. But the structure of Network Rail needs to reflect the funding reality that the Government guarantees the finances of the railway and will continue to do so for the foreseeable future. Network Rail's present private sector status and structure mask that reality and not only fails to deliver benefits to the industry and the travelling public, but actually produces the significant funding and governance flaws we have discussed. The Government needs to move quickly to take control of the infrastructure into the public sector.

111. However, in order to rationalise the railway and provide a platform for significant future service improvements, the Government must go further. It also needs to have a much tighter grip of the outputs it requires from the rail industry. To achieve that, the current artificial barriers between those specifying the outputs and those operating the infrastructure (which largely determine those outputs) must be removed. In the next Chapter we examine the SRA's current role in specifying outputs, and the way in which the present structure frustrates its ability to carry out this key leadership function.

4 Strategic Rail Authority

Purpose

112. The SRA is a non Ministerial government body set up under the Transport Act 2000 to provide strategies, planning and co-ordination for the railway, and to guard passengers' rights.¹⁵² It purchases rail services and infrastructure, effectively deciding on the industry outputs; it also provides standby financial facilities for Network Rail. The Secretary of State may give the SRA guidance and directions on a range of matters.¹⁵³

113. The Government's *Directions and Guidance to the Strategic Rail Authority* explain its purpose which is to "provide leadership for the rail industry and ensure that the industry works co-operatively towards common goals."¹⁵⁴ The SRA's "primary objective" is increasing rail use; and its "equal primary objective" is to "work with the rail industry to achieve substantial lasting improvements in performance"¹⁵⁵ In order to achieve its purpose and objectives the *Directions and Guidance* state that the SRA "will need to address all aspects of the operation of the railway".¹⁵⁶ To do this a number of means are identified:

"...to influence and in some cases to direct the industry, through the passenger franchises which it awards and manages, the investments which it promotes or undertakes, through other forms of financial assistance, and through its regulatory role for consumer protection. It should use these powers as appropriate. But it will also need to guide the industry through dialogue and persuasion. It will in particular, need to set priorities for action by itself and others (emphases added)."¹⁵⁷

This is done by means of activities such as the creation of strategies for the railway and rail passenger franchise management.¹⁵⁸

114. Our predecessor Committee concluded two years ago that, "The Strategic Rail Authority has failed to date to provide the leadership, priorities and precise timetable for implementation of improvements to the railways that were the main purposes of its establishment."¹⁵⁹ In the remainder of this Chapter we examine aspects of the SRA's franchise management; its formulation of strategy; and its ability to work "co-operatively" with other rail bodies, in order to take a view of its current approach to structure, leadership and vision.

152 A body carrying out public functions but which is not a Government Department

153 *Directions and Guidance to the Strategic Rail Authority* may be found on the SRA 's website

154 *Directions and Guidance*, para 2.1

155 *Ibid*, paras 5.5, 6.2

156 *Directions and Guidance*, para 6.3

157 *Ibid*, para 6.4

158 *Directions and Guidance*, Chapters 7 and 9

159 Transport, Local Government and the Regions Committee, *Passenger Rail Franchising and the Future of Railway Infrastructure*, para 12

Franchises

115. **The letting and management of passenger rail franchises is at the heart of the SRA's work and where its impact can be assessed most clearly. It is also an area where the private sector is most directly involved in providing railway services and where its freedom to innovate is greatest.**

Train operating companies' costs

116. The nature of franchises and the franchising process has changed radically since the current structure was last examined by our predecessors. Eighteen train operating companies received subsidy in 2002-03.¹⁶⁰ According to the SRA's last published *Strategic Plan 2003*, subsidy, net of receipts, was projected to grow to over £1.4 billion in 2003-04,¹⁶¹ and nearly £1.6 billion in 2004-05.¹⁶²

117. The original franchise bids assumed a decline in both staff costs and total operating costs.¹⁶³ In fact in the 4 years to 2001/02 staff costs rose 28% and other operating costs rose 22%. 29% more staff were employed by the train operating companies in 2001/02 than had been anticipated – 33,376 was the bid assumption, 43,027 was the actual total.¹⁶⁴ In addition, annual staff earnings increased by 18% over the same period. While franchise revenues outpaced predictions this was insufficient to cover the greater costs. The SRA states when franchises were let originally it was assumed that annual operating losses before subsidy could be reduced by £600 million per annum but this has not occurred. In 2001/02 the reduction was £222 million with the shortfall of £378 million being shared between franchisees in the form of lower profits and the SRA in higher subsidy levels.¹⁶⁵

118. The Association of Train Operating Companies (ATOC) told us that train operating company costs have 'marginally increased in recent years' citing insurance as an example.¹⁶⁶ Mr Garnett of GNER said that "We [train operating companies] have held our costs static."¹⁶⁷ This is a far cry from the efficiencies originally predicted. The SRA's *Strategic Plan 2003* states "In the short to medium term, SRA projections show an upward trend in costs and government support levels continuing."¹⁶⁸ We were given no indication of when subsidy for train operating companies would cease.

119. Some franchises have performed in the way that was expected. However, it is clear that the vast majority have not been able to produce the efficiency gains that were confidently anticipated at the time of privatisation. The network is now being run by a

160 *On Track*, October 2002 – March 2003, p 20

161 *SRA Annual Report 2002-03*, Appendix 3

162 *SRA Strategic Plan 2002-03*, p 52, Table 10. Public subsidy paid to train operating companies in 2002-03 was £1,320.8 million, *On Track*, October 2002 – March 2003, p 20

163 *Ibid*, p 48

164 *SRA Strategic Plan 2002-03*, p 51, Table 9

165 *Ibid*, p 48

166 FOR 95

167 Q1081

168 *SRA Strategic Plan 2003*, p 49

patchwork of companies, which operate in a variety of ways, with a variety of incentives. It is not for us to judge whether more efficient companies could have performed more creditably; however, the number of franchises in difficulties suggests something is fundamentally wrong with the structure of the industry. Either the private sector is no more efficient than the public, or it is being given tasks that no one can fulfil.

Low bids

120. Some of the extra franchise operating costs come about, at least in part, because the infrastructure is not of the quality the bidders assumed. The failure to deliver the promised West Coast Main Line upgrade by May 2002 meant Virgin West Coast and Virgin Cross Country demanded and received substantial payments from the SRA. Mr Bowker confirmed to us that the sum set aside for Virgin was £291 million.¹⁶⁹ The SRA included this payment in evidence to us as one of the factors contributing to general cost escalation in the rail industry.¹⁷⁰

121. Even without such infrastructure failures, the SRA states that “the costs of operating the current franchises have escalated and are substantially higher than bid levels”.¹⁷¹ Connex, for example – stripped of the South Eastern rail franchise by the SRA in 2003¹⁷² – received £58 million from the SRA in 2002. According to Mr Bowker this was “Because the difference between their cost and revenue assumptions and the subsidy that they had bid for when they originally won their franchise had diverged in order to need additional support for that financial year. They had got their numbers wrong.”¹⁷³ M. Olivier Brousse, Managing Director of Connex South Eastern Ltd, indicated that Connex would not be returning any part of the additional sum of £58 million to the Government.¹⁷⁴

122. In our view, the essence of private sector involvement is that the private sector pays if it gets its sums wrong. It is outrageous that such astonishingly large sums of taxpayers’ money have been used to prop up palpably failing businesses such as £58 million in the case of Connex. While we accept that failures in the initial franchise process may have been to blame originally, we cannot understand why action was not taken earlier by the SRA. As a result of this failure to monitor Connex properly the SRA bailed out a company using taxpayers’ money only to strip it of its franchise a short time later. The SRA’s management of this franchise has been woefully poor.

Management contracts

123. In July 2003 Mr Bowker estimated that out of 25 franchises, nine would be running on management contracts by the year’s end.¹⁷⁵ The distinction between the provision of

169 Q234

170 FOR 97A. The West Coast Main Line upgrade is discussed in detail later in this Chapter.

171 *SRA Franchising Policy Statement*, November 2002, p 5

172 Connex ceased operating the franchise on 9 November 2003, SRA Press Release , 8 November 2003

173 Q310

174 Q1101

175 Q386

rail services by means of a successful franchise and a management contract is crucial and lies in which party assumes the revenue risk: in the former the profile of subsidy payments which the franchisee estimates is required at the time the bids are made means that he accepts the revenue risk; in the case of the latter the franchisee is paid a fee equivalent to his costs and the SRA as franchisor accepts the operational revenue risk. **Nearly a third of the franchises were no longer expected to function in the entrepreneurial, risk-taking way that was one of the fundamental justifications for private sector involvement in running train services but simply to function as fee paid agents of the SRA. This indicates the extent of the present malaise.**

Franchise extensions

124. Under the existing rules, franchises which have expired should be subject to further competition. In fact, many will be extended. Even now that the SRA and Network Rail have had over a year to produce stability, extensions continue, produced in part by delays in dealing with the new franchising structure. On 9 October 2003 the SRA announced a two year extension from 2004/05 to the Central Trains franchise held by National Express Group plc.¹⁷⁶ It appeared that precise cost figures were still being worked on, but the SRA stated that subsidy levels will be increased by about £54 million in 2003/04 and by £69 million in 2005/06; the entire subsidy bill for these two years will be around £600 million.¹⁷⁷ Mr Bowker, while agreeing that “as a matter of general policy competitive tendering will always get you the best results”,¹⁷⁸ explained that amongst the reasons for the decision to extend the franchise, were “issues” around Birmingham New Street Station and with the West Coast Main Line and that was “most likely to deliver certainty for passengers, least disruption and best value.”¹⁷⁹ More recently, there have been three further two year extensions.¹⁸⁰ **Existing franchise agreements should be extended only if there are compelling operational requirements, or clear value for money justification. Extensions are a measure of last, not first, resort, and these examples suggest that the SRA has failed to plan ahead adequately.**

New franchising policy

125. Since our predecessors’ last inquiry into franchising,¹⁸¹ a new franchising policy has been announced by the SRA, which considered that the old agreements set performance levels too low and lacked service quality standards.¹⁸² The new model franchise has four levels of performance for service punctuality, cancellations and capacity: target level, remedial plan level, breach level, and “event of default” level. Each level demands an improvement in performance from the franchisee over the period of the franchise. The

176 SRA Press Release, 9 October 2003

177 Ibid

178 Q1557

179 Q1557

180 SRA Press Release, 13 February 2004

181 Transport, Local Government and the Regions Committee, *Passenger Rail Franchising and the Future of the Railway Infrastructure*

182 *SRA Strategic Plan 2003*, p 64. The SRA announced on 30 January 2004 that it had signed the first new franchise agreement with National Express Group plc to operate the new Greater Anglia franchise

agreement contains a “Key Performance Indicator regime” which covers the passenger’s journey.¹⁸³ The first franchise to be based on the new arrangements will be Greater Anglia which should begin in April 2004.¹⁸⁴ A major aspect of the new arrangements is that the franchisee, by achieving the “target level”, is able to obtain an automatic three year extension but “In order to obtain an extension the franchisee ... has to do the best that has ever been achieved on those franchise routes for every cause[of delay], every day.”¹⁸⁵

126. We asked Mr Bowker if the new arrangements would prevent the practice of unreasonably low bidding by companies for franchises which would later require additional financial support from the Government. Mr Bowker said that what he was seeking was the “best value bid, not the lowest price bid”.¹⁸⁶ Mr Bowker had referred in a speech to the Rail Finance Summit on 23 October 2003, to the new franchises as removing risk for train operators.¹⁸⁷ We asked whether this meant increased risk for the taxpayer but failed to elicit a clear answer.¹⁸⁸ Professor Glaister of Imperial College, London, gave evidence of how removing risk transfer can weaken the incentive on the private sector to reduce costs.¹⁸⁹

127. The new generation of franchises must be structured in a way which prevents franchisees returning for ever more public money, and ensures that costs are properly anticipated and controlled. Revenue risk should be assumed by the private sector wherever possible. The passenger must be the focus of the whole exercise. The SRA’s record of franchise management to date is poor.¹⁹⁰ While the new franchise arrangements appear to be an improvement over the existing agreements in certain respects, we are particularly concerned that there is an automatic right of extension for three years if targets are met. If the new arrangements are to succeed, targets will need to be set sufficiently high that passengers notice a real difference in day to day performance of railway services; and SRA monitoring will require to be exceptionally accurate and rigorous. We have no confidence that the SRA is presently up to this task.

Train operations

128. The Connex South Eastern franchise will be absorbed into a new Integrated Kent Franchise which will run services in Kent, South East London and parts of Sussex, and include domestic services on the Channel Tunnel Rail Link. Meanwhile, the lines formerly run by Connex are being operated by South Eastern Trains, acting on behalf of

183 FOR 97C

184 SRA Press Release, 30 January 2004

185 FOR 97C

186 Q1511

187 SRA Website

188 Q1512

189 Q479

190 Mr Bowker said in evidence on 1 March 2004 to the Committee of Public Accounts that ‘the SRA has not actually been...good in terms of putting together its overall franchising’, Q59, HC 408-i

the SRA and headed by SRA managers with private consultancy support, for a period before being re-let to the private sector in 2005.¹⁹¹

129. We questioned Mr Bowker closely as to whether, were the experiment with South Eastern Trains to prove successful, the SRA would consider running failing franchises directly.¹⁹² He was willing to learn from the experience,¹⁹³ but thought that the private sector was invariably more efficient than the public sector, and in any case the policy that passenger train operations should be conducted by the private sector was clear.¹⁹⁴ Pressed further to say whether the policy should be changed even “if the public sector comparator shows that you [SRA] could do it [run services] more cheaply and more efficiently” than the private sector, Mr Bowker said he did not.¹⁹⁵ When we took evidence from the Minister of Transport, he, too, rejected any role for the SRA as an operator of trains.¹⁹⁶ **The Government has undertaken to share the results of South East Trains with us and we look forward to seeing these.**¹⁹⁷

130. **We were surprised at the evident unwillingness and timidity of the Government and the SRA to contemplate the SRA running train services directly, even if the SRA’s experience of managing South East Trains demonstrated clearly that this could be done by the SRA at the best price and highest efficiency. It seems common sense that where benchmarking identifies the most cost effective solution to running a franchise then that solution should be adopted. The public are rightly concerned with excellent service and value for money. The record of the private sector in running trains overall is poor. To adhere to the policy of restricting such operations on ideological grounds does not appear sensible. In fairness, this evidence was given before the Government’s recent announcement of its rail review. We trust that now a fundamental review is underway, the Government will consider this option much more actively.**

Conclusion

131. **Even where the SRA has direct responsibility, as with the franchising of passenger rail services, its imagination, focus, and performance are deficient. It has no day to day control of the delivery of passenger rail services, working, as it does, through the train operating companies. The degree to which the SRA is able to improve the journey of the travelling public directly is therefore limited by the sophistication of its contractual arrangements with franchisees. The extreme difficulties inherent in this process are obvious. The quality of the present franchises is poor; the new arrangements appear tighter, but their effect on train performance cannot yet be judged.**

191 SRA Press Release, 22 December 2003

192 Q1501

193 Q1503

194 QQ1504,1506

195 Q1507.

196 Q 1644. The SRA must provide passenger rail services if a franchise comes to an end, or is terminated without a new agreement being put in place, or a direction not to seek a franchise has been made by the Secretary of State, Railways Act 1993, section 30, as amended by the Transport Act 2000, section 212(51).

197 FOR 77B

Strategies

132. The Transport Act 2000 requires the SRA to “formulate strategies”¹⁹⁸ which “should...cover both its own activities and those of the industry.”¹⁹⁹ The SRA requires the consent of the Secretary of State before publishing its strategies.²⁰⁰ The SRA’s strategies embody its approach to various operational aspects of the railway. How effective are these strategies in grappling with key issues of today’s railway?

“Mixed” railway

133. Britain’s railway is a “mixed” system carrying freight and passengers. There is no absolute consensus about whether this “mixed” system is proving a brake on delivering performance enhancements on the railway. But our evidence suggests clear difficulties in certain areas. Amongst operators, FirstGroup plc considers that “congested daytime train paths...reduce day time passenger capacity”.²⁰¹ The Royal Mail, whose commitment to rail freight appears uncertain, believes that “mixed” traffic is a significant problem for the railway.²⁰² Maersk’s view is that there are problems with the ‘mixed’ mode because freight is disadvantaged due to “pathing incompatibility with some passenger services”. In contrast, Freightliner believes that “mixed” freight/passenger traffic is most likely to “produce the intensity of utilisation which makes an expensive investment such as the railway system economically effective.”²⁰³ Mr Christopher Garnett, representing the Association of Train Operating Companies (ATOC), also supported a “mixed” rail system.²⁰⁴

134. Academic commentators suggested considerable problems with operations which contain a mixture of freight and passenger trains.²⁰⁵ Professor Roderick Smith, Head of Mechanical Engineering, Imperial College, London, argues that capacity is limited because of the inherent contradictions of a “mixed” traffic railway which causes bottlenecks and a “huge number of conflicting movements”,²⁰⁶ a view shared by Professor David Newbery, Director of the Department of Applied Economics, University of Cambridge.²⁰⁷ We heard a good deal of evidence about the importance and potential of a dedicated passenger railway. Professor Sir Frederick Holliday argued for the removal of rail freight to road on the basis that this would permit an increase in *passenger* rail performance sufficient to attract compensating traffic from road to rail.²⁰⁸ Professor Smith argued for the construction of a completely new, high speed, dedicated

198 Section 206, Transport Act 2000; *Directions and Guidance*, para 7.1

199 *Directions and Guidance*, para 7.2

200 *Ibid*, para 7.11

201 FOR 34

202 FOR 105

203 FOR 04

204 Q1137

205 FOR 23

206 FOR 43

207 Q474

208 FOR 103

passenger rail network.²⁰⁹ The cost of the construction of such a network were estimated by him to be in the range £11 billion to £27 billion.²¹⁰

135. The concerns about a “mixed” rail system, and a policy of pursuing performance improvements on such a system, are widespread. Dr Kim Howells, Minister of Transport, indicated that a “better option, [a] more realistic one” than building “brand new railways through this country” was “to make better use of the rail network that we have got now with better signalling and better technology”.²¹¹ The SRA told us that it spent £1.3 million last year investigating the case for a “North/South” high speed passenger line, but concluded that its “current budget does not cover the development or implementation of a high speed line”. The SRA’s *Specification of Network Outputs* strategy places emphasis on more capacity being squeezed from the existing rail network.²¹²

136. It appears from the Government and SRA evidence that the railway will remain ‘mixed’ in the near future. Visionary proposals for passenger-only high speed networks have obvious funding drawbacks. Nevertheless, in the context of deciding on a railway future for the 21st century such ideas must be explored thoroughly. We agree that it may be politically and financially difficult to contemplate high speed passenger networks when the existing system is so clearly in need of overhaul, but there must be scope for imaginative thinking about the country’s future transport needs. We hope that this issue will be revisited and the arguments set out clearly.

Freight

137. Freight rail transport is not covered by franchise arrangements. It is undertaken by a number of private companies on the basis of access contracts negotiated with Network Rail. 18.7 billion tonne-kilometres of freight was carried by rail and 149.8 billion tonne-kilometres by road in 2002.²¹³ The SRA’s freight strategy reflects the Government’s objective of an 80% increase in rail freight by 2010 from 2000 levels, a target Mr Bowker thinks may be achieved.²¹⁴ Last year the SRA announced a revision in the “Sensitive Lorry Miles” (SLMs) values – the first since 1996. SLMs are designed to provide an assessment of the external benefits produced by moving freight from road to rail through the payment of Freight Facilities Grant (FFG) and Track Access Charges (TAG).²¹⁵ According to the SRA, SLMs ‘form an essential tool in the appraisal of grant schemes’.²¹⁶

209 FOR 43

210 Professor Smith compared the costs of building a new network with ‘the estimate that the economic damage done by current road congestion and resulting inefficiency is in the order of £20 billion/year.’ FOR 43

211 Q1665

212 FOR 97B

213 National Statistics, *Transport Statistics in Great Britain 2003*, Tables 5.12 and 4.1. The figures for 1997 were 16.8 and 149.6 billion tonne-kilometers respectively, *Transport Statistics in Great Britain 1998*, Tables 5.12 and 4.1

214 Transport Committee, *Overcrowding on Public Transport*, Ev 55

215 SRA *Sensitive Lorry Miles: Results of Analysis*, May 2003

216 *Ibid*, p.2

138. As a result of pressures on the SRA budget, or an inability to manage its budget, and despite the policy of freight subsidies, the SRA suspended new applications for the FFG - which helps to offset the capital cost of providing rail freight handling facilities; and TAG, which helps to pay Network Rail track access charges, in England in January 2003. A new grant, the Company Neutral Revenue Support Grant, designed to encourage inter-modal freight traffic and due to commence in 2003,²¹⁷ will now not be brought in until later this year.²¹⁸ The Confederation of British Industry has queried how the SRA's decision to suspend FFG and TAG fitted with the Government's target to boost rail freight.²¹⁹

139. We heard from two of the rail freight industry's customers, ASDA and the Royal Mail, about the importance of grants to their decisions about whether or not to place freight on the railway. ASDA told us that the savings the company makes by using rail freight facilities amounts to £1.33 million pa.²²⁰ The performance of rail in Royal Mail's case was less than the company considered satisfactory. In ASDA's case the disparity between road and rail concerned the company, but appeared not to be considered critical to continuing with freight on rail because the time lost was made up later in the delivery chain.²²¹

140. It was clear both that ASDA's decision to use rail freight was unlikely to have been taken without the assistance of grants;²²² and that had grants been available for the Royal Mail –an existing customer of rail freight and therefore not eligible for grants- this might have weighed in its decision to scale down, or even abandon, its historic reliance on rail.²²³

141. The SRA's suspension of rail freight grants at the very time that it was fulfilling its strategic remit by updating an environmental benefits methodology, shows the difficulties facing the organisation. In scrambling for short-term savings, the SRA had to compromise its ability to carry out its strategy which caused a loss of credibility throughout the industry in the Government policy on rail freight. Those responsible for the railway in future need to ensure much better coordination of budgetary management and strategy.

Specification of Network Outputs

142. The rail freight industry and the passenger transport executives felt under pressure from the *Specification of Network Outputs* strategy.

217 *SRA Strategic Plan 2003*, p 32

218 *SRA Freight Progress Report 1*, 2003, p. 15. In 2002-03, the value of FFG awarded was £19.3 million leveraging £15.2 million of private sector investments; TAG awarded in the same period amounted to £5 million removing 59 million lorry kilometres from UK roads. Ibid, p 12. ' Around 80 - 85% of Track Access Grant is replaced by [Company Neutral Revenue Support Grant] , SRA Press Release, 10 February 2004

219 '*Credibility on the Line: Ten Year Plan Progress Report*', July 2003

220 FOR 106A

221 Q 632

222 Q 649

223 Q 699

143. The aims of the SRA's outputs approach are stated to be faster train performance on key routes and cost efficiencies. The specification strategy is designed, first, to provide Network Rail with longer periods of time to work on the track ("possessions") intended to promote working and financial efficiencies; and, second, to target maintenance and renewals spending better. The top priority will go to: "Primary/London and South East commuter/main secondary routes"; a lesser priority to: "Other secondary/rural/freight-only routes".²²⁴ The "main secondary routes" will include ports' links from Felixstowe, Holyhead, Immingham, Hunterston, Grangemouth, and Middlesborough (Teesport) to the main infrastructure network.²²⁵

144. Some freight rail users have been disturbed by this "differentiated" approach, seeing it as effectively down grading their own activities.²²⁶ The SRA claims that cost savings of approximately £400 million can be made as a result of its policy, and up to £350 million from longer renewals.²²⁷

145. However, the SRA's scope to take decisions which affect freight operators appears constrained: "In the case of open access passenger and freight train operators, the SRA has no contractual relationship with them analogous to franchise agreements. It would require them to negotiate a lowering of Network Rail's obligations to them in their track access agreements."²²⁸ In addition, the Rail Regulator specifically rejected the SRA's request to lower the budget for Network Rail maintenance and renewals expenditure on the basis of the anticipated savings arising from this strategy, considering that the extent of the savings was uncertain.²²⁹ We make no judgment about the merits of the issue. **The Rail Regulator's refusal to adjust Network Rail's expenditure to take account of the SRA's Specification of Network Outputs is an excellent indication of how severe the limitations are on any SRA strategy in the present structure of the industry when it affects the operation and budget of the infrastructure provider, which are effectively specified by the Regulator.**

Research and data

146. Network Rail has a clear view that "railway research has been neglected in the UK over the past decade."²³⁰ According to Rail Research UK (RRUK), Government funding for rail research in the UK is "similar to the average in the EU on a pro rata basis" but less than half the Swedish level and 8 times less than Spain.²³¹ Professor Roderick Smith called attention to the contrast today's situation offered with 30 years ago where the UK was a world leader in the field.²³² In the aftermath of the Hatfield accident the necessary

224 *SRA Specification of Network Outputs*, para 5.6

225 *Ibid*, para 5.7

226 For example, *Daily Telegraph*, 3 October 2003

227 *SRA Specification of Network Outputs*, paras 4.18 and 4.21

228 *ORR The Interim Review of Track Access Charges: Second Consultation Paper, The Incentive and Financial Framework*, p 79

229 *ORR Access Charges Review 2003: Final Conclusions*, p 16

230 In 2002/03 it spent approximately £8 million on research and development in a variety of collaborative relationships and expects to spend similar amounts this year and next. FOR 57B

231 FOR 23A

232 FOR 43

research rail engineering skills could not be found in the UK and had to be imported.²³³ Extremely few UK sourced rail research papers are now published; research careers in the UK are limited; and there is a knock-on effect on the UK's "technical policy making and technical capacity."²³⁴ Japan is the clear world leader in railway research.²³⁵

147. Research is vital to decisions about the future of the railway, as the Secretary of State's *Directions and Guidance* makes clear. The SRA is not given an explicit co-ordinating role in rail research but the importance of research to its activities is stressed, as is the need for it to be aware of the range of research activities in the UK and Europe generally.²³⁶ The SRA should "encourage and as appropriate commission research related to its purposes and objectives' and should ensure that its research is developed in consultation with other bodies, including the Research Councils, HSE, Railway Safety [now Rail Safety and Research Board] and Government Departments...."²³⁷

148. RRUK receives £1.4 million of Engineering and Physical Sciences Research Council (EPSRC) funding annually which must be matched by the industry. On a wider field, the European Rail Research Advisory Council established in 2002 (on which the RRUK is represented) has led to the founding of the European Railway Research Network of Excellence covering 60 universities and research centres and which has attracted 6 million euros of EU funding over 4 years.²³⁸ The RRUK's view is that more funding might be available if the industry itself were to organise better,²³⁹ and though some maintenance and renewal firms were moderately upbeat about the current level of research, we were generally disappointed at the apparently restricted range of research and development being undertaken.²⁴⁰

149. While modest funding for rail research is available in the short term there are long term uncertainties. The result is that careers in the industry are not attractive and vital expertise may not be available. The present effort to stimulate rail research lacks focus. Rail Research UK's evidence suggests that the industry itself could do more. The SRA has not been given the direct task of co-ordinating and funding railway research. This was a mistake. One of the tasks of the body charged with industry leadership in the future must be to build on the efforts of the EPSRC to ensure that the United Kingdom has a sound research base to underpin railway developments. The Government needs to consider carefully future arrangements for the better co-ordination of rail research.

150. The key importance of making transport costs transparent was stressed by Professor Sir Frederick Holliday who said "if we do not try to make the costs transparent for every mode of transport then we are never going to have an objective appraisal of which mode to back."²⁴¹ It was suggested to us that insufficient data about the railway is

233 FOR 43

234 FOR 43

235 Ibid

236 *Directions and Guidance*, para 10

237 Ibid

238 FOR23A

239 Ibid

240 QQ 832-833

241 QQ 1030, 1035

being made available publicly by the SRA.²⁴² Professor Newbery, discussing cost benefit analysis, complained that there was not an “honest supply of statistics” for the railway.²⁴³

151. The *Directions and Guidance* provided by the Secretary of State to the SRA contains a Memorandum of Understanding on the “Collection and Publication of Data”.²⁴⁴ Mr Bowker told us that route and line specific information was available; but that he was anxious that information should be publicly withheld which “would not give anybody a competitive advantage”.²⁴⁵ He told us that “I believe the information that people do need is made available. If people do not think we are doing it they should ask; they do not.”²⁴⁶ **It may be that there are good reasons for keeping some data at aggregate level, but the presumption should be that as much as possible is made available publicly. Without full and accessible data it is impossible to conduct a sensible debate about the future shape and purpose of the railway, a debate in which there is a wide public interest.**

Working co-operatively

152. **The severe limitations of its powers and the fragmentation of the industry into competing “baronies” means that the SRA needs to work closely with other bodies to maximise its leadership influence across the industry. We highlight briefly below examples where the SRA has been sidelined, has little or no influence, or has failed – because of the fragmented structure of the industry – to cooperate effectively with another transport body. These failures are not confined to the bodies directly concerned, but have important, knock-on effects on the rail sector as a whole, and the travelling public.**

Enhancements – West Coast Main Line upgrade project

153. The SRA has a role as a chief customer for railway enhancements. However, as we have seen, its discretion is fettered by the ability of the Rail Regulator to specify Network Rail’s outputs in some detail. One example of this confusion is the West Coast Main Line upgrade project where the SRA has sought to exert control but does not have the power to do so.

154. This project is one of the most important underway currently on the railway. It was described to us by Mr Andrew McNaughton, Network Rail’s Chief Engineer, as a process of revitalising an “essentially life-expired railway”.²⁴⁷ SRA published its strategy consultation for the project on 5th September 2002, and its final strategy document nearly a year later on 16th June 2003.²⁴⁸ In our report, *Railways in the North of England*,

242 QQ 412,1032-1034

243 Q 436

244 *Directions and Guidance*, Annex D

245 QQ 1574,1575

246 Q1576

247 Q 1697. Mr McNaughton contrasted the West Coast project with that of the earlier, and more restricted, East Coast Main Line electrification project. He made clear his view that the 2 projects were not compatible.

248 *SRA West Coast Main Line Strategy*, June 2003

published later that month,²⁴⁹ we praised the SRA for appearing to have exerted control over this complex, troubled project. On 8th July, in evidence to us, Mr Bowker indicated that progress appeared to be going as planned.²⁵⁰ However, more recent developments on the project place parts of the timetable in doubt again.

155. The SRA's strategy for the project published on 16th June 2003 stated the cost as capped at £9.9 billion.²⁵¹ The SRA has told us that recent scoping and efficiency reviews have resulted in savings of around £2 billion.²⁵² The scope of the WCML upgrade is wider and more complex than the East Coast Main Line (ECML) electrification which took place in the 1980s. However, critics are right to query the substantial difference in cost per mile between the WCML - £16.68 million – and the ECML - £1.8 million – in 2000-1 prices.²⁵³ Even more telling are the comparisons with British Rail's earlier plans to upgrade the WCML; in 1990, for example, the cost was put at only £750 million, or £1.034 billion in 2000-1 prices.²⁵⁴ The SRA's published strategy document carefully defined the governance, roles and responsibilities of the respective parties in the project as follows: "specification" - SRA; "prime contractor" – Network Rail; "efficient project costs" – Rail Regulator.²⁵⁵

156. On the 24th July 2003 the Regulator and SRA issued press notices in which the former indicated that he was, "asking Network Rail to evaluate options for improving the efficiency of the West Coast route modernisation project";²⁵⁶ while the latter stressed that, "there will be no delay in delivering the strategy and its benefits for passengers and freight customers."²⁵⁷

157. On 29th October 2003 the Regulator expressed the view that the upgrade allowing 125 mph running between Liverpool and London by September 2004 might not happen.²⁵⁸ He was clear why: "The position that I have taken in relation to the west coast is that I am concerned that the work which Network Rail is doing involves a considerable amount of inefficiency and waste."²⁵⁹ When we asked Mr Bowker about this on 5th November he said that, "the strategy which everybody is working to for September 2004 is the SRA strategy and nothing else"; but, pressed, admitted that, "It is possible that September 2004 is October 2004 and that is a matter of risk."²⁶⁰ But the Regulator's comments indicate that he was not working to the SRA's strategy.

249 Transport Committee, Fourth Report of Session 2002-03, *Railways in the North of England*, HC 782-I, p 13

250 Q 237

251 SRA Press Release, 16 June 2003

252 FOR 97B

253 Transport 2000, 5 November 2003

254 Terry Gourvish, *British Rail :1974-97 From Integration to Privatisation*, Oxford, 2002, pp 307-8

255 *SRA West Cost Main Line Strategy*, Executive Summary, section 3

256 'Rail Regulator identifies substantial savings on planned rail infrastructure costs', ORR Press Release, 24 July 2003

257 'Statement: West Coast Upgrade Remains on Schedule', SRA Press Release, 24 July 2003

258 QQ 1282, 1283, 1284

259 Q1281

260 Q1522

158. On 12th December 2003 the ORR published the Rail Regulator's *Final Conclusions* on Network Rail's funding requirements in the period 2004/05 to 2008/09. On the WCML project he concluded that:

“Network Rail should be funded to deliver improved journey times between London and Glasgow and other major cities on the route such as Manchester, Birmingham and Liverpool by September 2004.... He has also concluded that there should be no delay to the further journey improvements to Liverpool and Preston, sought for June 2005, and to Cumbria and Glasgow, sought for December 2005. *Beyond these specific improvements, however, the Regulator has concluded that in order to reduce the risk of cost escalation and non-delivery, and to ensure delivery at an acceptable level of cost, it is necessary to extend the timescale for their delivery by 18 – 24 months. This effects in particular the capacity enhancement work between Rugby and Stafford on the Trent Valley route (emphasis added).*”²⁶¹

Mr Winsor reduced the allowance for Network Rail expenditure on the WCML by £640 million.²⁶²

159. On 19th December the SRA issued a press release noting the Regulator's view that the “latter stages [of the project]should be deferred by 18/24 months, a view that the SRA has consistently resisted” and stating that there was an agreement with Network Rail that there would be “no changes at all to the agreed programme of works on the ground” until the SRA had reviewed “options” for the WCML project.²⁶³ On 23rd December Mr Winsor countered, “I am aware that the SRA has consistently resisted rephasing of the outputs of the project. However, *my decision has been made and is final (emphasis added)*”.²⁶⁴

160. We are deeply concerned by the nature of the decision making process revealed by the recent events on the West Coast Main Line upgrade project. Even now there appears to be no agreement on the entirety of the project. Neither the SRA, the Rail Regulator or Network Rail seems to have power to make a final decision. The Government seems powerless to intervene. It is hard to think of a more telling example of the divided leadership of the railway and the powerlessness of the SRA.

Network Rail's decision to take over rail maintenance

161. On 24 October Network Rail announced that it was to take direct charge of rail maintenance and dispense with private sector contractors.²⁶⁵ This is a crucial change in policy. When we asked Mr Bowker about this on 5th November he said “It was a matter for Network Rail to decide, but they are a professional company and they sought the views of their senior colleagues. So, yes, it was discussed with me and I supported it.”²⁶⁶ However, shortly before, Mr McAllister, Chairman of Network Rail, had maintained

²⁶¹ ORR Access Charges Review 2003: *Final Conclusions*, p 5

²⁶² *Ibid*, p 6

²⁶³ SRA Press Release

²⁶⁴ ORR Press Release

²⁶⁵ Network Rail Press Release

²⁶⁶ Q 1482

that “this was a decision for Network Rail and we did not discuss the issue with either the SRA or the Government...It was our responsibility. We advised the Government of what we were considering and we also advised the SRA.”²⁶⁷

162. Irrespective of the exact nature of the exchanges between Network Rail and the SRA over the company’s decision to take rail maintenance in-house, it is clear that the present structure of rail governance reduced the SRA in this crucial decision to a bystander. This is yet another example of the utter impotence of the SRA.

Private sector investment

163. The SRA has placed great emphasis on private sector investment, “Rail investment strategy has at its core a substantial role for the private sector.”²⁶⁸

Rolling Stock

164. Mr Bowker told us that the “vast majority” of that investment has been in rolling stock.²⁶⁹ We examined the role of the Rolling Stock Leasing Companies (ROSCOs) in some detail in an earlier inquiry.²⁷⁰ Here we simply note that between 2001 to 2003 the private sector invested £1,488 billion in rolling stock.²⁷¹ According to the SRA “The average age of rolling stock is seen as a indicator of comfort on the railways.”²⁷² The investment has produced a decline in the average age of the rolling stock fleet (all operators) from 20.67 years to 19.35 years.²⁷³ This compares unfavourably to an average life of 16 years prior to the rolling stock leasing companies.²⁷⁴ **For a private sector investment of almost £1.5 billion since 2001/2, the average age of the UK rolling stock fleet appears to have declined by approximately 16 months only. This seems to us a rather modest achievement.**

165. The SRA published its *Rolling Stock Strategy* in December 2003 too late for us to take specific evidence on it.²⁷⁵ However, we did receive evidence on rolling stock, in particular, from the PTEs expressing their view that leasing charges were too high.²⁷⁶ The *Strategy* sets out the SRA’s position which is to encourage “an efficient and sustainable market” but which avoids imposing any detailed plan for rolling stock provision or “cascade” arrangements, “It is not appropriate for the SRA to meddle where the market does a better job.”²⁷⁷ However, that strategy also suggested that it was

267 QQ 1476,1477

268 *SRA Strategic Plan 2003*, p 13

269 Q283

270 Transport Committee, *Overcrowding on Public Transport*, paras 39 – 52

271 Transport Committee, *The Departmental Annual Report 2003*, Ev 22

272 *SRA National Rail Trends 2003 – 2004*, Quarter Two, p 47

273 Between 2000/01 (Quarter 3) and 2003/04 (Quarter 2), *Ibid*, p 47

274 Terry Gourvish, *British Rail 1974-97: From Integration to Privatisation*, Oxford, 2002, p 420. The SRA says that 4500 rolling stock vehicles have been procured by the private rolling stock market (Press Release, 19 December 2003). This compares with 3,767 under British Rail from 1984 to 1994 (Gourvish, *op cit*, pp 219, 308)

275 ‘Future of Rolling Stock Lies in the Private Sector’, SRA Press Release, 19 December 2003

276 FOR 62

277 ‘Future of Rolling Stock Lies in the Private Sector’, SRA Press Release, 19 December 2003

unclear that the market was doing an entirely perfect job. It noted “there are a number of factors that suggest that the ROSCOs may well enjoy a degree of market power, in some cases quite a high degree, in relation to the negotiation of leases for existing stock” and that “over the next few years, when the majority of transactions are likely to involve the re-leasing of existing stock...competition is often unlikely to be strong.”²⁷⁸ The SRA has said that it “will advise TOCs and franchise bidders if it perceives that proposed lease prices and terms do not constitute good value for money, while protecting the commercial confidentiality of prices agreed between TOCs and ROSCOs.”²⁷⁹ **We wish to stress that it is essential that the ROSCOs do not receive more than a reasonable return, and that their market power does not lead to abuse. The cost of excessive returns for the ROSCOs is less money for the railway. We are concerned that the market may not be acting appropriately to provide rolling stock at economic cost; and that the SRA’s rolling stock strategy may have missed an opportunity to rationalise rolling stock requirements.**

Funding by ‘Special Purpose Vehicles’

166. The SRA was also keen to bring in private sector money from so-called “Special Purpose Vehicles” (SPVs) – privately-financed companies established to finance and build major railway enhancement projects. While the Department for Transport has said that there is some prospect of an SPV for the East London Line Extension later in the year,²⁸⁰ firm plans have yet to materialise. When giving evidence to us on the Department’s Annual Report, the Secretary of State for Transport claimed that the Channel Tunnel Rail Link was an SPV,²⁸¹ although that project was put in place before the policy on SPVs was announced,²⁸² and is underwritten by the taxpayer with more financial risk recently transferred to the public sector. While the private sector has indeed participated in this project, we have already noted recently that ultimately the Government needed, in effect, to guarantee its cash flow.²⁸³

167. We tried, but failed, to identify private sector investment which is neither rolling stock, nor infrastructure funded by Network Rail. The Department for Transport has told us that such investment has been made in “plant and machinery” but that details are not available for reasons of “commercial confidentiality”.²⁸⁴ **It is clear that the policy of Special Purpose Vehicles has failed to attract private sector investment into the industry as originally intended. The SRA can only bring in private sector money if it has suitable projects and, we suspect, if the public bear most, if not all, of the risk.**

278 SRA Rolling Stock Strategy, paras 7.6,7.7

279 Ibid, para 7.10

280 Transport Committee, *The Departmental Annual Report 2003*

281 Ibid, Ev 3

282 FOR 77

283 Transport Committee, *The Departmental Annual Report 2003*, paras 44-51

284 FOR 77B

Stakeholders

Passenger Transport Authorities

168. The fragmentation of the railway means that it is vital for the SRA to work well with stakeholders. It does not appear able to do this. In our report *Railways in the North of England*²⁸⁵ we deplored the SRA's poor relationship with local stakeholders.²⁸⁶ In July Mr Bowker had told us of the efforts he had been making to involve stakeholders, including forming a "regional team" in the SRA to be the 'focus point' for consultation.²⁸⁷

169. It was disappointing to learn from the Passenger Transport Executives later in the year that, while relationships with the SRA were better, concerns remained. The guarded judgment of Mr Roy Wicks, Director-General, South Yorkshire PTE, speaking for the PTE Group in November, that the SRA are "listening more and are working much harder with PTEs and the local authorities"²⁸⁸ was radically different from the up-beat view of Mr Bowker earlier in the year that "Our relationship with the PTEs is really good."²⁸⁹

170. In part, this concern of the PTEs was rooted in a deep mistrust of SRA policies, for example, the SRA's *Specification of Network Outputs* strategy which the PTEs saw as 'naïve, simplistic and arbitrary'.²⁹⁰ **The PTEs' discontent was not rooted in any unwillingness to work with the SRA, but was the result of what they saw as structural flaws in the rail industry which resulted in a mismatch of objectives between franchises and local transport plans as in the case of the Northern franchise.**²⁹¹ The Passenger Transport Executives saw two roles in the rail industry, "setting policy" and "delivering."²⁹² **They considered that because the operations of Network Rail were funded by the SRA, directly through grants or by subsidy to train operating companies which fed through to Network Rail, consideration should be given to drawing the responsibility for delivering train operations and infrastructure together under one organisation.**²⁹³

Merseyside

171. Where the SRA does make an effort to co-operate with local stakeholders the results can be promising, though even here vigorous follow up action seems lacking. We were told about the unique experiment with the train operating company Merseyrail Electrics involving the local Passenger Transport Authority and Executive (Merseytravel) and

285 HC 782-1

286 Ibid, para 57

287 Q244

288 Q1142

289 Q354

290 Q1144

291 Q1143

292 Q1147

293 Q1151

SERCO/NedRailways in a 25 year long franchise, in which the franchise specification has been devolved by the SRA to the PTE and the franchisee is seeking to operate on the basis of the “whole journey”, passenger-focused approach of the Dutch Railways.²⁹⁴ The “whole journey” approach includes, for example, a so-called “clockface” or regular interval timetable, a focus on cleanliness, safety and convenience for passengers within the station environments operated by the company, a co-ordinated approach with other transport modes, and is also similar to the transport approach presented to us by Jonathan Tyler of Passenger Transport Networks reflecting the experience of the railways in Switzerland.²⁹⁵ Mr Scales, Director-General, Merseytravel, identified integration as one main advantage of the new arrangements, “We do not have to go 200 miles down to London to get a decision; it is all done in Merseyside. It is local solutions to local issues by local people.”²⁹⁶

172. The emphasis here is on strong partnership with other operators, the local authority, the British Transport Police and the PTE which seeks to go beyond the basic fulfilment of contractual obligations.²⁹⁷ For example, the company maintains its own rolling stock; and is developing its relationship with Network Rail to seek operational integrations that approach “vertical integration” in order to improve Public Performance Measure (PPM) results. The results achieved for passengers by the Merseyrail operation since its start on 20 July 2003 so far appear promising with a PPM for the period July - September 2003 of 94.2%.²⁹⁸

173. A “high level” SRA objective is to contribute to the development of integrated transport, and the Secretary of State’s *Directions and Guidance* to the SRA enjoin it to give weight to measures to improve “door to door” journeys when examining franchise proposals.²⁹⁹ **While the SRA is to be commended for facilitating the Merseyside arrangements by relinquishing the specification for the franchise to the PTE, we are worried and puzzled that the SRA indicated in a press release that this interesting example of local, public/private partnership initiative in Merseyside, was something which could not readily be repeated.**³⁰⁰ We accept that the nature of the Merseyside franchise area makes it an obvious candidate for devolution of rail services. But the SRA’s position on closing the door to the approach adopted here appears highly unimaginative. We hope that the Government – in line with the reference in Mr Darling’s Statement of 19 January to seeking devolution of rail to PTEs – will ensure, wherever possible and with appropriate local adjustments, that the arrangements in Merseyside can be repeated not only with the PTEs, but wherever they appear workable. More generally, we think that there are lessons to be learned by all franchisees in the absolute focus on passenger service which lies at the centre of this operation. Any

294 Q1070; FOR 114

295 FOR 84

296 Q1157

297 FOR114

298 *SRA National Rail Trends 2003-2004* (Quarter Two), Table 2.1b, page 16. This represents increase of .5 over the corresponding quarter in 2002 when the operation was under a different franchisee and is the second best result on the entire network. The average for Quarter 2 for all ‘Regional operators’ (such as Merseyrail) was 83.8%, *ibid*, pp 15-16

299 Ev SRA supp letter of 19 January 2004

300 SRA Press Release, 31 January 2002

devolution of rail to the PTEs should also ensure financial flexibility and the possibility of modal change.

Controlling costs

174. The SRA is the conduit through which Government investment in the railway flows. Its purchasing power should help it achieve its strategic objectives. As the SRA itself notes, costs are rising more quickly than performance:

“The total cost that Railtrack/Network Rail and passenger and freight operators incur to provide the national train service has risen from £6.1 billion in 1999-00 to a projected £9 billion in 2002-03. But this increase is not being matched by equivalent growth in revenues. The consequence is a financial imbalance which the measures set out in this Strategic Plan are designed to put right....The operating surplus/deficit ...has declined from a small deficit in 1999-00 to an estimated deficit of £1.5 billion in 2002-03....”³⁰¹

175. The *Strategic Plan 2003* spells out that these increasing costs place projects at risk, and put the Governments targets for rail in doubt.³⁰² This is bad enough, but it is clear that the reasons for these cost increases are not understood precisely by the SRA, “A better understanding of the causes of the cost pressures is needed to distinguish those arising from providing improved outputs and those arising from inefficiency.” The SRA state that the reasons for cost escalation were “*believed* to include increased safety and quality standards, rising staff costs, a more conservative approach to managing the infrastructure and the overall growth in train mileage...(emphasis added).”³⁰³ Even the responsibility for arriving at such an understanding is not the SRA’s: “This is a key issue in the Interim Review which the Rail Regulator is undertaking working closely with Network Rail and the SRA. The SRA cannot pre-judge its outcome.”³⁰⁴

176. Even though the areas in which costs appear to be rising are not under SRA control, an intelligent customer should have a grasp of where savings can be made. **Even though there remains some confusion in the SRA about the causes of the cost escalation in the railway, it is clear that the greatest increase is in the cost of rail infrastructure. As we have pointed out earlier, this is presently the responsibility of Network Rail and the Regulator, and the SRA has no direct control.**

Conclusion - vision, structure, and leadership

177. **In order to provide coherence and morale for the industry, the SRA needed to articulate a clear vision for the railway of the 21st century and the goals needed to achieve that vision. This vision required to be sufficiently broad to be shared by the travelling public and the Government, and precise enough to energise and inform the operational work of the railways. The SRA also needed to take account of, and lead, the**

301 *SRA Strategic Plan 2003*, p 36

302 *Ibid*, p 36

303 *SRA Strategic Plan 2003*, p 36

304 *SRA Strategic Plan 2003*, p 36

debate about the nature of rail that our work uncovered. Has the SRA led that debate? Does the SRA have a vision for the railway?

178. There is wide and vigorous debate taking place about the future of the railway and this was reflected in the evidence submitted to us. For example, Dr Tim Leunig of the London School of Economics was critical of the degree of subsidy which the railway attracted and was prepared to contemplate a much smaller railway with higher passenger charges.³⁰⁵ Professor Newbery argued that there had been a “massive misallocation” of investment in rail based on over estimates of demand and underestimates of costs.³⁰⁶ In contrast, Jonathan Tyler laid emphasis on the social potential of the railway “as an underpinning of a civilised way of life”.³⁰⁷ Chris Nash, Professor of Transport Economics, University of Leeds, also argued that the economics of traffic density provided a case for rail subsidies, and stressed that the growth of rail depended upon improved quality of service and additional capacity.³⁰⁸ Professor Phil Goodwin of the Centre for Transport Studies, University College, London, pointed to the buoyancy of railway demand against a backdrop of press hostility; the fundamental changes road charging policies would be likely to have on the economics of the railway – including a larger role for rail; and the absence of any work “which projects forward a dynamic, long term view of the interactions of supply and demand, road and rail, in a timescale in which road pricing would interact with rail demand.”³⁰⁹ We had evidence of the environmental case to be made for rail from English Nature and Professor Sir Frederick Holliday, though English Nature pointed to the need for more research;³¹⁰ and from Dr Leunig on the relationship between relative environmental benefits and passenger densities.³¹¹ **We found little evidence of the SRA leading the debate in the development of new thinking about the railway, or even engaging fully with many who are contributing to that debate.**

179. Mark Casson, Professor of Economics at the University of Reading said that “When you look at the SRA’s view of what the railway system will be in 20 years’ time, there is no view at all. In other words it is very much authority now to sort out problems, but not much strategy in terms of long-term thinking”,³¹² which summarises the opinion of many who talked to us. **That we should have found no strong, organising vision for the railways is depressing but, in the light of the evidence we received, not surprising. The SRA was set up to provide leadership through strategy direction – in other words, to provide this vision. On the evidence received in this inquiry it simply does not have the power to do so.**

180. Last July Mr Bowker told us “It is not necessary in any circumstances to have to be able to direct somebody as to what to do in order to achieve a desired result. That is the

305 Q 427

306 QQ 396, 436

307 Q 443

308 FOR 23

309 Professor Phil Goodwin, ‘What Future For Rail in the Ten Year Plan For Transport?’, *Report to the All Party Parliamentary Rail Group*, November 2003, p 29

310 FOR 21A

311 Q 412

312 Q 417

lesson of every other industry”;³¹³ and last November he said: “I believe that the industry we have is now capable of operating efficiently. I have never really held the view that structure is the primary cause. People, management, and process is what is needed to be fixed.”³¹⁴

181. We agree that successful leaders need not, and indeed, usually cannot, control everything. But the leader needs to be able to control *some* significant part of his organisation. **The SRA does not control the day to day activities of franchisees; the infrastructure; the contracts by which companies get access to that infrastructure, the resources that are put into that infrastructure; or the measures to ensure the safety of the industry and the travelling public. All it controls directly is the letting and monitoring of franchises, and the giving of various grants.**

182. It is clear to us that the SRA does not have the powers and responsibilities to provide it with the commanding position of leadership that the industry requires, and to drive through the improvement in rail operating performance which the Government and the travelling public are entitled to expect. Consequently the SRA has failed to provide the scale of improvements which it was set up to deliver. Mr Bowker’s assertion that the railway is structurally sound is unfounded. Restructuring the railway to enable output specification and control over the means of delivering infrastructure improvements to be exercised within a single management structure should be the core of the new arrangements for the railway, as we discuss in more detail in Chapter 6. Structures emphatically do matter. “People, management and process” do not exist in a vacuum. A rational framework for the railway is required which allows the industry to work together to improve railway services for passengers.

313 Q 257

314 Q 1487

5 Safety

Regulation

183. The enforcement of the safety legislation applying to the railway is the responsibility of Her Majesty's Railway Inspectorate (HMRI) within the Health and Safety Executive (HSE), the executive arm of the Health and Safety Commission (HSC). The HSC regulates safety on the railways using the provisions of the Health and Safety at Work Act 1974 together with a variety of specific rail regulations set out as secondary legislation. The HMRI is independent of the railway industry. Other organisations, such as the British Transport Police, the Crown Prosecution Service, and the new Rail Accident Investigation Branch (RAIB),³¹⁵ may also become involved in rail safety when accidents occur. When operational, the RAIB will have responsibility for investigating serious rail accidents, but will have no powers of prosecution.

184. The Rail Safety and Standards Board, a body owned by the railway industry, is responsible for rail safety research, a wide range of industry standards, and leading the industry to improvements in health and safety performance.³¹⁶ The Board is not involved directly in the safety regulation of the railways, but as the industry "leader" on safety, works closely with the HSE.

Safety record

185. Rail travel is comparatively safe and is becoming progressively safer,³¹⁷ as shown in the following graph:

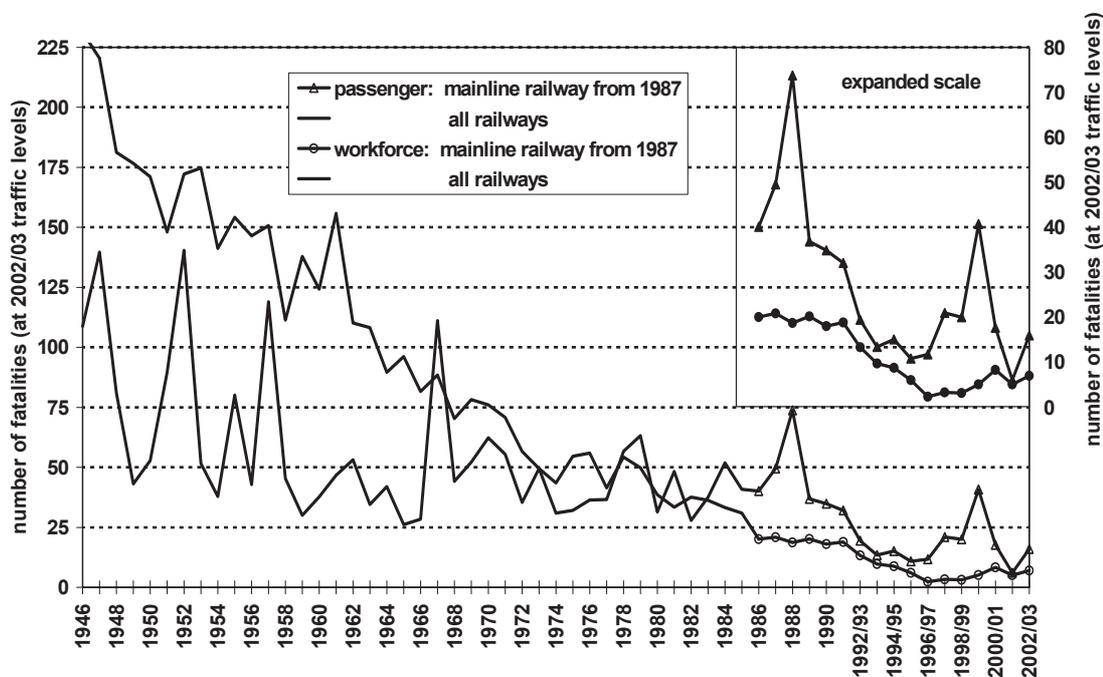
315 The establishment of an independent body to investigate railway accidents was a recommendation of Lord Cullen, *The Ladbroke Grove Rail Inquiry, Part 2 Report*, recommendations 57-73, pp 177-179. The Railways and Transport Safety Act 2003 provided the statutory foundation for the Rail Accident Investigation Branch.

316 The establishment of the RSSB is the product of recommendations by Lord Cullen's inquiry, *Ladbroke Grove Rail Inquiry, Part 2 Report*, recommendations 40-56, pp 175-177. It was established on 1 April 2003, *ORR Annual Report 2002-2003*, p 19

317 FOR 77

Chart 2

Passenger and Workforce Fatality Rates since 1946



Source: Based on HMRI Annual Report data for all railways, adjusted by the RSSB to remove non-mainline railway multi-fatalities, and normalised by current train miles. From 1987 HMRI data is for mainline railway only, ie BR/Network Rail/TOCs. NB 2002/03 figure is estimated on HMRI basis.

Source: Network Rail

186. The figures comparing road and rail fatalities are telling. In 2002, 3,431 people were killed on the roads;³¹⁸ while according to the HSE “a total of 50 passengers, railway staff and other members of the public” were fatally injured and 256 people who died as a result of trespass and suicide on the railway.³¹⁹ The SRA points out that “On average more road users die in accidents each day than rail passengers in a year.”³²⁰ There will always be dangers on the railways. The recent tragic death of four railway workers in Cumbria on the 15 February 2004 is evidence of that.³²¹ It remains the case, however, that for the public the railway is an extremely safe way to travel.

Criticism

187. During this inquiry we received a number of informed criticisms of rail safety matters and the Health and Safety Executive (HSE), the rail safety regulator. Mr Alan Osborne, who recently left the HSE as Director of Rail Safety after less than one year in post, considered that safety standards were being “gold plated” because the criterion for balancing risks and costs (“reasonable practicability”) was imprecise and was being

318 National Statistics, *Transport Statistics Great Britain 2003*, Table 4.15

319 Health and Safety Executive, *Railway Safety 2002-03*, sections, ‘Incidents involving passengers, staff and members of the public’ and ‘Trespass and vandalism (or route crime)’, no pagination

320 *Everyone’s Railway, the wider case for rail*, p 7

321 ‘Runaway wagon kills rail workers’, *BBC News On Line*, 15 February 2004

applied inconsistently which, he felt, could lead to inappropriately high costs when applying safety measures;³²² that the rail expertise of the HMRI was being seriously diluted;³²³ that poor communication by HSE with the rail industry had led to ignorance about its function and it being held in low esteem by rail “stakeholders”; and there was an inappropriate split between the rail policy and operations branches of the HSE. Mr Osborne considered that the regulation of rail safety should be removed from the HSE; and that an exclusive, legal regulatory framework was required specifically for rail.³²⁴

188. Network Rail had criticisms of the present safety arrangements, including the inappropriate classification of the industry by the HSE as a “major hazard” industry with the offshore oil, chemical and nuclear industries which, in its view, has contributed to its insurance costs rising fourfold. It considered that the rail safety and standards framework as a whole should be reviewed to ensure consistency and cost effectiveness because of the complexity of the regulations and the number of organisations involved; and that the threat of prosecution in the aftermath of accidents has induced a culture of ‘risk aversion’ in the industry.

Costs

189. When Dr Kim Howells, the Minister of Transport, gave evidence to us, he pointed out that 100% safety on the railway was not possible.³²⁵ While it was vital that the travelling public should have complete confidence in the railway’s ability to deliver them safely to their destination, the costs of achieving almost complete safety were problematic:

“...when perhaps the final increments towards that target of 100% rail system become fantastically expensive and it is at that point you have to ask, I guess, is it worth spending that much more money in terms of the perceived risk, and those are not easy decisions to make.”³²⁶

190. While the HSE,³²⁷ Network Rail,³²⁸ and the RSSB,³²⁹ could readily tell us their administrative budgets for rail safety, no one could provide us with a sum totalling the cost of safety to the industry as a whole. In Network Rail’s case this was because “the needs of safety arise in every activity we carry out as a company”.³³⁰ We asked the Secretary of State for Transport who said “It is difficult to put a precise figure on it....Frankly, safety should be in with the bricks”.³³¹ In the absence of a credible overall

322 Definitional problems also highlighted by the Chief Executive of the RSSB, Q1799

323 FOR 124. Lord Cullen was concerned that the railway inspectorate should have sufficient numbers with rail expertise, *The Ladbroke Grove Rail Inquiry, Part 2 Report*, para 9.55. Evidence received from the HSE was that at December 2003, of 123 railway inspectors ‘55 were Railway Specialist Inspectors, paid a premium for their railway knowledge and experience.’ FOR 122B

324 FOR 124

325 Q1649

326 Q1650

327 FOR 122A

328 FOR 57C

329 Q1811

330 FOR 57A

331 Transport Committee, *The Departmental Annual Report 2003*, Ev 4.

figure for the costs of rail safety - which may be extremely difficult to arrive at - it is impossible to conclude that safety on the railways as a whole may be costing too much, or that insufficient is being spent. This does not mean that judgements on the cost effectiveness of particular projects are not possible. However, we have received evidence that the HSE has caused unnecessary extra cost by “gold-plating”.

“Gold plating”

191. While the HSE was adamant that it was not applying an unreasonably high standard of safety,³³² we did receive allegations of rail safety standards being “gold plated” on projects as a result of the unclear criterion for balancing risks and costs, and the fear of prosecution (‘risk aversion’).³³³

Updating standards

192. We were astonished to hear from Mr Osborne that one cause of inappropriate standards being applied resulted from a decision on the part of the HSE’s Director-General to “put on hold” the updating of Railway Safety Principles and Guidance documents with the result that standards applied by the Railway Inspectorate appeared not to have undergone proper risk assessment. The reason for the delay was, apparently, internal HSE budgetary considerations.³³⁴

193. All safety standards applied by the HSE must be constantly updated and be the result of proper and rigorous risk assessment. Unless this is carried out the HSE’s service to its railway customers will be unacceptably diminished. It is also completely unacceptable that the industry should risk incurring huge costs for inappropriate safety measures because of relatively small budgetary considerations in the HSE. Where such costs are incurred there will be an inevitable knock-on to the travelling public who are therefore made to bear at least a part of the costs of the safety regulator’s poor practice.

194. Mr Osborne provided several instances of “gold plating” in supplementary evidence, for example, automatic level crossings which are the most expensive in the world; Train Protection Warning System (discussed below); and an inflexible approach to permitting selective door opening on trains which are longer than the platforms serving them.³³⁵ Mr Osborne indicated that he had intervened to change the HSE’s ‘fairly aggressive’ policy of seeking “very expensive” platform alterations in the longer term so that selective door opening was acceptable. He pointed out that the prospect of these expensive alterations had placed new train services at risk because the train operating companies balked at the costs, thereby risking the economic viability of services. Two particular instances of “gold plating” cases give us cause for concern.

332 FOR 122B

333 FOR 124; FOR 57A

334 FOR 124

335 FOR 124B

“Major hazard”

195. When we asked HSE about its classification of the railway as a “major hazard” industry, Dr Sefton, Director of Rail Safety at the HSE, appeared to down-play the classification by stating that “The truth of the matter is that this is simply a shorthand that is used within HSE.”³³⁶ In the HSC’s Annual Report 2002/3, however, rail features in a section entitled ‘Major Hazard Industries’ alongside the nuclear, offshore petroleum, gas conveyance, and mining industries.³³⁷ It is clear to us that HSE’s classification of the railway as a “major hazard industry” is rather more than simple “shorthand”.

196. Network Rail told us that this classification was inappropriate in the light of the safety record of the industry and had an adverse effect upon its insurance premiums which have increased from £20 million to £100 million per annum.³³⁸ Mr Osborne believes that the relevant benchmarks for rail are other transport modes, not separate industries,³³⁹ and instanced the Potters Bar accident where the HSE investigation had been led by a nuclear industry expert whose recommendations appeared to him inappropriate.³⁴⁰ Mr Len Porter, Chief Executive of the Rail Safety and Standards Board, was not more sympathetic to the present classification “if you want to class the rail industry...as a ‘high hazard industry’, then you would have to class the highways as ‘high hazard’ in terms of carrying hazards loads.”³⁴¹

197. We probed Dr Sefton about bracketing a rail accident in the UK which, at worst, might involve hundreds of people but was more likely to involve many less, with a major nuclear or chemical accident which would almost certainly involve many thousands, or more. He indicated that the characteristics of major hazard industries were, the rarity of accidents coupled with the scope of the result when such accidents occur, affecting “considerable numbers of people in exactly the same way that a serious train crash would.”³⁴² We asked if the HSE had received representations on the classification point from Network Rail. Dr Sefton was clear that “nobody has come to me and said, ‘Will you stop referring to us as a major hazard industry?’”³⁴³ However, we received supplementary evidence from Network Rail that its concern about this had been raised “directly” with representatives of the HSC and the HSE in different forums such as the Rail Industry Advisory Committee and the Safety Advisory Committee.³⁴⁴ **It is extremely disappointing that Network Rail’s representations on the inappropriateness of designating the industry as a ‘major hazard’ appear not to have been brought to the attention of the current HSE Director of Rail Safety.**

336 Q1753

337 Health and Safety Commission, ‘Delivering Health and Safety in Great Britain’, *Health and Safety Commission Annual Report and the Health and Safety Commission/Executive Accounts 2002/03*, Table 9, p 36

338 FOR 57A

339 Q1862

340 ‘the fundamental point was it was an example of nuclear standards being put into the railway.’ Q1879

341 Q1758

342 Q1789

343 Q1755

344 FOR 57C

198. We do not accept that parallels exist between the rail, nuclear and chemical industries. We certainly do not underestimate the extremely serious consequences of any train accident; but the scale of nuclear and chemical accidents is not likely to be similar to those on the railway. In our view, this places in doubt HSE’s designation of the railway as a “major hazard” industry which we think could result in a “gold plated” approach being taken to rail safety. The HSE needs urgently to rethink its approach to the classification of rail as a “major hazard” industry and generally to adopt a more nuanced, railway-specific approach to such matters.

Train Protection Warning System

199. Installation of the Train Protection Warning System (TPWS), a safety system designed to stop trains at speeds of up to 75 mph, was completed throughout the UK network at the end of 2003.³⁴⁵ Mr Armitt, Chief Executive of Network Rail, told us that the cost of TPWS was £575 million.³⁴⁶ He said that. “the original proposal would have saved approximately 60 lives over 25 years and the consequence of what we have done, the full implementation, is 65 lives over 25 years. The extra five lives have cost the difference between £190 million, which was the original estimate, and £575 million [i.e. £385 million].”³⁴⁷

200. The original cost of the project escalated.³⁴⁸ Dr Sefton denied that this was as a result of any additional HSE requirement over those to which Railtrack had agreed (“though there remained some areas of technical contention where it disagreed with the HSE”).³⁴⁹ However, Mr Osborne, who was directly involved with the TPWS installation during his period as Director of Rail Safety, was quite clear:

“HSE directly caused through the Railway Safety Regulation 1999 (and through their further interpretation) the blanket fitment of TPWS to all signals controlling conflicting moves regardless of risk. This resulted in fitment of 40% of signals increasing the cost by some 30%....There was a mindset within HSE that any cost saved must be ploughed back into additional safety features demonstrating that HSE’s motivation is to continue to ratchet up safety standards without a full understanding of risk and when something is safe enough.”³⁵⁰

Mr Osborne influenced the granting by the HSE of exemptions to fit TPWS, but this did not prevent ‘significant costs’ being incurred.³⁵¹

201. We are not convinced that the HSE’s approach to TPWS demonstrated a reasonable balance of costs and safety. Further, we were appalled to see so profound a

345 Network Rail/Association of Train Operation Companies, Press Release, 29 December 2003

346 Q1685

347 Q1690. The value of the lives saved, on these figures, appear in excess of the present £1.24 million ‘value of preventing a fatality’ which the HSE indicated to us is used when estimating the costs and benefits ‘in assessing safety measures against risks.’ FOR 122

348 FOR 122A

349 FOR 122

350 FOR 124B

351 FOR 124B

disagreement between Network Rail and the HSE over the extent of the TPWS system to be fitted on the network.

202. It is vital that the Government, the rail industry and the HSE learn lessons from this episode if the spectacle of such disagreements are not to weaken public confidence in the safety regulation of the industry. There needs to be much closer collaboration between the safety regulator and the industry to ensure consensus on the relative costs and benefits of rail safety systems so that demonstrable and significant safety gains are made for the travelling public and value for money can be achieved .

Safety research

203. The Rail Safety and Standards Board, the industry leader on safety matters, railway standards, and rail safety research, is nevertheless funded by the Strategic Rail Authority via Network Rail until 2006. The Government made £76 million available after the Ladbroke Grove accident to spend on rail safety research over 5 years, and the Board has stewardship of that sum.³⁵² Thereafter, we were told, funding will be the industry's responsibility.³⁵³

204. We asked Mr Porter whether the HSE, as safety regulator, might not undertake the work of the Board too. He thought not, pointing out that “We are a member driven body and the HSE is very much a regulator.”³⁵⁴ It was our impression nevertheless that more could be done to co-ordinate the work of the Board and the HSE in the field of rail safety research. **The Government funds rail safety research but, in effect, hands the money over to the rail industry to spend. We think that the Government needs to examine the use that is being made of such research funding against the overall objectives for rail safety to ensure that these sums are being put to best use. For example, we wondered why the function of rail safety research could not be taken into the Railway Inspectorate and those sums administered directly in order to promote research which would then inform policy directly for improving rail safety regulation.**

205. We were also told of the Board's work to review Railway Group Standards³⁵⁵ “alongside Network Rail standards and indeed the European technical standards for inter-operability”.³⁵⁶ Dr Sefton said that the standards were “difficult to comply with” and that they proved a “barrier for many people in the industry to getting on with their job.”³⁵⁷ The rationalisation of the numerous railway technical standards is an important initiative. Lord Cullen considered that maintaining distance between the safety regulator and the those setting industry standards was important to maintain the integrity of the regulator's independence and also to prevent standards becoming prescriptive “detailed

352 Q1812

353 Q1808

354 Q1815

355 The ‘Standards’ are defined by the Board as ‘Technical and operational documents whose objective is to provide a framework for system safety and safe interworking....’ Failure to comply with the ‘Standards’ is ‘potentially a criminal offence’ as this could involve breaches of the Railways (Safety Case) Regulations 2000, see, <http://www.railsafety.org.uk>

356 Q1750

357 Q1752

regulations” rather than “goal setting in nature”.³⁵⁸ We are not in a position to say definitely whether more could be done to further the rationalisation of Railway Standards were the responsibility for these to be taken up by the safety regulator. However, it appears that railway standards may have become over-complex and rigid and that further streamlining is necessary. We would expect the Government’s present review of the railway’s structure to address this issue.

Conclusion

206. **The highly disturbing evidence of our inquiry is that the rail industry’s confidence in the HSE is at a low ebb.** The industry considers that the HSE does not understand the railway business it is seeking to regulate and may be inflating the costs of safety at a time when the evidence is that rail is a safe mode of travel, and has been getting safer. We were told that the HSE is unimaginative in overhauling its approach to risk in the light of historically low risk levels on the railways, and is institutionally complacent about improving its internal procedures.³⁵⁹ Mr Alan Osborne expressed fears that unless safety costs take full account of the economic circumstances of the railway, then its continued viability may be in doubt.³⁶⁰

207. Lord Cullen’s inquiry into the Ladbroke Grove accident called for “a person of outstanding managerial ability, not necessarily with a railway background” to head Her Majesty’s Railway Inspectorate.³⁶¹ **It is a matter of profound concern to us that the person appointed to the key post of Director of Rail Safety, leading the Inspectorate in the HSE, left his post after less than a year with the clear perception that the HSE’s regulation of the railway industry was so flawed as to require it to relinquish its responsibility.**

208. We heard of fears that the already complex mass of safety regulation, and overlapping interests of various bodies, would be compounded by the imposition of a European safety regime and a European Rail Agency. The evidence of the HSE sought to be reassuring about this,³⁶² but that message appeared to carry little reassurance to the industry.³⁶³ Astonishingly, we were told the HSE’s own research suggested that industry stakeholders are poorly informed about its roles and responsibilities,³⁶⁴ calling into question its ability to communicate effectively with the industry. This is a disturbing picture of a dysfunctional safety regulator.

209. **Safety measures must take proper account of the ability of the industry to pay for them, and be clearly proportionate to the risk. The justification for such measures must be based on cost benefit analysis principles that are agreed across the industry, and such calculations need to be shared between the relevant bodies. Benchmarking to establish best practice needs to be extended to other transport modes, and not only to apparently**

358 *The Ladbroke Grove Rail Inquiry, Part 2 Report*, paras 9.44-9.45

359 FOR 42A

360 FOR 124A

361 *The Ladbroke Grove Rail Inquiry, Part 2 Report*, recommendation, 36, p 175

362 FOR 122

363 FOR 57; FOR 42A

364 FOR 124

inappropriate comparators such as the nuclear industry. It is apparent that the HSE has lost the confidence of the industry. It should be a priority for the Government's review of the railways to consider whether Her Majesty's Railway Inspectorate should be removed from the HSE and either made an independent Agency of the Department for Transport, or merged with the new unified rail delivery body we propose in the final Chapter.

6 The Future of the Railway

Present confusion

210. The present confused and fragmented state of the railway meant that we found no satisfactory answers to the four questions with which we started. However, our inquiry has enabled us to be confident about changes that will be required to ensure the future of rail.

211. The current railway structure blurs responsibility for policy and railway services and is not fit for purpose. Rail policy can never be divorced from decisions about overall public expenditure which are the responsibility of Government. The Government's function of adjudicating on the public interest has been passed to the Regulator who acts as a "proxy for the public interest". The Government is presently compelled to carry out his funding decisions; Network Rail is required to carry forward and manage the operational consequences of his financial planning; the SRA has struggled to determine railway outputs because the Regulator has effective control over the infrastructure. In addition, however well advised, the Regulator is ultimately not professionally equipped to take detailed operational and managerial decisions about the railway. Our evidence has shown in detail how this present rail structure, far from focussing the various parts of the railway as a whole on improving services to the passenger, has meant that valuable energy has been diverted to intra-industry squabbling and "buck-passing", while co-operative moves by the various rail bodies governing the industry have had little or no demonstrable effect upon improving performance.

212. Further restructuring of the railway will be disruptive. Nevertheless, we cannot see how the railway can ever be made to work significantly more effectively and transparently under present conditions. It is imperative that the Government uses the review of the railways announced on 19 January 2004 to address these fundamental problems. A model of railway governance is required which restores to the Government control over the public interest, public expenditure, rail policy, and objective setting; while allowing the railway industry full operational responsibility for the delivery of improved infrastructure, train service outputs and strategy objectives.

Focussed economic regulation

213. One of the most negative aspects of the present railway governance arrangements is the Rail Regulator's autonomy and its undermining of the SRA's strategic role. When we asked Mr Winsor why the accountability of Network Rail is stronger with an unelected regulator than under ministerial control he said:

"It is stronger because the powers of the Regulator are much more precise and reach far more areas of the activities of the industry than ever did the powers of any elected minister. Under the days of nationalisation, ministers could usually hire and fire the board and give general directions to the board of a nationalised authority. I believe that the cases in which general directions were given could be counted on the fingers of one hand. It has been told to me by senior civil servants that general directions were never given because they were not quite sure how general they would need to

be. Independent economic regulation of the railways is much more precise in many other respects than ever was the power of a minister. For example, in relation to the financial framework of the industry, in relation to asset stewardship, in relation to the allocation of capacity, the abuse of monopoly power, anti- competitive practices and much else besides.”³⁶⁵

214. **However, the success of the present regulatory regime in fundamental aspects of controlling costs, laying down strong incentives, providing for secure knowledge of the industry’s assets, quantifying investment arising from it, and working well with other railway bodies under Government guidance, has been abysmally poor. It did nothing to prevent the appalling débâcle of Railtrack when the railway came close to collapse. The costs of the industry have still to be brought under control. In addition, as we have demonstrated, it is the Government and not the Rail Regulator which guarantees the railway and the private investment. Finally, the Regulator appears to have extended his role in setting track access charges into the forward management of Network Rail’s business – something that was surely never envisaged to be a part of his function – thus subverting the proper function of that management and risking a further confusion of roles.**

215. It is unlikely that the Government will wish to be involved in running railway operations directly.³⁶⁶ But regulation by the Government is not the only alternative to the present regime. Other railway networks have regulatory regimes which do not involve governments losing so substantial an amount of control of railway funding. We looked, for example, at regulation on the Dutch Railways, where the equivalent Dutch regulatory body appears to have more limited room for manoeuvre, for example, the Dutch Government sets the infrastructure operator’s budget.³⁶⁷ Even if experience were to show that direct public sector train operation was effective in certain circumstances, some private train operating companies have performed well. **It is difficult to envisage a situation in which the private sector will not be involved in providing some train and railway services and will not need to negotiate a range of contracts with a unified infrastructure provider. In those circumstances, the role of an independent regulator will be required. The question is, what will that role comprise?**

216. In 1998, the Environment, Transport and Regional Affairs Committee, reviewing the prospect for a new Strategic Rail Authority, and the potential for entanglement with the responsibilities of the Rail Regulator, expressed its concern.³⁶⁸ It recommended a reduced role for the Regulator “umpiring contracts and fair competition issues with a heavily reduced staff”; and considered that “restoring the original requirement in section 4 of the Railways Act 1993 for the Regulator to take into account guidance by the Secretary of State” would provide an adequate safeguard. That requirement was restored

365 Q1252. While Mr Winsor’s picture of Ministerial regulation may have been true of the 1960’s and 1970s, by the 1980s control was much tighter, for example, public service obligation reductions in November 1979, March 1980, October 1983, October 1986, March 1988; and detailed requirements for individual BR businesses in March 1980, June 1981, October 1983, August 1984; culminating in a very detailed set of obligations in December 1989 and March 1993. Terry Gourvish, *British Rail 1974 – 97: From Integration to Privatisation*, Oxford, 2002, pp 108, 267, 268

366 The Secretary of State has said, ‘Of course no Government Department can or should attempt to operate the railways...’ HC Deb 19 January 2004, col 1078

367 FOR 91A

368 Environment, Transport and Regional Affairs Committee, Third Report of Session 1997-98, *The Proposed Strategic Rail Authority and Railway Regulation*, HC 286-I, para 140

by the Transport Act 2000 which includes a provision for the Secretary of State to give the Regulator guidance,³⁶⁹ but, as we have shown in this inquiry, this appears to have been ineffective.

217. We consider that there may be some continuing role for independent regulation of the railway to ensure that contractual obligations are met, that access is properly controlled, and to perform a speedy arbitration function in the event of contractual disputes. However, we think that the Government in its present review of the railway structure needs to cut back severely the present, highly interventionist, regulatory regime. In particular, we consider that it is completely inappropriate for the Regulator to determine alone the funding which the Government must set aside for the railway infrastructure, given the size of the sums concerned and the knock-on effect on other areas of public expenditure. The planned move to a regulatory board structure with the same functions as the Regulator later this year does not, in our view, affect this argument.

Unified delivery for the passenger – Railway Agency

218. If there is to be any prospect of a significant improvement in performance discernible to the travelling public, then the present unstructured relationship between infrastructure provision and output specification, needs to be disciplined within a formal, structured framework. If the Government, for ideological or other reasons, will not operate the railway directly, a unified and powerful rail delivery organisation - a Railway Agency - which includes relevant railway expertise with the wider public interest and regulatory functions, and combines the present functions of the SRA and Network Rail, should be created in the public sector.³⁷⁰ We think, therefore, that an Executive Agency model for such a body is likely to be appropriate. The top management of the new body should comprise a small executive team with clearly focussed strategic *and* functional responsibility for the delivery of key operational elements of the railway, for example, infrastructure, passenger operations, customer service, freight development. It should be led by a chief executive and a chairman of world class professional stature. Those leading the UK railway industry in future should be highly knowledgeable and internationally respected professional railway men and women. It will be essential that the new body re-establishes public respect for the railway in order to attract talented and committed individuals to all levels to the industry. Sweeping away the present confused organisational arrangements and substituting a single delivery body responsible for a unified railway, offers the hope that lines of responsibility and funding will be clarified, strategy and operations will be “joined-up”, and the potential for performance improvements radically maximised. The record of British Rail in the 1980s when subsidy was reduced, financial targets met, investment increased, and service quality improved, demonstrates that an integrated railway can function efficiently.³⁷¹

369 Section 4(5)(a) of the Railways Act 1993 as amended by section 224 of the Transport Act 2000

370 European Directive 91/ 440 of July 1991 is not in conflict with this proposal. The Directive insists that the *accounts* of rail infrastructure and operations should be separately identified, Gourvish, *op cit*, p 262

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219. Many of the passenger train franchises are being run as management contracts; franchises have been extended; and Network Rail has taken over rail maintenance directly. This all suggests that the present, fragmented state of the railway is forcing consolidation incrementally on the industry. Whether or not this amounts to “creeping re-nationalisation”, our proposal for a unified public sector Railway Agency responsible for train outputs and the rail infrastructure, sits well with the industry’s present evolution.

220. We do not envisage that this new body would necessarily be required to run all the infrastructure and passenger train services directly. The Government will wish to consider the merits of continuing to involve the private sector in infrastructure provision and passenger train services, where clear benefits exist for doing so; equally, its mind should be far more open than before to the public sector providing services directly where appropriate. Privately owned rail freight companies would continue to operate freight services. In some cases a measure of so-called “vertical integration”, where track and trains are operated by the same body might be appropriate, as in the case of Japan’s regionally based passenger rail companies; and in rural areas the specification of services might be devolved to the local bodies, as in the case of Merseyside. A wide variety of service provisions, tailored locally to passenger requirements, could be accommodated within the arrangements we propose. In general, the provision of rail services needs to take much greater account of local and regional needs. Unifying the delivery of railway services emphatically must not mean bureaucratic centralisation; nor, of course, does it mean breaking up the network. Responsibility for the infrastructure and the delivery of all railway outputs should rest clearly with an Executive Railway Agency acting as the unified train service delivery organisation.

Safety

221. The Secretary of State has pointed out that safety is integral to the railway.³⁷² It is right that this should be so. It is also right that those regulating rail safety should take full account of the industry’s safety achievements and problems in order to target future effort accurately and use resources effectively.

222. The evidence we have taken in the course of this inquiry indicates that the relationship between the HSE and the industry has broken down. We cannot see how fully effective railway safety regulation can be carried out in these circumstances. It should be a priority for the Government’s review of the railways to consider whether Her Majesty’s Railway Inspectorate should be removed from the HSE and made, either an independent Agency of the Department for Transport, as is the case with the newly established – but regrettably delayed – Rail Accident Investigation Branch, or merged with the new Rail Agency body we have proposed.³⁷³

372 Transport Committee, *The Departmental Report 2003*, Ev 10

373 Section 3, Part 1, Railways and Transport Safety Act 2003

Rail Passengers Council

223. A mature industry needs a strong and constructive consumer voice, particularly at times when the industry's performance is weak, its structure fragmented, and it lacks any strong vision for the future, as at present. We were frankly disappointed with the contribution of the Rail Passengers Council (RPC) to our inquiry. In addition, the profile of the RPC throughout the network is too low. We likened the Council to a 'secret' which the industry likes to "keep to itself".³⁷⁴ We were concerned, for example, that members of the public who wanted to complain about train services would not find the RPC's contact details readily available. This needs to change. If this organisation is to make a significant contribution to the debate about the future of the railway, then it will need to represent passengers' concerns much more powerfully than at present. It may be that a body representing interests of passengers which is not sponsored directly by the body responsible for the railway, as the RPC is presently by the SRA, would find a more insistent public voice.

Conclusions and recommendations

Introduction

1. The Government and Mr Bowker, Chief Executive and Chairman of the SRA, assured us that the structure of the industry was not going to be changed, and that the industry's focus should be on making the existing arrangements work properly. Nevertheless, we felt it was important to look at fundamental issues. To this end, we posed four questions:

is rail an outmoded form of transport?

is the present network the right one, and if not, will it have to be changed?

what sort of traffic is the network best used for?

how does our network compare with other railways and what lessons can we learn from other countries? (Paragraph 3)

2. The constant theme throughout our work was the complaint that the current structure of the industry is too fragmented to provide clear lines of responsibility and leadership and a satisfactory basis for improved rail performance. (Paragraph 4)
3. We have seen no evidence, since our predecessors reported two years ago, that fragmentation in the rail industry has reduced. Indeed, our evidence has suggested that it is getting worse. In addition, industry costs are increasing; performance remains in the doldrums; and the SRA appears utterly incapable of managing significant improvements. The evidence of the Rail Regulator's Interim Review of track access charges is that the Regulator and the SRA are not co-operating well. (Paragraph 7)
4. It became clear that, as the railway system is currently governed, there is no one organisation capable of properly addressing the four questions with which we started. In our view, until there is a single body with the authority to deal with these questions, Government and the rail industry are condemned to spending energy debating structural issues rather than getting on and running the railway for the benefit of the travelling public and the country. This report addresses the fundamental questions: who does, and who should, run the railway? (Paragraph 9)
5. It is essential that costs are brought under control for the future of the railway. (Paragraph 15)
6. The damaging consequences of these and other failures for the sound regulation and governance of the railway are the subject of the remainder of this report. However, the fundamental failure of the railway is one of Government policy. The Government has not been able to exert control on the extra costs of the railway system, identify clearly the root causes of the extra costs, nor has it after two attempts produced a governance structure that has clear lines of accountability for public money and ensures appropriate transfer of risk to the private sector. (Paragraph 17)

7. It is vital that the recent surge in costs for the railway is checked. The Government has told us that it is in control of the industry. But the swelling subsidy figures of recent years tell the real story of an industry that is out of effective control. The siren song of the SRA is that a “gradualist”, evolutionary approach based on intra-industry co-operation will enable costs to be reduced and performance to improve. Others we heard from were in favour of restructuring. We publish the evidence of both with this report. Relying on incremental improvements may take many years to produce results; ill judged restructuring will damage the industry further. However the Government chooses to reverse the present position of the railway, it will be essential that in future it ensures proper control over the money it provides. The Government must ensure that the private sector assumes real risk where it is involved in providing railway services in future. The Government also needs to ensure that the funding of the railway is properly integrated with other transport modes. The Government has the responsibility to sort out the current mess; it needs to make sure that it has the powers required to do so, and that the powers and responsibilities of all the bodies involved in the railway industry are appropriately structured. (Paragraph 18)
8. We are delighted that the Secretary of State has changed his mind over the four months since he gave evidence to us and has also decided to review the structure of the railway. (Paragraph 20)

Rail Regulator

9. Network Rail has now indicated that “a baseline asset register providing an inventory of the assets and their key attributes” will not be ready until mid-2005. (Paragraph 30)
10. It is utterly astonishing to learn that Network Rail’s Asset register, a fundamental management tool, will now be available only in 2005, four years after a Select Committee of this House drew attention to its absence. The Regulator has clearly failed to ensure that first Railtrack and now Network Rail, have produced information needed to assess performance of the system. This is not an academic exercise. If the state of the infrastructure is not thoroughly known then reliable decisions about the levels of maintenance and renewals are simply not possible and the basis of the Regulator’s Interim Review is placed in doubt. This episode demonstrates graphically how the Regulator has failed in his core function of effectively regulating the ‘stewardship of the national rail network’. (Paragraph 31)
11. The Government has made clear its role in guaranteeing investment, as in the case of the securitisation to refinance Network Rail’s short to medium term borrowing. Mr Darling said in a recent answer to a written parliamentary question in the House of Commons:

“Railways are essential to the economy of Britain. Whatever the institutional structure, the Government will need to be at least as closely involved as it currently is in expenditure decisions and in making financial commitments to the industry and those who finance it; so that lenders to the industry enjoy at least the same strength of financial support from the government as they do today.”

It is the Government, not the Rail Regulator, which guarantees private investment in the railway. (Paragraph 36)

12. The Regulator, Network Rail and the SRA clearly differ about who exactly runs the railway infrastructure in the UK. Although we understand the need for a measure of regulation to prevent a monopoly company abusing its position, the Regulator is not the customer, and should not specify what the customer should be buying. It seems that the Regulator cannot do the job of economic regulation without effectively acting as the informed customer. This is to confuse the roles of economic regulation with the SRA's job of purchasing services. In those circumstances, it is clear that the railway structure must be fundamentally changed. (Paragraph 41)
13. Our inquiry exposed an astonishing and fundamental disagreement between the Government and the Regulator about the extent of the latter's powers. According to the Minister, the Government had a choice about whether to accept the Regulator's access charges settlement; but the Regulator considered that the Government had no option but to accept his decision. This is a prime example of the confusion which lies at the heart of the present structure of the railway and why it is essential that this structure must be streamlined. Since we took this evidence, the Secretary of State has made clear, in answer to a parliamentary question, that the Government is committed to the Regulator's access charges settlement. We were pleased to note that in the same answer the Secretary of State indicated that the Government would need to consider "whether options for changes to the industry structure might imply consequential changes to the details of economic regulation." (Paragraph 48)
14. It appears that both the Government and the SRA were unprepared for the result of the Rail Regulator's Interim Review of track access charges and that a last minute panic took place about how the financial implications of the Regulator's settlement for the SRA were to be met. The SRA and the Government should not have been surprised that the Regulator was proposing to set aside his duty to have regard to the SRA's budget because Mr Winsor said so specifically in his Draft Conclusions document published in October 2003. The Regulator chose not to give appropriate weight to his statutory duty by ignoring the SRA's budget; and the Government and the SRA failed to challenge this decision. (Paragraph 49)
15. This whole episode is not only an example of the high handed manner in which the Regulator approaches his role; it is an example of a deep failure in the structure of rail governance which has allowed the Regulator to act as a "Rail Czar", something that was never intended and which must be corrected. (Paragraph 50)
16. The private sector needs appropriate protection from arbitrary Government decisions. But the current power of the Regulator goes far beyond reasonable bounds and must be reined back. The enormous sums of public money directed to the railways by the Regulator are ones over which, astonishingly, neither the Government, nor the SRA, have any practical control. The Government has little choice but to honour the cheques which the Regulator writes for it. (Paragraph 51)
17. The present situation is an intolerable restriction on the Government. The sums of money decided by the Rail Regulator are so large, and the issues for the transport

infrastructure of the country so important, that the Government needs to take back from the Regulator decisions over the level of infrastructure funding. (Paragraph 52)

Network Rail

18. Network Rail did not convince us that the members of the company were exercising an effective control of the company. We were also concerned that industry members were virtually self appointing. These members include contractors, and while members have a duty to the company, there was always some possibility of the appearance of a conflict of interest. Finally, the public members are appointed by the Board of the company and represent no-one but themselves. (Paragraph 59)
19. The actions of the Rail Regulator to strengthen the terms of Network Rail's network licence may be welcome in themselves, but are no substitute for sound day to day management and powerful managerial accountability to the owner. We do not believe that appropriate accountability is demonstrated at present by the company. (Paragraph 61)
20. That the performance of the infrastructure provider should have plummeted on the railway in the period since Hatfield by 92%, and from 70% to 92% between June and October 2003 alone is scandalous, and demonstrates the utter inability of the industry as presently structured to improve its performance. (Paragraph 64)
21. The fact that Network Rail has to assume for business planning purposes that industry partners will make improvements in step with its own, is a further example of the extreme difficulties caused by the structure of the industry. In the present circumstances of extreme industry fragmentation the company's key main performance indicators – improved safety, higher performance, increased system capability, improved customer and stakeholder relationships, improved financial control, improved asset stewardship, improved business performance - can never be measured and scrutinised to any satisfactory degree against the company's own activities alone. (Paragraph 67)
22. That overall railway performance depends on such a large number of companies is not just a problem for Network Rail. The problem is that while it is possible, for example, to collect statistics on the number of trains running, or the number of minutes of delay, and who is responsible for them, unless there is a body empowered to direct performance, companies blame one another for poor performance, rather than working together for improvements. One result is that the responsibility for train service interruptions is not transparent: the fault may lie with Network Rail, the train operating company, a train operating company elsewhere which has caused a "knock on" delay, or a combination of these. That train passengers often do not know who is responsible for delays under the current system is a further, major, frustration for those using the service. (Paragraph 68)
23. It appears most unlikely that the targets for reducing delays set by the Rail Regulator for Network Rail will be met fully, if at all. The cause is, in large part, the result of the fragmented state of the railways and the enormous, wasted effort required to co-ordinate effort between a wide range of parties. Network Rail alone has over 10,000 suppliers of goods and services and approximately 200 main contractors on the

infrastructure. Many delays will arise from events beyond its control. For the Regulator to place ever more challenging targets on a structure which is incapable of meeting them fully is nonsensical. (Paragraph 69)

24. We are utterly unconvinced that “step in” rights for the SRA provide an effective incentive for Network Rail to improve its performance and live within its means. This is an example of the Rail Regulator “dressing up” Government financial support as a regulatory “incentive” to defend the present regulatory regime. (Paragraph 72)
25. Network Rail is far from profitable. (Paragraph 74)
26. We understand the arguments in favour for adding overspend to the Regulatory Asset Base (RAB), but it might be thought that this seems rather like increasing someone’s credit limit on the grounds that the goods they have bought by overspending increase their real wealth. The huge sum of £5.5 billion was overspent in the period 2001-2004. The addition of this amount to the “regulatory asset base” of Network Rail –apparently a decision for the Rail Regulator alone- is the equivalent of a massive, one-off subsidy to the rail infrastructure. Yet, even so, Network Rail has posted a loss of £290 million. (Paragraph 78)
27. This episode demonstrates the extent of the power which the present structure has allowed the Regulator to accumulate at the expense of all the other parts of the railway, and of the Government. The Regulator is meant to be restraining costs and seeking value for money. Instead, the present structure has permitted him to write off astonishingly large sums of public money, apparently on his own authority. One highly significant aspect of the overspending during the period in which Railtrack was in administration is that, in the middle of the most severe crisis for the industry in the last 10 years, the SRA, which must have been backed by the Government, bypassed the Regulator. The system was not flexible enough for all parties to join together in finding the best solution in extreme circumstances. (Paragraph 79)
28. Network Rail’s debt is soaring. (Paragraph 80)
29. In effect, what has happened is that the Government has accepted the risk of the Network Rail operation, but on more expensive terms than it need have had it direct ownership of the company. (Paragraph 85)
30. We are deeply concerned that the cost of servicing Network Rail’s considerable debt is higher than it need be because of the company’s private status which means that the cheapest Government borrowing is unavailable to it. We can see little prospect of the company becoming profitable and able to feed funds back into the rail industry under present circumstances. This makes it all the more important for borrowing to be done as cheaply as possible. (Paragraph 86)
31. The present Network Rail ownership arrangements do not make sense. The company is not expected to make a profit for the foreseeable future; the cost of funding it as a private sector company is higher than it need be; and its governance arrangements are weak. We consider that it is time for the Government to cut through this tangle of responsibilities and take direct ownership of Network Rail on the grounds that a Railways Agency, incorporating the rail infrastructure, will ensure

both the lowest borrowing costs to meet the necessary funding requirements and direct, democratic accountability. (Paragraph 87)

32. We think that the company's decision to take all infrastructure maintenance in-house is a move in the right direction, though we had expected to be given a rather more exact estimate for the likely savings than the range of figures presented to us. It appears obvious that overheads associated with contracting for such work with the private sector do swell overall costs, and that in the absence of private sector profit margins the cost of maintenance should fall. However, the company will need to manage the costs of increasing its own workforce to cope with this work carefully to preserve potential savings. It will also be particularly important that the company attracts the appropriate mix of engineering expertise from the private sector. (Paragraph 93)
33. Network Rail's decision to retain the private sector for track renewals could be problematic. While inefficiencies may, or may not, be driven down to the level the company is seeking by this decision, there will remain a contract profit margin cost to the company which will be absent from the rail maintenance side of the business. The efficiency gains will need to be demonstrably significant for National Rail's present renewals' policy to be persuasive. Taking more work "in-house" would also be an opportunity to reduce the number of company 'interfaces' and contracts which currently burden the industry. In the longer term, Network Rail should reconsider its decision to retain private sector contracts for track renewals. It should also review now what other services it currently purchases and which might be more economically provided under direct management control. (Paragraph 95)
34. We are concerned that the drive to reduce costs appears in conflict with long term investment in the infrastructure. Balancing costs and investment needs to be undertaken on the basis of solid data and agreed targets, both of which appear to be in short supply. The company needs to get a better grip on the level of renewals required so that there can be confidence that cost and investment are in reasonable balance. (Paragraph 105)
35. The Regulator was entitled to challenge Network Rail's estimates of work required where these appeared to him to be in excess of necessity. We are nevertheless astonished at the spectacle of two bodies – Network Rail and the Rail Regulator- in dispute in this manner. This is not an outside body (the Regulator) undertaking a straightforward check of the operator's documentation, but appearing to undertake a root and branch parallel exercise by consultants of renewals' estimation. Either the renewals documentation of Network Rail is grossly deficient – as the Rail Regulator appears to believe – or the Regulator undertook too detailed an examination, at a considerable consultancy cost. (Paragraph 106)
36. It was inefficient and highly expensive for Network Rail and the Rail Regulator to undertake parallel exercises assessing renewals' requirements of the rail infrastructure. It should be a firm objective for the future economic regulatory authority and the infrastructure provider to ensure that the quality of the latter's estimation processes and records is sufficient to provide a very high degree of

confidence in what is being proposed, allowing there to be much less parallel checking and micro-management in future. (Paragraph 107)

37. It is also unacceptable that Network Rail did not have its estimates of overall funding requirements under control. We accept that the original estimate in March 2003 may have been inaccurate owing to the requirement to publish and the relative shortness of preparation time. However, even after an element of joint working with the Regulator and his consultants, the company's final requirements estimates vary by an excess of £2.5 billion from those of the Regulator. (Paragraph 108)
38. In these circumstances it is difficult to understand why the company has now agreed to a settlement which its own estimated figure appears to suggest is too low for the work it considers necessary without complaint. It had options to ask the Regulator either to issue a new review notice, or refer his determination to the Competition Commission, but chose not to do so. This suggests that the company's estimates of funding requirements cannot be relied upon. The company needs to take urgent steps to demonstrate that it has adequate systems in place to ensure future funding forecasting is accurate to establish credibility. (Paragraph 109)
39. Taking the company into direct ownership together with removing the Regulator's present role of determining the level of the company's funding, as discussed in Chapter 2, would enable the Government to ensure cheaper funding for, and more effective overall control over, the railway infrastructure, particularly maintenance, renewals and enhancements. It is likely that there will continue to be a role for the private sector in aspects of infrastructure provision. But the structure of Network Rail needs to reflect the funding reality that the Government guarantees the finances of the railway and will continue to do so for the foreseeable future. Network Rail's present private sector status and structure mask that reality and not only fails to deliver benefits to the industry and the travelling public, but actually produces the significant funding and governance flaws we have discussed. The Government needs to move quickly to take control of the infrastructure into the public sector. (Paragraph 110)

Strategic Rail Authority

40. The letting and management of passenger rail franchises is at the heart of the SRA's work and where its impact can be assessed most clearly. It is also an area where the private sector is most directly involved in providing railway services and where its freedom to innovate is greatest. (Paragraph 115)
41. Some franchises have performed in the way that was expected. However, it is clear that the vast majority have not been able to produce the efficiency gains that were confidently anticipated at the time of privatisation. The network is now being run by a patchwork of companies, which operate in a variety of ways, with a variety of incentives. It is not for us to judge whether more efficient companies could have performed more creditably; however, the number of franchises in difficulties suggests something is fundamentally wrong with the structure of the industry. Either the private sector is no more efficient than the public, or it is being given tasks that no one can fulfil. (Paragraph 119)

42. In our view, the essence of private sector involvement is that the private sector pays if it gets its sums wrong. It is outrageous that such astonishingly large sums of taxpayers' money have been used to prop up palpably failing businesses such as £58 million in the case of Connex. While we accept that failures in the initial franchise process may have been to blame originally, we cannot understand why action was not taken earlier by the SRA. As a result of this failure to monitor Connex properly the SRA bailed out a company using taxpayers' money only to strip it of its franchise a short time later. The SRA's management of this franchise has been woefully poor. (Paragraph 122)
43. Nearly a third of the franchises were no longer expected to function in the entrepreneurial, risk-taking way that was one of the fundamental justifications for private sector involvement in running train services but simply to function as fee paid agents of the SRA. This indicates the extent of the present malaise. (Paragraph 123)
44. Existing franchise agreements should be extended only if there are compelling operational requirements, or clear value for money justification. Extensions are a measure of last, not first, resort, and these examples suggest that the SRA has failed to plan ahead adequately. (Paragraph 124)
45. The new generation of franchises must be structured in a way which prevents franchisees returning for ever more public money, and ensures that costs are properly anticipated and controlled. Revenue risk should be assumed by the private sector wherever possible. The passenger must be the focus of the whole exercise. The SRA's record of franchise management to date is poor. While the new franchise arrangements appear to be an improvement over the existing agreements in certain respects, we are particularly concerned that there is an automatic right of extension for three years if targets are met. If the new arrangements are to succeed, targets will need to be set sufficiently high that passengers notice a real difference in day to day performance of railway services; and SRA monitoring will require to be exceptionally accurate and rigorous. We have no confidence that the SRA is presently up to this task. (Paragraph 127)
46. The Government has undertaken to share the results of South East Trains with us and we look forward to seeing these. (Paragraph 129)
47. We were surprised at the evident unwillingness and timidity of the Government and the SRA to contemplate the SRA running train services directly, even if the SRA's experience of managing South East Trains demonstrated clearly that this could be done by the SRA at the best price and highest efficiency. It seems common sense that where benchmarking identifies the most cost effective solution to running a franchise then that solution should be adopted. The public are rightly concerned with excellent service and value for money. The record of the private sector in running trains overall is poor. To adhere to the policy of restricting such operations on ideological grounds does not appear sensible. In fairness, this evidence was given before the Government's recent announcement of its rail review. We trust that now a fundamental review is underway, the Government will consider this option much more actively. (Paragraph 130)

48. Even where the SRA has direct responsibility, as with the franchising of passenger rail services, its imagination, focus, and performance are deficient. It has no day to day control of the delivery of passenger rail services, working, as it does, through the train operating companies. The degree to which the SRA is able to improve the journey of the travelling public directly is therefore limited by the sophistication of its contractual arrangements with franchisees. The extreme difficulties inherent in this process are obvious. The quality of the present franchises is poor; the new arrangements appear tighter, but their effect on train performance cannot yet be judged. (Paragraph 131)
49. The Transport Act 2000 requires the SRA to “formulate strategies” which “should...cover both its own activities and those of the industry.” The SRA requires the consent of the Secretary of State before publishing its strategies. The SRA’s strategies embody its approach to various operational aspects of the railway. How effective are these strategies in grappling with key issues of today’s railway? (Paragraph 132)
50. It appears from the Government and SRA evidence that the railway will remain “mixed” in the near future. Visionary proposals for passenger-only high speed networks have obvious funding drawbacks. Nevertheless, in the context of deciding on a railway future for the 21st century such ideas must be explored thoroughly. We agree that it may be politically and financially difficult to contemplate high speed passenger networks when the existing system is so clearly in need of overhaul, but there must be scope for imaginative thinking about the country’s future transport needs. We hope that this issue will be revisited and the arguments set out clearly. (Paragraph 136)
51. The SRA’s suspension of rail freight grants at the very time that it was fulfilling its strategic remit by updating an environmental benefits methodology, shows the difficulties facing the organisation. In scrambling for short-term savings, the SRA had to compromise its ability to carry out its strategy which caused a loss of credibility throughout the industry in the Government policy on rail freight. Those responsible for the railway in future need to ensure much better coordination of budgetary management and strategy. (Paragraph 141)
52. The Rail Regulator’s refusal to adjust Network Rail’s expenditure to take account of the SRA’s Specification of Network Outputs is an excellent indication of how severe the limitations are on any SRA strategy in the present structure of the industry when it affects the operation and budget of the infrastructure provider, which are effectively specified by the Regulator. (Paragraph 145)
53. While modest funding for rail research is available in the short term there are long term uncertainties. The result is that careers in the industry are not attractive and vital expertise may not be available. The present effort to stimulate rail research lacks focus. Rail Research UK’s evidence suggests that the industry itself could do more. The SRA has not been given the direct task of co-ordinating and funding railway research. This was a mistake. One of the tasks of the body charged with industry leadership in the future must be to build on the efforts of the EPSRC to ensure that the United Kingdom has a sound research base to underpin railway developments.

The Government needs to consider carefully future arrangements for the better co-ordination of rail research. (Paragraph 149)

54. It may be that there are good reasons for keeping some data at aggregate level, but the presumption should be that as much as possible is made available publicly. Without full and accessible data it is impossible to conduct a sensible debate about the future shape and purpose of the railway, a debate in which there is a wide public interest. (Paragraph 151)
55. The severe limitations of its powers and the fragmentation of the industry into competing “baronies” means that the SRA needs to work closely with other bodies to maximise its leadership influence across the industry. We highlight briefly below examples where the SRA has been sidelined, has little or no influence, or has failed – because of the fragmented structure of the industry – to cooperate effectively with another transport body. These failures are not confined to the bodies directly concerned, but have important, knock-on effects on the rail sector as a whole, and the travelling public. (Paragraph 152)
56. We are deeply concerned by the nature of the decision making process revealed by the recent events on the West Coast Main Line upgrade project. Even now there appears to be no agreement on the entirety of the project. Neither the SRA, the Rail Regulator or Network Rail seems to have power to make a final decision. The Government seems powerless to intervene. It is hard to think of a more telling example of the divided leadership of the railway and the powerlessness of the SRA. (Paragraph 160)
57. Irrespective of the exact nature of the exchanges between Network Rail and the SRA over the company’s decision to take rail maintenance in-house, it is clear that the present structure of rail governance reduced the SRA in this crucial decision to a bystander. This is yet another example of the utter impotence of the SRA. (Paragraph 162)
58. For a private sector investment of almost £1.5 billion since 2001/2, the average age of the UK rolling stock fleet appears to have declined by approximately 16 months only. This seems to us a rather modest achievement. (Paragraph 164)
59. We wish to stress that it is essential that the ROSCOs do not receive more than a reasonable return, and that their market power does not lead to abuse. The cost of excessive returns for the ROSCOs is less money for the railway. We are concerned that the market may not be acting appropriately to provide rolling stock at economic cost; and that the SRA’s rolling stock strategy may have missed an opportunity to rationalise rolling stock requirements. (Paragraph 165)
60. It is clear that the policy of Special Purpose Vehicles has failed to attract private sector investment into the industry as originally intended. The SRA can only bring in private sector money if it has suitable projects and, we suspect, if the public bear most, if not all, of the risk. (Paragraph 167)
61. The PTEs’ discontent was not rooted in any unwillingness to work with the SRA, but was the result of what they saw as structural flaws in the rail industry which resulted

in a mismatch of objectives between franchises and local transport plans as in the case of the Northern franchise. The Passenger Transport Executives saw two roles in the rail industry, “setting policy” and “delivering.” They considered that because the operations of Network Rail were funded by the SRA, directly through grants or by subsidy to train operating companies which fed through to Network Rail, consideration should be given to drawing the responsibility for delivering train operations and infrastructure together under one organisation. (Paragraph 170)

62. While the SRA is to be commended for facilitating the Merseyside arrangements by relinquishing the specification for the franchise to the PTE, we are worried and puzzled that the SRA indicated in a press release that this interesting example of local, public/private partnership initiative in Merseyside, was something which could not readily be repeated. We accept that the nature of the Merseyside franchise area makes it an obvious candidate for devolution of rail services. But the SRA’s position on closing the door to the approach adopted here appears highly unimaginative. We hope that the Government – in line with the reference in Mr Darling’s Statement of 19 January to seeking devolution of rail to PTEs - will ensure, wherever possible and with appropriate local adjustments, that the arrangements in Merseyside can be repeated not only with the PTEs, but wherever they appear workable. More generally, we think that there are lessons to be learned by all franchisees in the absolute focus on passenger service which lies at the centre of this operation. Any devolution of rail to the PTAs should also ensure financial flexibility and the possibility of modal change. (Paragraph 173)
63. Even though there remains some confusion in the SRA about the causes of the cost escalation in the railway, it is clear that the greatest increase is in the cost of rail infrastructure. As we have pointed out earlier, this is presently the responsibility of Network Rail and the Regulator, and the SRA has no direct control. (Paragraph 176)
64. In order to provide coherence and morale for the industry, the SRA needed to articulate a clear vision for the railway of the 21st century and the goals needed to achieve that vision. This vision required to be sufficiently broad to be shared by the travelling public and the Government, and precise enough to energise and inform the operational work of the railways. The SRA also needed to take account of, and lead, the debate about the nature of rail that our work uncovered. Has the SRA led that debate? Does the SRA have a vision for the railway? (Paragraph 177)
65. We found little evidence of the SRA leading the debate in the development of new thinking about the railway, or even engaging fully with many who are contributing to that debate. (Paragraph 178)
66. That we should have found no strong, organising vision for the railways is depressing but, in the light of the evidence we received, not surprising. The SRA was set up to provide leadership through strategy direction – in other words, to provide this vision. On the evidence received in this inquiry it simply does not have the power to do so. (Paragraph 179)
67. The SRA does not control the day to day activities of franchisees; the infrastructure; the contracts by which companies get access to that infrastructure, the resources that

are put into that infrastructure; or the measures to ensure the safety of the industry and the travelling public. All it controls directly is the letting and monitoring of franchises, and the giving of various grants. (Paragraph 181)

68. It is clear to us that the SRA does not have the powers and responsibilities to provide it with the commanding position of leadership that the industry requires, and to drive through the improvement in rail operating performance which the Government and the travelling public are entitled to expect. Consequently the SRA has failed to provide the scale of improvements which it was set up to deliver. Mr Bowker's assertion that the railway is structurally sound is unfounded. Restructuring the railway to enable output specification and control over the means of delivering infrastructure improvements to be exercised within a single management structure should be the core of the new arrangements for the railway, as we discuss in more detail in Chapter 6. Structures emphatically do matter. 'People, management and process' do not exist in a vacuum. A rational framework for the railway is required which allows the industry to work together to improve railway services for passengers. (Paragraph 182)
69. While the HSE, Network Rail, the RSSB, could readily tell us their administrative budgets for rail safety, no one could provide us with a sum totalling the cost of safety to the industry as a whole. In Network Rail's case this was because "the needs of safety arise in every activity we carry out as a company". We asked the Secretary of State for Transport who said, "It is difficult to put a precise figure on it...Frankly, safety should be in with the bricks". In the absence of a credible overall figure for the costs of rail safety –which may be extremely difficult to arrive at- it is impossible to conclude that safety on the railways as a whole may be costing too much, or that insufficient is being spent. This does not mean that judgements on the cost effectiveness of particular projects are not possible. However, we have received evidence that the HSE has caused unnecessary extra cost by "gold-plating". (Paragraph 190)
70. All safety standards applied by the HSE must be constantly updated and be the result of proper and rigorous risk assessment. Unless this is carried out the HSE's service to its railway customers will be unacceptably diminished. It is also completely unacceptable that the industry should risk incurring huge costs for inappropriate safety measures because of relatively small budgetary considerations in the HSE. Where such costs are incurred there will be an inevitable knock-on to the travelling public who are therefore made to bear at least a part of the costs of the safety regulator's poor practice. (Paragraph 193)
71. It is extremely disappointing that Network Rail's representations on the inappropriateness of designating the industry as a "major hazard" appear not to have been brought to the attention of the current HSE Director of Rail Safety. (Paragraph 197)
72. We do not accept that parallels exist between the rail, nuclear and chemical industries. We certainly do not underestimate the extremely serious consequences of any train accident; but the scale of nuclear and chemical accidents is not likely to be similar to those on the railway. In our view, this places in doubt HSE's designation of

the railway as a “major hazard” industry which we think could result in a “gold plated” approach being taken to rail safety. The HSE needs urgently to rethink its approach to the classification of rail as a ‘major hazard’ industry and generally to adopt a more nuanced, railway-specific approach to such matters. (Paragraph 198)

73. We are not convinced that the HSE’s approach to TPWS demonstrated a reasonable balance of costs and safety. Further, we were appalled to see so profound a disagreement between Network Rail and the HSE over the extent of the TPWS system to be fitted on the network. (Paragraph 201)
74. The Government funds rail safety research but, in effect, hands the money over to the rail industry to spend. We think that the Government needs to examine the use that is being made of such research funding against the overall objectives for rail safety to ensure that these sums are being put to best use. For example, we wondered why the function of rail safety research could not be taken into the Railway Inspectorate and those sums administered directly in order to promote research which would then inform policy directly for improving rail safety regulation. (Paragraph 204)
75. The highly disturbing evidence of our inquiry is that the rail industry’s confidence in the HSE is at a low ebb. (Paragraph 206)
76. It is a matter of profound concern to us that the person appointed to the key post of Director of Rail Safety, leading the Inspectorate in the HSE, left his post after less than a year with the clear perception that the HSE’s regulation of the railway industry was so flawed as to require it to relinquish its responsibility . (Paragraph 207)
77. Safety measures must take proper account of the ability of the industry to pay for them, and be clearly proportionate to the risk. The justification for such measures must be based on cost benefit analysis principles that are agreed across the industry, and such calculations need to be shared between the relevant bodies. Benchmarking to establish best practice needs to be extended to other transport modes, and not only to apparently inappropriate comparators such as the nuclear industry. It is apparent that the HSE has lost the confidence of the industry. It should be a priority for the Government’s review of the railways to consider whether Her Majesty’s Railway Inspectorate should be removed from the HSE and either made an independent Agency of the Department for Transport, or merged with the new unified rail delivery body we propose in the final Chapter. (Paragraph 209)

The Future of the Railways

Present Confusion

78. The present confused and fragmented state of the railway meant that we found no satisfactory answers to the four questions with which we started. However, our inquiry has enabled us to be confident about changes that will be required to ensure the future of rail. (Paragraph 210)
79. The current railway structure blurs responsibility for policy and railway services and is not fit for purpose. Rail policy can never be divorced from decisions about overall

public expenditure which are the responsibility of Government. The Government's function of adjudicating on the public interest has been passed to the Regulator who acts as a 'proxy for the public interest'. The Government is presently compelled to carry out his funding decisions; Network Rail is required to carry forward and manage the operational consequences of his financial planning; the SRA has struggled to determine railway outputs because the Regulator has effective control over the infrastructure. In addition, however well advised, the Regulator is ultimately not professionally equipped to take detailed operational and managerial decisions about the railway. Our evidence has shown in detail how this present rail structure, far from focussing the various parts of the railway as a whole on improving services to the passenger, has meant that valuable energy has been diverted to intra-industry squabbling and "buck-passing", while co-operative moves by the various rail bodies governing the industry have had little or no demonstrable effect upon improving performance. (Paragraph 211)

80. Further restructuring of the railway will be disruptive. Nevertheless, we cannot see how the railway can ever be made to work significantly more effectively and transparently under present conditions. It is imperative that the Government uses the review of the railways announced on 19 January 2004 to address these fundamental problems. A model of railway governance is required which restores to the Government control over the public interest, public expenditure, rail policy, and objective setting; while allowing the railway industry full operational responsibility for the delivery of improved infrastructure, train service outputs and strategy objectives. (Paragraph 212)

Focussed economic regulation

81. One of the most negative aspects of the present railway governance arrangements is the Rail Regulator's autonomy and its undermining of the SRA's strategic role. (Paragraph 213)
82. However, the success of the present regulatory regime in fundamental aspects of controlling costs, laying down strong incentives, providing for secure knowledge of the industry's assets, quantifying investment arising from it, and working well with other railway bodies under Government guidance, has been abysmally poor. It did nothing to prevent the appalling débâcle of Railtrack when the railway came close to collapse. The costs of the industry have still to be brought under control. In addition, as we have demonstrated, it is the Government and not the Rail Regulator which guarantees the railway and the private investment. Finally, the Regulator appears to have extended his role in setting track access charges into the forward management of Network Rail's business – something that was surely never envisaged to be a part of his function – thus subverting the proper function of that management and risking a further confusion of roles. (Paragraph 214)
83. It is difficult to envisage a situation in which the private sector will not be involved in providing some train and railway services and will not need to negotiate a range of contracts with a unified infrastructure provider. In those circumstances, the role of an independent regulator will be required. The question is, what will that role comprise? (Paragraph 215)

84. We consider that there may be some continuing role for independent regulation of the railway to ensure that contractual obligations are met, that access is properly controlled, and to perform a speedy arbitration function in the event of contractual disputes. However, we think that the Government in its present review of the railway structure needs to cut back severely the present, highly interventionist, regulatory regime. In particular, we consider that it is completely inappropriate for the Regulator to determine alone the funding which the Government must set aside for the railway infrastructure, given the size of the sums concerned and the knock-on effect on other areas of public expenditure. The planned move to a regulatory board structure with the same functions as the Regulator later this year does not, in our view, affect this argument. (Paragraph 217)

Unified delivery for the passenger – Railway Agency

85. If there is to be any prospect of a significant improvement in performance discernible to the travelling public, then the present unstructured relationship between infrastructure provision and output specification, needs to be disciplined within a formal, structured framework. If the Government, for ideological or other reasons, will not operate the railway directly, a unified and powerful rail delivery organisation - a Railway Agency - which includes relevant railway expertise with the wider public interest and regulatory functions, and combines the present functions of the SRA and Network Rail, should be created in the public sector. We think, therefore, that an Executive Agency model for such a body is likely to be appropriate. The top management of the new body should comprise a small executive team with clearly focussed strategic *and* functional responsibility for the delivery of key operational elements of the railway, for example, infrastructure, passenger operations, customer service, freight development. It should be led by a chief executive and a chairman of world class professional stature. Those leading the UK railway industry in future should be highly knowledgeable and internationally respected professional railway men and women. It will be essential that the new body re-establishes public respect for the railway in order to attract talented and committed individuals to all levels to the industry. Sweeping away the present confused organisational arrangements and substituting a single delivery body responsible for a unified railway, offers the hope that lines of responsibility and funding will be clarified, strategy and operations will be “joined-up”, and the potential for performance improvements radically maximised. The record of British Rail in the 1980s when subsidy was reduced, financial targets met, investment increased, and service quality improved, demonstrates that an integrated railway can function efficiently. (Paragraph 218)
86. Many of the passenger train franchises are being run as management contracts; franchises have been extended; and Network Rail has taken over rail maintenance directly. This all suggests that the present, fragmented state of the railway is forcing consolidation incrementally on the industry. Whether or not this amounts to “creeping re-nationalisation”, our proposal for a unified public sector Railway Agency responsible for train outputs and the rail infrastructure, sits well with the industry’s present evolution. (Paragraph 219)

87. We do not envisage that this new body would necessarily be required to run all the infrastructure and passenger train services directly. The Government will wish to consider the merits of continuing to involve the private sector in infrastructure provision and passenger train services, where clear benefits exist for doing so; equally, its mind should be far more open than before to the public sector providing services directly where appropriate. Privately owned rail freight companies would continue to operate freight services. In some cases a measure of so-called “vertical integration”, where track and trains are operated by the same body might be appropriate, as in the case of Japan’s regionally based passenger rail companies; and in rural areas the specification of services might be devolved to the local bodies, as in the case of Merseyside. A wide variety of service provisions, tailored locally to passenger requirements, could be accommodated within the arrangements we propose. In general, the provision of rail services needs to take much greater account of local and regional needs. Unifying the delivery of railway services emphatically must not mean bureaucratic centralisation; nor, of course, does it mean breaking up the network. Responsibility for the infrastructure and the delivery of all railway outputs should rest clearly with an Executive Railway Agency acting as the unified train service delivery organisation. (Paragraph 220)

Safety

88. The Secretary of State has pointed out that safety is integral to the railway. It is right that this should be so. It is also right that those regulating rail safety should take full account of the industry’s safety achievements and problems in order to target future effort accurately and use resources effectively. (Paragraph 221)
89. The evidence we have taken in the course of this inquiry indicates that the relationship between the HSE and the industry has broken down. We cannot see how fully effective railway safety regulation can be carried out in these circumstances. It should be a priority for the Government’s review of the railways to consider whether Her Majesty’s Railway Inspectorate should be removed from the HSE and made, either an independent Agency of the Department for Transport, as is the case with the newly established – but regrettably delayed – Rail Accident Investigation Branch, or merged with the new Rail Agency body we have proposed. (Paragraph 222)

Rail Passengers Council

90. A mature industry needs a strong and constructive consumer voice, particularly at times when the industry’s performance is weak, its structure fragmented, and it lacks any strong vision for the future, as at present. We were frankly disappointed with the contribution of the Rail Passengers Council (RPC) to our inquiry. In addition, the profile of the RPC throughout the network is too low. We likened the Council to a ‘secret’ which the industry likes to “keep to itself”. We were concerned, for example, that members of the public who wanted to complain about train services would not find the RPC’s contact details readily available. This needs to change. If this organisation is to make a significant contribution to the debate about the future of the railway, then it will need to represent passengers’ concerns much more powerfully than at present. It may be that a body representing interests of passengers

which is not sponsored directly by the body responsible for the railway, as the RPC is presently by the SRA, would find a more insistent public voice. (Paragraph 223)

Annex 1

Table: British Rail's performance, 1982-1989/90

Year	InterCity punctuality: trains within 5 minutes of booked time	Network SouthEast punctuality: trains within 5 minutes of booked time	InterCity operating results*	Network SouthEast operating results*	Provincial operating results*	All railway operating results*
1982			-£294m	-£465m	-£734m	-£1,484m
1983			-£226m	-£353m	-£696m	-£1,239m
1985/6	85%	87.5%				
1988/9	90%†	90%	+£61m	-£147m	-£498m	-£523m

Source: Mike Anson, Appendix, Tables E2 and J3, in Terry Gourvish, *British Rail 1974-97* (Oxford 2002 and 2004).

† within 10 minutes of booked time

* turnover minus expenditure, before grant, in constant 1989/90 prices

Year	Passenger traffic [bn miles]	Freight traffic [bn tonne-miles]	Gross Investment [constant 1989/90 prices]	Subsidy PSO from central + local govt [constant 1989/90 prices]	Subsidy as % of passenger income %	Central govt subsidy [constant 1989/90 prices]
1982	16.9	9.9	£584m	£1,331m	49	£1,226m
1983	18.3	10.6	£619m	£1,329m	45	£1,218m
1988/9	21.3	11.3	£778m	£648m	25	£567m
1989/90			£891m	£587m	24	£495m

Ibid. Tables A.1, B.2, D.1-2.

Formal minutes

The following Declarations of Interest were made:

Mrs Gwyneth Dunwoody, Member, Associated Society of Locomotive Engineers and Firemen

Mr Brian H Donohoe, Clive Efford, Mrs Louise Ellman and Mr George Stevenson, Members of Transport and General Workers' Union

Ian Lucas and Mr Graham Stringer, Members of MSF Amicus

Miss Anne McIntosh, Member, RAC, Holder of shares in: First Group, Eurotunnel, BAA plc, BA and BAE SYSTEMS

Wednesday 24 March 2004

Members present:

Mrs Gwyneth Dunwoody, in the Chair

Mr Gregory Campbell

Mr Paul Marsden

Mr Brian H Donohoe

Miss Anne McIntosh

Clive Efford

Mr John Randall

Mrs Louise Ellman

Mr George Stevenson

Ian Lucas

Mr Graham Stringer

The Committee deliberated.

Draft Report (*The Future of the Railway*), proposed by the Chairman, brought up and read.

Ordered, That the Chairman's draft Report be read a second time, paragraph by paragraph.

Paragraphs 1 to 3 read and agreed to.

Paragraphs 4 to 15 brought up and read.

Motion made, to leave out paragraphs 4 to 15 and insert the following new paragraphs:

The costs of the railway in Great Britain are enormous. The SRA projected that the national train service would cost £9 billion in 2002-03, up from £6.1 billion in 1999-00. These sums largely comprise rail infrastructure, which is the responsibility of Network Rail, and passenger rail franchising costs, the SRA's direct funding responsibility. The costs of the latter were projected by the SRA to be £3.860 billion in 2004-05, but will not be known until the Government announces the results of its Spending Review in

the summer. The infrastructure costs for the next 5 years are now clear from the Rail Regulator's Access Charges Review 2003: Final Conclusions document published in December and stand at £22.2 billion. The gross revenue requirement for the infrastructure in 2004-05 will be £5.125 billion.

Taking a longer perspective, of the £181.9 billion set aside for transport in the Government's Ten Year Plan, £64.9 billion, approximately one third, is allocated to the railway in the period 2001/02 – 2010/11. Since the Plan was published the Government has had to provide the railway with additional funds, and Mr Richard Bowker has indicated that additional funding will be required. Yet only 6 % of journeys were made by train in Great Britain in 2002, a figure which has not been exceeded in the previous 10 years. Such a disparity between the amounts spent by the Government on the railway, and the proportion of journeys by rail is noteworthy. In these circumstances it is vital that the sums spent represent excellent value for money not only for the fare paying passenger, but for the taxpayer. Is this the case?

The performance of the passenger railway in recent years has been well below par. The most recent figures for the percentage of trains arriving on time - the official public performance measure - is 76.5% which compares with 89.7% in 1997-98, itself the best figure in the period 1997 – 2003. That 1 in 4 trains arrives late demonstrates the train industry's inability, as presently structured, to improve its performance substantially. The underlying causes of delay are broadly attributable to train operators and the infrastructure provider on a 50-50 basis. The performance of the trains depends crucially on the performance of the infrastructure as measured in delay minutes. The Rail Regulator told us that in October 2000, immediately before the Hatfield accident, that the delay on the railway attributable to inefficient infrastructure was 7.7 million minutes with the latest available figures showing a delay total of 14.7 million minutes. These figures were not disputed by Network Rail. The Regulator pointed out that this meant the performance of the infrastructure operator had fallen by 92% since October 2000. It is clear from these figures that neither the fare payer nor the tax payer is presently receiving good value for money from the railway.

A significant contribution to the industry's inability to reduce costs and to pull itself back to pre-Hatfield levels of performance, lies in the confusing and fragmented nature of the railway's present organisation. The Strategic Rail Authority, which is meant to ensure that the performance and growth of the industry are on upward trends, and is officially the industry leader, does not have control over the means of achieving those objectives. It has no control over the Regulator who is responsible for funding Network Rail and specifying its maintenance and renewals outputs in detail; or over Network Rail which is a private company funded by debt, even though the SRA holds stand-by loans which help to guarantee that lending; or over the regulation of safety on the railway which is the sole responsibility of the Health and Safety Executive. The result is that costs have risen sharply: while the scale of work on the WCML upgrade is greater, 16.68 million for the WCML and £1.8 million in the case of the ECML at current prices – provide a dramatic example of how the railway industry has lost control of major projects.

This fragmentation means there is no focus on the needs of the customer. When something does go wrong, passengers are unaware who is responsible and therefore who to complain to. For example, Network Rail are generally at fault over passenger train delays, however the passengers blame the train operating companies. We need to see greater transparency for our travelling public. The Rail Passengers Council, which should be the traveller's champion, is far too low profile. The profile of the RPC throughout the network is too low. We likened the Council to a 'secret' which the industry likes to 'keep to itself'. We were concerned, for example, that members of the public who wanted to complain about train services would not find the RPC's contact details readily available. This needs to change.

Taking a broader view of rail, there is a fundamental lack of clarity about where rail fits into the wider transport planning picture. Funding decisions need to take account of technological and other improvements in all modes of transport, but this rarely seems to happen. For example, bus design and performance has improved significantly over the last 20 years and might benefit from a measure of funding being switched from the railway. We were told that road schemes were subject to efficient and accurate cost benefit analysis, but that the forecasts of increased traffic from rail projects were optimistic, while the forecasts of costs was invariably too low.

The result of the present arrangements is that rational choices by the Government about what to fund are made difficult, if not impossible, risking poor value for money. It is the Government's job to ensure that intra-modal planning, and the subsequent funding decisions, are of the highest quality, and that finite resources are not wasted. Extraordinary amounts of money have been ploughed into a railway which has failed to deliver any significant improvements and has provided excessive profits for the private sector.

These problems can only be addressed by looking at the questions we started with. We take each in turn.

Rail is not necessarily an outmoded form of transport, but it can no longer be taken for granted as the most efficient means of transporting people long distances. As we explored in our aviation inquiry, rail cannot compete with air travel for journeys above three hours. There are circumstances in which bus or coach travel offers a valuable and more flexible alternative to rail. While rail may be a sensible way of moving people around congested city centres, where car use impose a significant external costs, car or coach may be more sensible for inter-urban or rural travel. The aim must be to examine what the railway does best, and how it is best integrated into other modes, rather than to assume that the existing network must be protected at all costs.

We consider the current "mixed mode" railway needs to be reassessed. Academic commentators suggested considerable problems with operations which contain a mixture of freight and passenger trains. Professor Roderick Smith, Head of Mechanical Engineering, Imperial College, London, argues that capacity is limited because of the inherent contradictions of a 'mixed' traffic railway which causes bottlenecks and a 'huge number of conflicting movements', a view shared by Professor David Newbery, Director of the Department of Applied Economics, University of Cambridge. We heard a good deal of evidence about the importance and potential of a dedicated passenger railway. Professor Sir Frederick Holliday argued for the removal of rail freight to road on the basis that this would permit an increase in passenger rail performance sufficient to attract compensating traffic from road to rail. Passenger and freight operations need to be separated more rigorously than at present.

The SRA's Network Output Strategy proposes that rural and freight routes will receive low maintenance priority. The SRA made it clear to us that they did not think that 'retrenchment' was the answer for rural lines, pointing out that closure of the rail infrastructure was inconsistent with the Secretary of State's Directions and Guidance to it and, in any case, cost savings on a part of the network so starved of resources were limited. The SRA has appointed a new Director of Community Rail, and recently published a consultation on a new strategy for Community Railways which seeks to increase passenger volume and income, reduce unit costs and extend community involvement in local railways.

Professor Roderick Smith's evidence to us on the position of the rural railway in Japan, where such lines are owned by so-called 'third sector' companies comprising local authorities and private companies, is interesting and worthy of consideration in the UK. The 37 'third sector' companies run lines varying in length from 6.6 kms to 140 kms. In 2002 these companies carried 50.86 million passengers. Though most of the companies are loss making, vigorous local support means that the companies are well resourced with 20.006 yen being available in 2002 to the companies through various support and stabilisation funds.

The SRA's publication of a consultation document on Community Railways should be used as an opportunity to consider what level of support rural railways should have, and how that support could be delivered without massive direct subsidy. While rural branch lines provide a vital service to passengers they should be protected, but the costs should be reasonable. However, careful integration with other local transport services and significant local involvement of private and public bodies are prerequisites for success.

Our railways compare badly with others. We took extensive evidence from the Dutch railway organisation, and two members of staff paid a study visit to the Netherlands. The structure of railway governance in the Netherlands is far clearer than in the UK; there is no economic regulator, although there is a regulator who determines track access, and no equivalent of the SRA. Although ProRail, the

infrastructure manager, contracts out maintenance and renewals, it is meticulously planned, and ProRail has planned access to each section of the track for at least five hours every four weeks. The Government pays for maintenance separately from new projects, so that it is clear where money has been allocated, and what has been bought. Even though fares are lower than in the United Kingdom, the government owned NS Railway operates as a private company and pays a dividend to government. The operators are expected to focus on their customers' needs, so timetables are set by them. Rail is seen as part of the wider transport system, so that there are facilities for car parking, and interchanges with other modes, such as bus. Larger stations are better equipped for passengers than in the UK, but staff are not provided that small stations, although they do have call centres. In short, a simpler structure and greater focus on passenger needs and providing an appropriate level of service has produced an extremely efficient railway. This should be a model for Britain to follow.

The key to success must be:

- recognition that the rail network is part of the wider transport system, not an end in itself;
- focus on travellers' needs;
- clarity about what expenditure is buying;
- longer-term planning; and
- a realistic assessment of what the system can do, and how it should be improved so that ineffective uses of the railway are identified and discarded, while effective investments, such as those to produce more separation between the passenger and freight network, are supported.

Motion made, and Question put, That the paragraphs be read a second time.

The Committee divided.

Ayes, 1
Mr Brian H Donohoe

Noes, 8
Mr Gregory Campbell
Clive Efford
Mrs Louise Ellman
Ian Lucas
Paul Marsden
Mr John Randall
Mr George Stevenson
Mr Graham Stringer

So the Question was negatived

Paragraphs 4 to 15 agreed to.

Paragraphs 16 to 223 read and agreed to.

Annex agreed to.

Resolved, That the Report be the Seventh Report of the Committee to the House.

Ordered, That the Chairman do make the Report to the House.

Ordered, That the provisions of Standing Order No. 134 (Select committee (reports)) be applied to the Report.

Ordered, That the Appendices to the Minutes of Evidence taken before the Committee be reported to the House.

[Adjourned till Wednesday 31 March at 2.30 pm

Witnesses

Wednesday 25 June 2003

Mr John Armitt, Chief Executive, and **Mr Iain Coucher**, Deputy Chief Executive, Network Rail

Mr Tom Winsor, Rail Regulator, **Mr Michael Beswick**, Chief Rail Advisor, and **Mr Keith Webb**, Director, Corporate Affairs, Office of the Rail Regulator

Tuesday 8 July 2003

Mr Richard Bowker, Chairman, Strategic Rail Authority

Wednesday 15 October 2003

Professor Mark Casson, University of Reading

Professor Stephen Glaister, Imperial College, London

Dr Tim Leunig, London School of Economics and Political Science

Professor David Newbery, University of Cambridge

Mr Jonathan Tyler, Principal, Passenger Transport Networks

Mr Michael John Hughes, Chairman, and **Mr Keith Rodwell**, Deputy Chairman, Railfreight Interchange Investment Group

Ms Philippa Edmunds, Freight on Rail

Mr Stephen Joseph, Executive Director, Transport 2000

Mr Robert Goundry, Director of Strategy, Freightliner Group

Mr Neil McNicholas, Managing Director, Direct Rail Services

Mr Michael Schabas, Director, GB Railfreight

Mr Graham Smith, Planning Director, English Welsh and Scottish Railway (EWS)

Mr Mick Rix, General Secretary, Associated Society of Locomotive Engineers & Firemen (ASLEF)

Mr Paul Wright, Head of Logistics, and **Mr Peter Wildman**, Transport Development Manager, ASDA

Mr Allan Leighton, Chairman, **Mr Paul Bateson**, Managing Director Logistics, and **Mr John Nicolson**, Transport Review Director, Royal Mail

Wednesday 22 October 2003

Mr David Clarke, Strategy Director, Jarvis Rail

Mr Collin Carr, Engineering Director, Amey Rail

Mr Andrew Rose, Chief Operating Officer, Balfour Beatty Rail

Dr Keith Lloyd, Representative of Alstrom Transport UK

Mr Per Staehr, Chief Country Representative, Bombardier Transport UK Ltd.

Mr Anton Valk, Managing Director, NedRailways

Mr Gerlof Den Burman, Project Manager, ProRail

Mr Tom Winsor, Rail Regulator, **Mr Michael Beswick**, Director, Rail Policy and Chief Rail Advisor, **Mr John Thomas**, Head of Regulatory Economics, and **Mr Andrew Burgess**, European Policy and Competition Specialist, Office of the International Rail Regulator

Professor Roderick Smith, Imperial College, London

Professor Chris Nash, Institute for Transport Studies, University of Leeds

Mr Shaun Thomas, General Manager, and **Mr David Markham**, Transport and Recreation Advisor, English Nature

Professor Sir Frederick Holliday

Wednesday 29 October 2003

Mr Christopher Garnett, Chief Executive, GNER

Mr Olivier Brousse, Chief Executive, Connex Transport UK Ltd.

Mr Mark Beckett, Business Development Director, Chiltern Railways

Mr Patrick Verwer, Managing Director, Merseyrail Electrics

Mr Roy Wicks, Director General, South Yorkshire PTE

Mr Neil Scales, Director General, Merseytravel

Mr David Hoggarth, Assistant Director, Passenger Transport Executive Group

Mr Robert Crow, General Secretary, and **Mr Ken Sharpe**, Council of Executives Member, RMT

Mr Richard Rosser, General Secretary, TSSA

Mr Tom Winsor, Rail Regulator, **Mr Michael Beswick**, Director, Rail Policy and Chief Rail Advisor, and **Mr John Thomas**, Head of Regulatory Economics, Office of the Rail Regulator

Wednesday 5 November 2003

Mr Stewart Francis, Chairman, and **Ms Vinita Nawathe**, Policy Research Manager, Rail Passengers Council

Ms Christine Knights, Chair, North Eastern England Rail Passengers Committee

Mr Ian McAllister, Chairman, **Mr John Armitt**, Chief Executive, and **Mr Iain Coucher**, Deputy Chief Executive, Network Rail

Mr Richard Bowker, Chairman and Chief Executive, Strategic Rail Authority (SRA)

Dr Kim Howells, a Member of the House, Minister for Transport, and **Mr Phil West**, Head of Railways Delivery, Strategy and Communications, Department for Transport

Wednesday 7 January 2004

Mr John Armitt, Chief Executive, **Mr Iain Coucher**, Deputy Chief Executive, and **Mr Andrew McNaughton**, Chief Engineer, Network Rail

Dr Allan Sefton, Director of Rail Safety, and **Mr Nick Starling**, Policy Director, Health and Safety Executive

Mr Len Porter, Chief Executive, **Mr Anson Jack**, Acting Director, Standards, and **Mr Aidan Nelson**, Director Policy and Strategic Initiatives, Rail Safety and Standards Board

Mr Alan Osborne, Former Director of Rail Safety, Health and Safety Executive

List of written evidence

FOR

- 1 Alan Crowhurst Esq
- 2 Dr Roger Sexton
- 3 Richard Spencer Esq
- 4 Freightliner Group
- 5 Liam Powell Esq
- 6 Symonds Group Ltd
- 7 North Yorkshire CPRE
- 8 Graham Zeitlin Esq
- 9 AJ Lucking Esq
- 10 Manchester Chamber of Commerce and Industry
- 11 T Martin Blaiklock Esq
- 12 W J Measure Esq
- 13 Shrewsbury to Aberystwyth Rail Passenger Association
- 14 Dr John Disney
- 15 The Potter Group
- 16 Tony Bolden Esq and Reg Harman Esq
- 17 Railway Development Society, Midlands Branch
- 18 Coaley Junction Action Committee
- 19 Independent Transport Commission
- 20 John Busby Esq
- 21 English Nature
- 22 Manningtree Rail Users Association
- 23 Rail Research UK
- 24 Dr Tim Leunig
- 25 Transwatch UK
- 26 Colin Buchanan and Partners
- 27 The Association of Community-Rail Partnerships
- 28 The Public Transport Consortium
- 29 Laing Rail Ltd
- 30 Chingford Line Users' Association
- 31 The Royal Town Planning Institute
- 32 Rail Passengers Committee for Southern England
- 33 Hutchison Ports (UK) Limited
- 34 FirstGroup plc
- 35 The Royal Academy of Engineering
- 36 Kellogg Brown & Root (UK) Ltd
- 37 Freight on Rail
- 38 Transport 2000
- 39 National Union of Rail, Maritime & Transport Workers
- 40 Greater Manchester Passenger Transport Authority and Executive
- 41 Associated Society of Locomotive Engineers & Firemen

FOR

- 42 The Railway Forum
- 43 Professor Roderick A Smith
- 44 North East Assembly
- 45 English Welsh and Scottish Railway
- 46 Soroptimist International of South East England
- 47 Tyne Valley Rail Users' Group
- 48 Richard Bradford Esq
- 49 The Tandem Club
- 50 Freight Transport Association
- 51 Professor Stephen Glaister
- 52 Sustrans
- 53 AEA Technology
- 54 Professor Mark Casson
- 55 Rail Freight Group
- 56 Transport 2000, Herefordshire and Worcestershire
- 57 Network Rail
- 58 Railway Development Society, North East Branch
- 59 South West Regional Assembly
- 60 London Transport Users Committee
- 61 TSSA
- 62 Passenger Transport Executive Group
- 63 Rail Freight Interchange Investment Group
- 64 Institution of Civil Engineers
- 65 The Corporation of London
- 66 North West Regional Assembly
- 67 Maersk Company Ltd
- 68 The British Chambers of Commerce
- 69 West Midlands Regional Assembly
- 70 Birmingham Chamber of Commerce and Industry
- 71 Manchester Airport Group
- 72 Rail Passengers Council and Committee Network
- 73 British Ports Association
- 74 Cyclists Touring Club
- 75 Transport 2000 South West Network
- 76 National Express Group
- 77 Department for Transport
- 78 Professor David Newbery
- 79 Christian Wolmar Esq
- 80 Cast.Iron
- 81 David Stallard Esq
- 82 Stephen Plowden Esq
- 83 D Scott Hellewell
- 84 Passenger Transport Networks
- 85 Local Government Association

FOR

- 86 Bryan Frost Esq
- 87 David Crathorn Esq
- 88 Roger Ford Esq
- 89 East Suffolk Travellers' Association
- 90 National Federation of the Blind of the United Kingdom
- 91 Nederlandse Spoorwegen
- 92 Nigel Gansell Esq
- 93 Friends of the Earth
- 94 Dr Dieter Helm
- 95 Association of Train Operating Companies
- 96 Dr Mayer Hillman
- 97 Strategic Rail Authority
- 98 Gloucestershire County Council
- 99 Office of the Rail Regulator
- 100 I D King Esq
- 101 Direct Link North
- 102 Engineering and Physical Sciences Research Council (EPSRC)
- 103 Professor Sir Frederick Holliday
- 104 Direct Rail Services
- 105 Royal Mail plc
- 106 Asda
- 107 Bombardier
- 108 GB Railfreight
- 109 Transport for London
- 110 Jarvis
- 111 Balfour Beatty
- 112 Amey
- 113 Connex
- 114 Merseyrail
- 115 GNER
- 116 D Dalton Esq
- 117 RailFuture
- 118 Central Japan Railway Company
- 119 Quality Transport Partnership
- 120 Mark Blathwayt Esq
- 121 East Japan Railway Company
- 122 Health and Safety Executive
- 123 Rail Safety and Standards Board
- 124 Alan Osborne Esq
- 125 TUC
- 126 R M Bell Esq, D A Marshall Esq and P G Rayner Esq

Supplementary Evidence

FOR

- 21A English Nature
- 23A Rail Research UK
- 39A RMT
- 42A Railway Forum
- 53A Professor Roderick Smith
- 57A Network Rail
- 57B Network Rail
- 57C Network Rail
- 62A PTE Group
- 72A Rail Passengers Council
- 77A Department for Transport
- 77B Department for Transport
- 78A David Newbery
- 84A Passenger Transport Networks
- 91A Nederlandse Spoorwegen
- 95A ATOC
- 97A Strategic Rail Authority
- 97B Strategic Rail Authority
- 97C Strategic Rail Authority
- 99A Office of the Rail Regulator
- 99B Office of the Rail Regulator
- 106A Supplementary by Asda
- 107A Bombardier
- 107B Bombardier
- 110A Jarvis
- 114A Merseyrail Electrics
- 122A HSE
- 122B HSE
- 124a Alan Osborne
- 124B Alan Osborne

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Third Special Report	Government Response to the Eighteenth Report of the Transport, Local Government and the Regions Committee of Session 2001-02, National Air Traffic Services' Finances	HC 1305