Written response to the Shaw scoping report

This is Transport for London's response to *The future shape and financing of Network Rail: The scope*. TfL believes it has particular insight as it has transport planning, passenger service contracting, infrastructure management and operations experience within the TfL family.

Introductory overview

TfL believes that there is a strong case for a system-wide change to make the railway more accountable and responsive both to the railway's customers and to its funders that will indeed bring benefit to the UK's economy as a whole. The structure needs to have the customer or relevant market at its heart. Rail's markets can be broken down into the following:

1. InterCity where TOCs face real competition and should be instrumental in defining the service offering
2. City/Regions – London and the South East, the North and West Midlands where rail provision is tied in with regional planning, development and housing
3. Other regional services, many of which are already devolved to Scotland and Wales
4. Freight which is in many cases serving declining markets

Crucially these markets are not coterminous with Network Rail's current route structure. TfL proposes an evolution over time in Network Rail's structure to reflect the economic geography and increasingly the devolved political geography of the UK. Network Rail should not be broken up into separate entities but its management and delivery structure should evolve as the rail industry changes. Hence, Network Rail would:

- be structured over time around a number of regional entities reflecting the main regional passenger flows such as the West Midlands, North of England, Wales, Scotland and London & the South East
- continue to have funding set in five yearly blocks to provide some stability and planning certainty

These regional business units would be based in centres where the main high volume regional passenger flows exist. They would be accountable for passenger contracts that deliver day to day high performance as well as a portfolio of projects that yield the promised transport and economic outcomes. This would also correlate with the fact that enhancements are increasingly being funded by third party funders like TfL, developers and airports, with private sector funders arguably becoming even more crucial given ongoing constraints on public sector funding. ORR would have an arbitration role where there are potential conflicts between inter-regional requirements or with national requirements for InterCity services. Such regional devolution would also enable ORR to benchmark more effectively.

DfT would retain its UK-wide role, remaining accountable for the InterCity services and co-ordinating across regional partnership bodies as well as helping competence across more organisations. Passenger contracts would be let by DfT/Rail Executive, TfL, Transport Scotland and Transport for the North. Such change would be evolutionary in the sense that not all regional bodies need be set up simultaneously and each could take on additional functions over time.

For London and the South East, a market-focused infrastructure organisation should reflect the changing structure of service specification and contracting. TfL is increasingly looking to work in partnership with DfT and such a regional entity could interface with a corresponding part of Network Rail. This would enable a move towards greater single point accountability for rail services.

The strategic planning and decision making functions of Network Rail could be brought together with those of DfT into a strategic body at national level or a number of regional bodies.

The impacts go well beyond Network Rail, and planning as a whole has to take account of the changing patterns of economic activity which in turn affects transport provision and investment choices. The economic history of the last twenty years is that high-value employment sites are tending to cluster more greatly This requires an adequate supply of labour, in turn affected by housing supply. The London Plan identifies a need for 49,000 new homes per year, though the rate has been around half this over the last ten years or so. The resulting poor affordability of housing reduces the quality of life the city offers its labour force, which has damaging consequences for its international competitiveness. If unaddressed, this will affect the ability of London firms to recruit and expand. The need for more housebuilding especially in London means that rail schemes are increasingly being developed to improve accessibility to development sites, not just demand levels on existing routes and at existing stations. Barking Riverside, Brent Cross and Meridian Water are examples. It is essential for future growth that there is more a joined up approach to transport and land use planning between Network Rail, agents of central government and local authorities. Hence there is another reason to bring the customer (passengers & regional transport authorities) closer to the heart of the railway and its processes.

Response to the report's questions

1. What are your views on the scope of Network Rail's functions?

The majority of Network Rail's functions are core to the management and the operation of the railway infrastructure. Of the list in paragraph 3.9 however, three stand out as being non core:

- Owning and operating light maintenance depots for rolling stock which could be carried out by other organisations.
- Management of major stations. Network Rail does not have a direct interface with rail customers despite managing a number of major stations and there is scope to improve customer service. Network Rail has a role in maintaining non-discrimination between train operators at major stations.
- Commercial businesses such as Network Rail consulting

2. Have we failed to mention any specific and important factors?

Infrastructure planning and enhancement needs to be led by organisations with a long term perspective as incentives and timescales do not coincide with franchise dates. The report should also acknowledge that enhancements are increasingly being funded by third party funders like TfL, developers and airports. TOCs have an incentive to expand their operations but this could be at long term cost in terms of capacity or reliability.

3. What are your views on these accountability arrangements and their effectiveness?

Accountability across the railway industry is inadequate. It is too frequently the case that multiple parties have involvement in a function that the railway undertakes, but without any one having whole industry single-point accountability.

There is a dichotomy between the National Rail network and London Underground accountability arrangements. The latter has a model that more closely achieves the single-point accountability which TfL feels is desirable. TfL also has accountability to the Mayor which results in a greater focus on customer service and delivery. This means that TfL has a greater focus on the performance and customer service delivery of its rail concessions than does DfT for its franchises. When there is a problem on the network, TfL takes the approach that it may not be its fault but it is its problem.

Although it may not be possible to create single-point accountability, creating a Network Rail management structure more closely aligned to its customers and increasing its focus on their requirements would increase accountability.

4. Have we correctly identified and defined Network Rail's customers?

The ultimate customers of Network Rail are the rail passengers who choose to pay for their travel and the taxpayers who subsidise rail services.

Transport for London (TfL) and London Underground (LU) are identified as regulated entities in the report. TfL and LU are customers of Network Rail in that they pay track access charges to Network Rail to gain access for contracted and directly operated passenger rail services as well as funding similar elements of Network Rail enhancements. TfL's heavy rail operations will account for 20 per cent of UK passenger demand when Crossrail is open, making TfL a large customer.

TfL's role as specifier, funder and customer appears to have been overlooked by the scoping study. TfL also has a focus on the passenger through its customer facing remit.

5. How effectively are customer needs and expectations met by Network Rail at present?

As a customer of Network Rail, TfL considers that the strategic planning function involves it reasonably well and is generally content with the process.

However, analysis finds that performance on the Network Rail interface sections of the network is considerably lower than on the LU sections of the same lines. Network Rail states that it is funded only for a PPM of 92.5 per cent, but the current MAA of 89.5% means it does not currently meet this target overall.

It does not aim for the higher performance which TfL believes is vital for heavily used metro services that use these lines. Network Rail used to have regional targets and these should be reinstated with devolved targets which are appropriate to the markets being served. A national target is not appropriate for services as diverse as those to Truro, Thurso and Tottenham Hale. A higher target should be set for London and South East Commuter services. The industry could also usefully review whether PPM is the best possible measure that drives the right behaviours for high intensity services. LU uses measures such as lost customer hours, similar in some ways to delay minutes, and excess journey time, which avoid the use of potentially distorting thresholds found within the PPM measure.

6. Should direct customer pressure on Network Rail be strengthened? If so, how might this be achieved?

Direct customer pressure on Network Rail should be strengthened. There are a number of ways by which this could be achieved:

- A bigger role of regional bodies based around centres with the big regional passenger flows
- A more active sponsorship function by these regional bodies and funders in general
- More third party projects on network, which requires regulatory change to make this easier.
- An ORR function that has greater ability to benchmark infrastructure performance

TfL does not believe that a restructuring of access charges to increase the share of Network Rail's revenue that comes from TOCs rather than Network Grant will necessarily increase customer pressure. Most TOCs are held harmless by Government from changes in access charges and would not be incentivised to put pressure on Network Rail to improve performance.

7. Are there more positive incentives for delivery which would be useful? Are any of these incentives more effective than others?

TfL does not believe that present corporate financial incentives are effective or meaningful in a nationalised environment, hence it suggests an alternative approach above to generate greater ownership and accountability. Appropriate incentives could be designed to make management more responsive to customers. This is not to say that individual contracts with specific contractors should not have incentives provisions and /or scope for liquidated damages.

At present, Network Rail is mainly incentivised by ORR but incentives do not deal effectively with all types of poor performance. ORR Licence Enforcement should be reserved for sustained systemic failings whilst giving greater direct remedies to Network Rail's customers under their contracts.

8. Is there a case for changing the route structure and what are the advantages and disadvantages of different approaches to disaggregating the network, for example on the basis of:

TfL believes the review should examine in detail the case for a change in Network Rail's structure to reflect the economic geography and increasingly the devolved political geography of the UK. The current radial route structure which derived from old railway geography does match today's patterns of commuting demand. Nor does it fit with the geography of funders and specifiers in London, the Midlands or the North. Instead a more market based structure centred around devolved government would be appropriate.

There is a risk that an opportunity to increase the effectiveness of Network Rail's structure could be lost in a short term move to devolve more power to the existing routes.

The London commuter market is currently served by all of Network Rail's English routes, increasing the number of interfaces and reducing the scope for planning and delivery of infrastructure in an integrated way. There is therefore a case for disaggregation on a market based structure with routes serving London commuter services being separate from those serving InterCity services. Further decentralisation should focus on operations and maintenance allowing comparison and benchmarking between different regions.

Under this structure, there could be a greater London and South East market focus on the following functions:

Customer Service Delivery	• "Single source" of real-time information for customers • Consistent fares and ticketing solutions • Improved quality of station operations, with better links to the local area and consistent customer service

Command & Control	• Better coordinated command & control structure across the region • Standardised communication protocols and joint contingency plans
Maintenance	• Increase shared resources - common competencies / access - greater efficiency from joint working • Improved incident response and joint emergency planning • Co-ordinated delivery of engineering works and possessions

It would be possible to pilot such as change.

9. Does the current balance of responsibilities between the routes and the centre seem at the right level? Are there any further responsibilities that should be devolved or centralised?

The split of responsibilities seems to work adequately, although TfL notes that the ways of working are materially different within the different routes that operate around the London area. TfL is reluctant to recommend more devolution to the current route structure, as there are six routes that affect London & the South East which creates a large number of interfaces and makes coordination that much harder for a body such as TfL. Further devolution to existing route structure would not serve the needs of customers.

However, this conclusion would change if there was a regional body that reflected more closely at London & the South East and was aligned to the geography of the London commuter market.

10. Can you point to any specific economies of scale that should be protected at national rather than route level?

TfL is not able readily to identify any specific economies of scale. However there are functions including timetabling, planning and systems operation that are better carried out at national level rather than route level.

11. What processes and capabilities need to be in place (at both the centre and route level) to support Network Rail's current devolved structure?

TfL is not convinced that the structure is currently devolved as has already noted the arguments against further devolution to route level.

It is important that any new structure avoids discrimination against any operators. It should provide a consistent and fair-handed way of undertaking planning, which has to be joined up along and between routes given that there are multiple operators, including rail freight on some routes and operators that cross a number of routes.

12. Drawing on your previous experiences where relevant, what would be the potential impact on your organisation of further structural change within Network Rail?

Passenger Service Contracting: there may be impacts on the Crossrail and London Overground virtual alliance boards, and the network of working level contacts beneath that.

Planning (including freight): The route study process is well-established though it has some flaws. However, there is a consistency to the process and approach which is welcome since TfL deals with so many of the routes both for its own operations and for London and South East services.

Project Sponsorship: TfL sponsors projects on the National Rail network, some of which are delivered through Network Rail and some of which via TfL's own delivery teams.

Command & Control: The structure needs to be more closely coordinated across the London and South East Region. Network Rail and TfL should work together to create standardised protocols and joint contingency plans.

Maintenance (including incident response): TfL has worked with Network Rail to improve incident response on London Overground and would like to see a continued improvement in response times.

Infrastructure/Renewals: The Hendy Review proposed a reduction in renewals activity in CP5. An ongoing renewals process is essential and the focus on renewals needs to be maintained during structural change. Network Rail is not always incentivised to plan renewals such that they minimise the level of disruption to the operational railway.

Project Delivery (Enhancements): As noted elsewhere, a more market focused structure would benefit the delivery of enhancements in London and the South East.

13. What are the strengths and weaknesses of Network Rail's current approach to planning enhancements?

Strengths

- The planning process identifies demand and capacity challenges very well
- The process addresses the impact of large third party projects such as those associated with aviation and HS2, though the more local these are, the harder the industry finds it to react in a timely way (see comment on housing below)
- GRIP is thorough and systematic when applied correctly.

Weaknesses

- Politically driven investment decisions have led to some of the difficulties faced by Network Rail
- Accurate cost estimation remains a problem with costs of some projects such as STAR increasing during the GRIP process. The GRIP process does not seem to drive out costs and risks out but rather embeds them as the project becomes better defined, even when the scope has not seriously changed
- The planning process is slow and cumbersome and 'time to market' for projects is long. An example is the time lag between Market Studies and

Route Studies which can result in the need to review forecasts to take account of new data as for the Freight RUS.

- The IIP is produced by the industry but TfL and other funders have no direct role in its production
- The process finds projects associated with housing and regeneration much harder to deal with, where the transport benefits are secondary at best and traditional BCRs relatively poor. Hence part of the problems with Stratford – Angel Road (STAR) project for example

14. What are the strengths and weaknesses of Network Rail's current approach to delivering enhancements?

Strengths

Network Rail creates an organisational centre of excellence for project delivery resource, and more easily enables consistency of project delivery approaches, training and staff development. Opportunities for career progression are clearer and more straightforward.

The organisational separation drives a strict reliance on process – particularly GRIP. Sponsorship is well developed and professional, and the use of Client Requirements Documents, Route Requirements Documents and Detailed Route Requirements Documents to set out requirements, expectations, roles and responsibilities is effective. There is absolute clarity on the role of the Project Manager and his or her boundaries – organisationally necessary because the Project Manager operates outside the Route.

Weaknesses

The current Network Rail structure separates the management accountability for the delivery of enhancements from the day to day operation of the Routes. Using a separate structure and reporting line, through Infrastructure Projects, creates differing objectives between the project teams (deliver safely, to budget and on time) and the Route (minimise operational impact, ensure highest quality legacy assets and minimal maintenance liability). The Route is obligated to the franchise operators to limit access to the railway to avoid disruption to operation but the level of work given to Infrastructure Projects does not relate to this causing an inherent conflict.

While this ensures complete focus from Infrastructure Projects on successful project delivery it means there is often a lack of a unified view as to what project success really is. TfL notes a number of projects with painful and extended periods of commissioning, transition into operations and handback.

Generally, organisational misalignment between the Routes and Infrastructure Projects and national programmes (e.g. Signalling) is a weakness and creates the impression that projects are being "imposed" on the day to day operation by "outsiders". The mixture of national and local (Route) responsibilities can only create tension and differing objectives. Established relationships between the Route and operators become strained and disrupted by separate project teams which do not share the same objectives to drive up operational performance.

Delivery of enhancement projects serves the wider Network Rail organisation in its core role of being an infrastructure manager – Network Rail is not there to deliver projects for their own sake. TfL suggests that the project delivery function should be subservient to the core Network Rail business and delivery of enhancements should align to whatever organisational structure is selected to best deliver those core goals.

15. How well do the current delivery and planning processes work for projects of different sizes?

The evidence from CP5 shows that Network Rail's planning and delivery process has been more successful for well understood infrastructure projects than for large scale infrastructure works such as electrification that are infrequently carried on the network.

Network Rail needs to be adequately resourced and funded for planning and delivery of all sizes of project and for cross party projects such as Barking Riverside.

GRIP is not sufficiently flexible for small scale projects and light touch GRIP for expediting small schemes quickly would be welcome.

16. Are there any useful models or precedents from other sectors or countries for long term infrastructure planning and delivery processes that we should consider, including in relation to management of and engagement with suppliers during the planning process?

To date, the project management process associated Crossrail central tunnel section has kept the project largely to budget and programme.

London Underground where a long term partnership with Balfour Beatty for track renewals has led to innovation in working practice, including ballasted track renewals overnight, and is an example where long term collaboration with the supply chain has yielded demonstrable results. TfL would be happy to share more detail of this partnership with the review team if required.

17. What would be the most important structural features of any future infrastructure provider?

The main features should include a reduced number of interfaces with key customers and responsiveness to customer needs as described above. The infrastructure provider should have the flexibility to undertake a project or enable others to undertake it on the National Rail network.

18. Are there any other processes which we have not highlighted, either within Network Rail or the wider industry, which could be improved?

Command & Control, Maintenance (including incident response) and Infrastructure Management (Renewals) could be improved as described in response to Question 12. Change that enables reduction in response times is of particular importance in areas of high intensity services such as London.

19. Do you have any views on how the relationship between the periodic review process and other processes with which you are involved could be improved?

The Periodic Review process takes a significant amount of time and resource from across the industry but has failed to deliver robust plans. The evidence for this is that the plans for CP5 were given a high degree of scrutiny by multiple organisations including Network Rail, RDG, DfT and ORR, but still proved undeliverable in the timescales envisaged.

The process leads to a large number of interfaces and parties that TfL has to engage with in getting agreement to any given project or change initiative. A streamlining of the process should be considered with a strategic body set up to undertake long term planning and delivery. This could take the form of a single organisation combining some functions of Network Rail, DfT and ORR. Alternatively there could be a small number of regional organisations responsible for planning and delivery, including a Rail for London and South East organisation.

The five year control period process is important to long term planning and should be retained but with some overlap between the start and end of a control period to avoid a peak in activity towards the end of a control period and a slow start to the next control period.

20. What criteria should be used to assess structural options under consideration? How, if at all, should these criteria be prioritised?

The criteria should include the impact on:

- degree of accountability
- quality of the customer experience
- cost efficiency of delivery
- wider economic benefits and growth
- level of disruption from implementing change

Financing and funding of the company

21. Do you have any views on whether the RAB remains a relevant concept in the Railway, and, if not, what should replace it?

For the reasons mentioned in the Shaw Review call for evidence, the RAB is largely irrelevant as a means of protecting the interests of private investors in Network Rail, as there are no private investors. It may still be helpful as a means of accounting for or keeping track of how much capital is invested in Network Rail, in the event that it is desirable to recover the public capital invested through a later privatisation. It could continue to serve as a basis for computing a cost of capital allowance for the purposes of setting track access charges for TOCs. But since Government provides a net subsidy to the TOCs through the rail franchises, any variations in the cost of capital charges ultimately flow back to Government through variations in the subsidy, so the flow of money is largely circular.

The RAB also has limited incentive benefits in the absence of private capital at risk, and with strict controls imposed by Government on Network Rail's borrowing. This is likely to remain the case if Network Rail remains within the public sector.

The RAB could be retained or replaced with a simpler public funding arrangement (such as TfL's multi-year grant settlements) depending on whether the eventual goal is to re-privatise the company, or retain it in public ownership.

22. How should financial risk be managed in Britain's rail infrastructure in the future?

Financial risk can be well-managed within both public and private models of ownership for the rail infrastructure. There are examples of each from within the transport and utilities sector. The key elements are to ensure that a clear allocation of financial risks between Government, the fare-paying public, the infrastructure operator's management and investors and the train operating companies. TfL believes that Network Rail's management should be given strong incentives for efficient financial risk management (including the on-time, on-budget delivery of major track upgrades), but also provided with sufficient tools to do the job well (such as the ability to manage multi-year budgets with appropriate centrally held contingencies for programme risk, and with the ability to use borrowing to manage cashflow variations across time).

23. Do you have any views on how Britain's railway infrastructure should be funded in the future, regardless of corporate structure?

TfL understands that the current direction of travel is to route the majority or all of the direct network grant via the TOCs, so that Network Rail's business is funded entirely through regulated track access charges. This would return the funding model to its position at the time of the original privatisation.

Although TfL appreciates this is not within the current remit of the Shaw Review, it is important to ensure that all TOCs are placed on a level playing field in respect of changes to future track access charges, regardless of whether they are franchised by DfT or devolved to a regional or local authority. For instance, an abolition of the direct network grant and its re-routing via the TOCs will have the effect of sharply raising track access charges. While TOCs operating under franchises let by the DfT may be compensated for this directly, local transport authorities like TfL will have to pay the higher charges for Crossrail and Overground services without any corresponding increases in revenue, and will therefore need to be compensated separately.

TFL also believes that rather than routing the entirety of the network grant via the TOCs (as currently proposed), it may be worth considering devolving the HLOS and grant funding aspects in relation to London and the South-East to a local body responsible for planning the commuter transport network for the area. The specification and funding for InterCity services could still be retained centrally and routed via the TOCs. Devolution could be achieved in part through the prospective rates devolution package. This reform would create a single, powerful client for Network Rail's track infrastructure for all commuter services into London, with greater democratic accountability to the commuting customer. This would also provide a much more direct method of getting the "customer voice" heard within Network Rail.

24. What positive case studies are there (e.g. international examples in the railway sector, other sectors internationally/in the UK), where more affordable and sustainable funding and financing structures have been implemented, with or without private sector capital input? And how do you think the lessons learnt could be applicable to Britain's railway infrastructure?

TfL has no comments.

25. What are your views on the enabling factors facilitating a sustainable and affordable capital structure for Britain's railway infrastructure? What factors would be required specifically for private sector capital introduction?

TfL's own experience demonstrates that it is perfectly plausible to run a sustainable and efficient rail transport network within public ownership, using a mix of public and private capital. TfL is largely funded through a mix of fares, local rates income and central government grants, but it also borrows from the private capital markets as part of its Treasury operations, where this offers better value for money than using public works loan board funding.

The introduction of private capital requires a self-sustaining business model, able to recover the full costs of infrastructure operations, maintenance and renewal (including upgrades) from independently regulated track access charges. The proposed move to route the network grant via the TOCs will facilitate this. However, this does complicate the planning of the railway system, particularly if the earlier suggestion to also devolve an element of specification and funding for London and the South-East is taken up.

TfL's experience of PPP shows that introduction of private capital needs to be done selectively and is best directed as specific asset classes such as major stations or development land to minimise risk. TfL is happy to share more detail of lessons learnt with the review team.

26. What are the types of investors that may be interested in investing in Network Rail, any of its functions, or in select parts of it? And for these types of investors, can you indicate:

- key attractions;
- risk appetite;
- required enabling factors.

There is considerable demand in the capital markets (in both debt as well as equity) for long-term, regulated assets. However, given its history and the perception of political risks surrounding the railway, the Network Rail proposition would need to be substantively de-risked in order to appeal to such investors. As suggested above, a model where Network Rail is set up for full cost recovery through regulated track access charges is likely to be more attractive to investors than one where it is also reliant on one or more grant providers.

27. What characteristics do you think enhancement projects would need to have to attract private sector investment and to what extent and in what form would public sector support would be needed? What types of financing structure could be brought to bear?

Discrete enhancement projects with limited interface with the main railway network could be progressed through special purpose vehicles (e.g. Crossrail, HS2) or operated through competitively tendered PPP arrangements using private capital (e.g. HS1). New models such as the discrete RAB for the Thames Tunnel project could also be considered.

The key characteristics are the ability to isolate the risks of the project from the wider network (so limiting the interface risk), and the ability to assess, price and allocate risks within the private sector supply chain. It is likely that tail risks may require Government support (e.g. as provided in the support package to the Thames Tunnel project). The Crossrail example illustrate how this could benefit rail investment overall and provide alternative project delivery mechanisms. Outside of London, third party investment has been limited partly because develop schemes outside the NR process cuts against the grain too greatly, though potential schemes like better access to airports which could be delivered if the process was more flexible.

28. What incentive mechanics or control structures on Network Rail would facilitate third party involvement in the financing of enhancement projects?

Strong incentives to deliver enhancements to time and budget, and a duty to seek best value for money by minimising the whole life cost of infrastructure would best facilitate third party involvement in the financing of enhancement projects. It is unlikely in TfL's view that – unless insisted upon - third party financing would be used for anything other than very exceptional and completely separable projects.

Risks and implementation

29. Do these feel like the right concerns? Has anything been missed that it is vital to consider at this stage?

The Review team should consider how the planning of the railway infrastructure interacts with the funding flows, and the franchise bidding system. Ideally, the specification and funding for commuter services around major cities like London should be devolved to locally accountable authorities, together with the responsibility to bid for the franchises on those services. InterCity links should still be specified, funded and bid out centrally. Track access charges for Network Rail would be set (based on full cost recovery) by an independent regulator, and the prices for rail franchises would be set by competitive bidding. The governance of such arrangements requires more careful thought, as that is where the majority of the risks in implementation will arise.

The study appears to start from the premise that a restructuring is required. The industry has been through a number of restructurings and change in status of Network Rail since privatisation and it is not clear that a wholesale restructuring is required to bring about improvements. Costs and benefits of restructuring both during and after implementation will need to be taken into account by the Shaw Report. There are both risks and opportunities associated with restructuring and with moving functions and people into different organisations.