

Train Operators
Working Together

ATOOC



Better alignment of train and track:

Proposals by ATOOC

September 2010

Introduction

1. Since Network Rail was created, the two halves of the passenger rail industry – infrastructure owner/operator and train operators – have delivered significant whole industry improvements in performance and safety. This has not been sufficiently the case with costs and the consequence is the current focus of government and industry on improving efficiency, with the McNulty Value for Money Study a key piece of work the entire industry is engaged in.
2. It is no coincidence that in the areas of performance and safety the industry has established effective alignment of organisations and incentives. It is best illustrated by the Route-based approach to tackling performance as a joint enterprise between Network Rail and TOCs.
3. ATOC believes that if a similar approach is applied in aligning the two halves of the industry in the areas of whole industry cost and efficiency, then both immediate cost savings and, longer term, significant improvements in value for money can be delivered. Importantly, better alignment of train and track will also produce a railway more responsive to the needs and aspirations of passengers.
4. There are six principles to adhere to in considering how to achieve better alignment:
 - Greater transparency of industry income and costs. At present there is more transparency on the train side because of the existence of 19 separate TOCs. On the track side, transparency should extend down to Route level.
 - Decision making should be moved closer to the customer and in particular choices about infrastructure spend should be driven more closely by the market. Overhead structures should be the minimum needed for consistency of standards.
 - Boundaries and interfaces within the industry should be adjusted to reflect a more logical split of responsibilities, which in turn will also result in a shorter chain for decision making and hence speed up cost savings.
 - Both renewal and enhancement projects should be planned and prioritised by their positive impact on passenger experience and incremental revenue or passenger volume.
5. The alignment achieved on performance and safety should be enhanced.
6. Different models for implementing better alignment between train and track can work equally well in different situations. There is no one approach that is necessarily best for all parts of the network.
5. ATOC proposes five steps by which better alignment can be achieved, consistent with the principles above. Taken progressively, they would lead in time to a substantially non-public sector industry, with less government involvement and more private sector investment.
6. Each step implies significant change both in the way the two halves of the industry relate to each other and in the way they are structured and organised.
7. The ideas presented below are high level in nature. We stand ready to work them through in greater detail, in parallel with our input to the McNulty Study and the consultation on franchise reform, to both of which they are closely linked.

Step 1:

Strengthen the local TOC/Network Rail relationship

8. The examples of whole industry performance and safety confirm train operators in the view that things often seem to work best at a sub-national level and one of the strongest and best aligned relationships is between Route Directors and TOCs.
9. The beneficial effects of this aligned relationship could be extended by giving more authority and resource to Route Directors. Coupled with more transparency of costs and income at Route level, it would then lead naturally to establishment of self-standing business units within Network Rail by Route.
10. Each business unit would have clear accountability for operations, maintenance and renewal within its geographical area. Nationally, Network Rail would focus on ensuring the leanest possible overhead structure to enable essential network-wide coordination between business units and network-wide support activities such as timetabling, access and technical standards. The opportunity to make comparisons between business units would exert strong pressure to control costs.
11. The relevant TOC(s) and the business unit would work together to deliver passenger services at the lowest whole industry cost and each should be able to benefit from joint success in reducing costs. This could be achieved by, at one end of the spectrum, an informal “alliance” approach, in which both sides work voluntarily to reduce cost together. At the other end of the spectrum, working together for whole industry benefit could be the subject of regulatory oversight through a formal commercial relationship under which cost savings are shared between the TOC, the business unit and the taxpayer on a pre-agreed formula.
12. Whatever the precise approach, the advantage of the strengthened local relationship is that decisions and plans are developed and made with a closer focus on passenger need than at present.
13. To facilitate this, the regulatory regime should strengthen the position of the operator as customer under the track access agreement. Each agreement would incorporate key deliverables, such as targets for joint cost reduction, performance, network availability/capability etc. It should be backed by increased variable access charges (to better align the economic impact on train and track of fluctuations in demand), gain share arrangements (both on costs and revenue) and, in extremis, the ability of the operator to withhold payment for significant failure by the supplier.
14. To further entrench the customer/supplier relationship at local level, those elements of the DfT grant that currently go direct to Network Rail should flow via operators (as was the case until 2000).
15. The benefits of a local relationship strengthened as above would be:
 - The ability to benchmark business performance across different parts of the network and so drive cost-reduction;
 - Faster, more local decision making;
 - Better alignment with the needs of the passenger.

Step 2:

Develop different splits of responsibility at local level

16. The closer relationships described in Step 1 provide a ready basis for moves towards more vertical integration within the industry, which may be a good option in some circumstances for achieving further alignment between train and track. Two important principles when considering vertical integration are:
 - Some parts of the network are better suited than others;
 - There can be wide variation in the “depth” of the integration.
17. A clear objective of any vertical integration should be to extend the role of the private sector, as a means of introducing competition and innovation into aspects of the railway beyond pure train operation.
18. Compared to the status quo, the first and most limited step of vertical integration would be to make the train operator responsible for signalling and control. The next stage would be to add Mobile Operations Managers to the train operator. The next stage beyond that would be to make the train operator responsible for maintenance of track and associated systems; the next stage would add renewals responsibility as well; and finally full asset ownership and responsibility (which would be a radical departure from today’s railway and a very significant step in commercial, regulatory and operational terms).
19. There are already precedents for “shallower” vertical integration. Tyne and Wear Metro, London Underground and the French national railway are all examples of train operators taking responsibility for signalling, control and frontline maintenance intervention, with a (separate) infrastructure provider responsible for cyclical maintenance and renewal as well as asset ownership.
20. Vertical integration options must address the needs of passenger and freight companies who are not the lead operator in each area. This can be readily achieved by keeping in place the existing UK regime governing third-party access.
21. The principle that different models might be right for different circumstances is particularly applicable when considering vertical integration. Proposals to introduce vertical integration could be invited as part of franchise competitions – both Essex Thameside and Greater Anglia, each of which is largely self-contained operationally, would make interesting pilots.
22. The benefits of vertical integration trials would be:
 - Introduction of new companies into the role of infrastructure provider, giving further benchmarking and cost reduction possibilities;
 - Still better alignment of train and track by a more logical boundary between train operations and infrastructure provision;
 - Concentration of operational decisions in one place – to the advantage of the passenger.

Step 3:

New arrangements for railway operational property

23. There is strong evidence that train operators, with lower overheads and shorter chains of command, can maintain, renew and enhance stations at lower cost than Network Rail. ATOC estimates these saving would amount to £250-500 million over the five years of CP4. To enable this to happen, TOCs should be granted fully repairing and insuring, long term leases at stations; and Network Rail would be able to step back from its operational property responsibility and act purely as a ground landlord.
24. There is already a significant degree of common ground within the industry on moving to this arrangement for category B – F stations. TOCs should also be given the opportunity to compete for the running of Major Stations as part of refranchising, and to take on the commercial development of operational property in most circumstances. There is an opportunity to introduce and test the arrangement in the two franchise competitions due shortly.
25. A further step for those stations remaining under the active management of Network Rail for many years pending refranchising, and for the execution of the landlord role described above, would be to transfer Network Rail's property interests to an entirely new company. There is logic to this in that the railway operational and station responsibility parts of Network Rail's business are largely unrelated.
26. The benefits of substantial reform to the commercial arrangements for stations as described above would be:
 - Streamlined management with a commercial and holistic focus on the management of stations, including the impact on passenger revenue;
 - A route to lower cost maintenance and upkeep of the national station estate;
 - Better focus on investments and developments at stations that suit passenger needs and that drive incremental revenue;
 - A better basis for partnering with developers wishing to put significant investment into stations.

Step 4:

Integrate train and track in network enhancements

27. Enhancements to the network account for a significant element of Network Rail's expenditure. Generally, the input to enhancement schemes, whether at the development, design or implementation stage, that train operators can make is quite limited. This can lead to subsequent problems, ranging from a clash between infrastructure design and operating practice through to construction of a scheme that delivers little passenger or revenue benefit. There are a number of examples of this from the West Coast Route Modernisation, including the layouts at Stockport and Nuneaton, and the re-signalling at Norton Bridge.
28. There are two ways of giving train operators greater involvement.
- a) Except perhaps for the very largest schemes (of the scale of Thameslink and major Route modernisations), place responsibility for enhancements into the local business units described under Step 1. This will ensure that the affected operator(s) can be involved from the outset (but in a stronger position as customer than now) in determining the output the enhancement is to deliver, sifting options, designing the detail with an eye to future operation, planning implementation around day-to-day operational constraints and, finally, commissioning and bringing into operation.
- b) Encouraging TOCs to bid on enhancements as part of longer, investment-led franchises. In this instance the TOC would take the lead on scoping, financing and managing the enhancement, with its local Network Rail business unit acting as a delivery partner to agree implementation details. Construction work would be competitively tendered and on completion, subject to satisfactory handover tests, the OMR responsibility would pass to the NR business unit. Precedents for this type of arrangement exist in the Evergreen projects promoted by Chiltern.
29. We recognise that, in the case of the largest and most complicated enhancement projects (such as those involving multiple players in specifying, funding and delivering a scheme), alternative arrangements may be needed and we are committed to working with our partners in the industry on what such arrangements should be. However, while projects of this sort are significant in their own right, they represent only one part of the overall programme of capital expenditure on the network. Developing new solutions for these projects should not hold back adoption of the other reforms proposed in this note which have the potential to deliver benefit to passengers and taxpayers.
30. The benefits of integrating train and track in enhancements would be:
- Potential for increased contestability in enhancement work;
 - Avoidance of wrong or redundant functionality in the design of an enhancement;
 - More rapid progress on schemes;
 - Focus on downstream passenger and revenue benefits at the planning stage;
 - Better alignment of engineering proposals with passenger and operational need.

Step 5:

Realise value by selective sell off

31. The four steps outlined above create the possibility of today's Network Rail becoming a collection of semi-independent units whose business is ownership, management and (partial) operation of infrastructure in a working alliance with their train operator customers; and also the possibility of a new property company. In time, any or even all of these could be sold as standalone businesses, realising significant value and achieving transfer to the private sector.
32. There is a clear precedent for the sale of a geographically based unit in the current process to sell HS1. There are many precedents in other utility sectors of national monopolies being commercialised and broken into standalone regional companies.

Role of the Regulator

33. Under the steps outlined above, the Regulator would continue to play an important role but it would change to reflect the fact that train operators would provide closer day-to-day scrutiny of Network Rail's planning and spending under this structure. ORR would therefore over time be able to concentrate more strongly on the strategic aspects of regulation, rather than on the detail of Network Rail's spending. Separate price controls might be applied over time to each business unit, just as is the case currently between England & Wales and Scotland, and eventually each business unit could have a RAB and capital structure consistent with its own circumstances. ORR would continue to administer the track access regime, particularly in ensuring that all passenger and freight operators were treated fairly on routes where they compete, either for customers or for access.

Conclusion

Better alignment and integration of track and train is at the heart of these proposals.

The industry's progress on performance and safety provides evidence of what can be achieved.

The steps outlined in this paper provide a route to whole industry improvements in:

- Financial transparency
- Cost reduction
- Value for money
- Meeting the needs of passengers