Consultation response

To:

Office of Rail Regulation Consultation on Structure of Costs and Charges

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1. Introduction

1.1 ***pteg*** represents the seven Passenger Transport Executives of England and Scotland which between them serve more than thirteen million people in Strathclyde, Tyne and Wear ('Nexus'), West Yorkshire ('Metro'), South Yorkshire, Greater Manchester, Merseyside ('Merseytravel') and the West Midlands ('Centro').

1.2 Britain's PTEs are the driving force behind the development of public transport in some of Britain's largest City Regions. Their responsibilities include:

- producing the strategies for the development of local public transport networks
- planning and managing local rail services (in partnership with the SRA)
- planning and funding socially necessary bus routes
- working in partnership with private operators to improve bus services—for example through bus priority schemes
- running concessionary travel schemes—including those for older, disabled and young people
- investing in local public transport networks—including new rail and bus stations
- developing and promoting new public transport schemes—like light rail and guided bus networks
- providing impartial and comprehensive public transport information services—including by phone and internet
- managing and maintaining bus interchanges, bus stops and shelters

1.3 In some cases PTEs are the operators of public transport, such as the Tyne and Wear Metro, Glasgow Subway and some ferry services. However, most public transport in PTE areas is operated by private companies

1.4 The PTEs have a combined budget of more than a billion pounds a year, and are funded by a combination of local council tax and grants from national government. They are responsible to Passenger Transport Authorities (PTAs), made up of representatives of local councils in the areas they serve.

1.5 ***pteg*** welcomes the opportunity to respond to the ORR's consultation on the Structure of Charges and Costs. ***pteg*** believes that the financial structure of the industry has proven to be a key weakness and hampered the delivery of value for money for the taxpayer. Using the Track Access Agreements as the prime vehicle for funding NR has not been successful, and it has not cemented a good customer-supplier relationship. The TOCs don't see that their funding of NR is clearly related to the train services they operate, and all they are doing is acting as a post-box to pass funding between the government and NR.

2 Structure of Charges

2.1 Under the new industry structure, NR has two key groups of customers. Firstly TOCs, FOCs and other direct users of NR's services and facilities, and secondly the government which will be deciding the overall shape and size of the network and will be making decisions on the overall outputs. It therefore makes sense that the financial structure reflects the role of these two groups of customers.

2.2 The bulk of NR's funding should come from direct grant from government, and should reflect the fixed costs associated with NR providing an overall network which has the capabilities and outputs specified by the government. This funding arrangement would cement the relationship between NR and the government. Additional local or regional funding could be provided if a local funder (such as a PTE) wished to purchase a higher level of output than specified by the DfT.

2.3 TOCs would then have a much simplified contract with NR, and they would pay much lower access charges which are based only on the additional costs that the operation of their services impose on NR. Such an arrangement should improve the TOC/NR relationship, as the money flows will be far more aligned with NR's direct costs for providing services to the TOCs.

2.4 Under this overall framework, the base rail network is specified and provided by the government to train operators, which then pay the marginal costs associated with operating their services. This structure is then fully aligned with the policy of allowing local stakeholders such as PTEs to purchase additional services at marginal cost (where capacity allows), as effectively all TOC's services are provided at marginal cost by NR.

2.5 This model would also make the finances of the franchises more transparent, and allow for better decisions on the value for money of services to be made.

2.6 Making the above structure operate sensibly would require the Government to review how it wished define Network Rail as a company. Clearly under the proposed model, the bulk of NR's funding would probably come from the government directly, which is likely to cause difficulties with NR's theoretical private sector status. However, there are considerable transaction costs associated with passing large amounts of money through franchise agreements, especially when Clause 18.1 provisions are enacted. It must represent better use of public funding, as well as industry staff resources, for more money to pass directly to NR from the government.

3 Costs

3.1 In order for the above proposed structure to operate effectively, a clear understanding of NR costs is needed, and ***pteg*** supports the proposed development of a NR cost model. Given the government's longer-term aim to give PTEs' greater local financial responsibility once costs can be allocated more effectively, we see the development of this model as being of critical importance.

3.2 The model will clearly need to deal with issues of geographical disaggregation, and this should include being able to define costs within PTE areas, and not just at route level. The PTEs would like this work to be completed as soon as possible, however this should not be at the expense of accuracy.

3.3 ***pteg*** considers that the change in grant regime outlined above could be implemented quickly based on the current fixed/variable charge split. This would then be amended in the light of the outputs of the cost model. It may, however, be more straightforward to implement all the changes to the charging structure at such a time when the outputs of the cost model are known. This would avoid the industry having to go through two rounds of complex changes.

3.4 As ***pteg*** is proposing radical changes to the Schedule 8 Performance Regime, the existing capacity charge certainly ought to be reviewed.

3.5 ***pteg*** would also welcome a review of the current practice of access rights and charges not being applicable to empty stock moves. This is creating a number of instances where TOCs are operating services as ECS because they do not have access rights for them, when they could just as easily be operating in passenger service and providing greater industry and passenger benefits.

4 Conclusions

4.1 While PTEs have been insulated up to now from the full impact of the changes in access charges by the SRA grant mechanism, this is not expected to be the case into the future. PTEs will therefore be more fully exposed to changes in both the charging structure and level of costs, and therefore the need confidence in the mechanisms used.

4.2 The introduction of the current industry cost structure radically changed the basis under which PTEs funded rail services. Under British Rail, PTE services were often considered marginal users of the network and on this basis PTEs were therefore able to fund rail services from local funding sources. At the time of privatisation and the creation of Railtrack, the costs attributable for PTE rail services soared to such an extent that the government had to agree to fund local rail service costs directly, as they would otherwise have been unaffordable. The cost rises were largely attributable to the track access charges. In the case of South Yorkshire, for example, the costs of operating the rail network rose from £10m in 1995 to £24m in 1996. As income remained around £5m, the subsidy rose from about £4m to £19m virtually overnight.

4.3 ***pteg*** is therefore keen to ensure that any charging mechanism for track access provides a fair basis for the PTEs to debate the value of urban local services with the Government, and will allow our continued future investment in rail services to be both affordable and value for money.