Consultation Response - Shaw Report Scoping Study

SLC Rail – 24th December 2015

A. Introduction to SLC Rail

SLC Rail offers 2 core services – client-side strategic advice and management of scheme delivery.

For the first of these SLC Rail provides strategic advice to local transport authorities, Local Enterprise Partnerships and PTEs in assessment and development of rail strategy and policy, financial and economic justification (GVA/jobs) for investment in the rail network, scheme business case development, together with franchise specification, including devolution. With extensive experience in the industry SLC Rail also provides an informed, direct capability in engagement and negotiation with the Department for Transport/Rail Executive, Network Rail and Train Operating Companies/Freight Operating Companies. SLC Rail is currently engaged as rail advisor to Centro/West Midlands Rail, South Yorkshire PTE, Warwickshire County Council, Coventry City Council, Solihull Metropolitan Borough Council, Worcestershire County Council, Leicestershire County Council, and Northamptonshire LEP and, as a joint arrangement with JMP Consultants has been appointed to the DfT's Specialist Transport Advisory Framework (STAR). We also work with train operating companies and private sector developers.

We stress that our response below is solely on behalf of SLC Rail and does not represent the views of any of our clients.

For the second, SLC Rail provides financial, commercial and delivery support to public and private sector third parties wishing to manage completion of their own rail projects, taking a lead developer role whether with or as an alternative to Network Rail, whilst sustaining full and proper engagement with all rail industry bodies. Drawing upon its team members' experience at Chiltern Railways and Laing Rail in leading successful development, funding, commercial structures and delivery of Warwick Parkway (2000), Coleshill Parkway (2007), Aylesbury Vale Parkway (2008), together with the 3 third-party Chiltern route upgrade projects (Evergreen 1-3), SLC Rail developed and delivered Stratford-upon-Avon Parkway (2013) ahead of programme and under budget, and is now developing and delivering multiple third-party schemes including Worcestershire Parkway, Kenilworth New Station, Bromsgrove re-located station, as well as their associated train services (and rolling stock in the case of Kenilworth), as well as 2 new stations on the Nuneaton-Coventry line and a major local authority road bridge scheme serving Birmingham Airport over the electrified West Coast Main Line.

B. Responses to Questions

Network Rail's structure

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

The report categorises Network Rail's functions in a recognisable way.

It is worth noting that 'enhancements' could be further usefully divided into upgrades of existing infrastructure (for example electrification) and development of new infrastructure expanding the network (for example HS2).

In relation to the latter enhancement type, and as part of the strategic planning process, Network Rail also develops the business case for upgrades or improvements to the railway.

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

Third Party Investment

Not mentioned in the scoping document is Network Rail's role in the facilitation of third party investment in the railway. This is typically delivered through Templated Agreements (http://www.networkrail.co.uk/aspx/1606.aspx), whereby Network Rail either delivers the enhancement on an emerging cost basis (fixed price options exist but are impractical in application and thus never offered by Network Rail nor actually used in practice) or the third party delivers the investment with Network Rail acting in asset protection mode.

Projects that are delivered through template agreements are largely locally driven, developer or local authority led; they are either considered too difficult, too uncertain, too underdeveloped or have somehow 'missed the cut' from the HLOS process. The fact that the third party has chosen to go down the template agreement route rather than waiting for the next Control Period, is born out of the fact that these projects typically demonstrate a high level of local political, strategic or economic importance sufficient to demand scheme development in spite of the relative perceived difficulties, for the promoter at least, of going down this delivery route.

Funds Provider

Whilst it is unclear how this will change since reclassification to the public sector, Network Rail has previously acted (and presumably currently acts) as the custodian of multiple funds, either allocated by DfT (e.g. New Stations Fund, Access for All) or by virtue of the suite of Template Agreements for enhancement projects (Industry Risk Fund, Network Rail Fee Fund).

For the management of DfT funds, the commercial arrangements are very one-sided. Network Rail typically provides a fixed fund input but delivers the enhancement on an emerging cost basis; the risk sits with the scheme promoter, and Network Rail has no obvious incentive towards economy and efficiency.

For the management of Risk/Fee Funds, and particularly the Network Rail Fee Fund which exists for instances of Network Rail negligence or breach of contract, Network Rail is ultimately overseeing questions raised on its own performance in delivering the project. This potentially leads to a lack of objectivity in the determination of outcome of entitlement in relation to industry related risks or project management related issues, where one parties perception of what is an industry risk or management issue is different to another's. In addition, third parties who regularly work with Network Rail on projects are less likely to push these routes for recompense, as this might be to the detriment of future working relationships, and as a result have to bear costs that could be recovered through the risk fund route.

Business Case Provider

As noted above, Network Rail in its role as strategic planner is the developer of business cases for enhancements or improvements. There are financial benefits achieved by Network Rail through either performance or capacity benefits, and there can be more widely achieved economic benefits through increases to GVA and creation of jobs.

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

There is a lack of clarity on the role for DfT and ORR.

ORR should maintain its standards/safety role but the Periodic Review process, performance monitoring and specification of outputs should be with DfT.

Clearly one of the major failings of the whole system, whether Network Rail is classified as public or private sector, is the fact that there is only one body, Network Rail, which is responsible for spending the money of others, and, since any inefficiency or fines are funded by taxpayers, there is no tangible financial penalty for cost overruns. Indeed, as the recent Hendy review has demonstrated, the only real remedy for overspending on projects against a fixed budget is a reduction in scope of projects / outputs delivered; which could be argued also results in the taxpayer paying through not having the benefits expected for the funding provided.

Having said that, any potential accountability that could be put in place is hampered by multiple other factors; not least of which are i) Network Rail's lack of understanding of existing assets and lack of funding for getting that understanding and ii) lack of appetite for funding a general improvement in the state of existing assets until they are, as referred to in the scoping document, "life expired". Attempting to hold Network Rail accountable for these aspects of any enhancement upgrade project is thus going to be very difficult, and it is these aspects of projects that typically cause a reasonable proportion of all project problems; the other key element being the lack of a fully defined scope at the time of budget setting, clearly delivering railway projects is not an easy thing to do in light of the need for multi-disciplinary design coordination, the various resource constraints that exist, access constraints, complexity of commercial interfaces, consents required, and the need to progress generally in accordance with GRIP.

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

Four very important customers are omitted from section 04:

- **Local Transport Authorities** – who may be engaged in the specification of train services, and in the future may be involved in funding of services and new infrastructure. The coordination of rail projects with other enhancements to local transport is obviously a key enabler for capacity, connectivity and accessibility improvements, maximising economic and strategic benefits (particularly employment);
- **Local Authority and Local Enterprise Partnership (LEP) scheme promoters** – who, per the definitions in the scoping document, may have funding (either via the LEP, from specific European funds (i.e. ERDF), from DfT funds managed by Network Rail or from internally allocated grant funding), or finance (from prudential borrowing), to provide in support of schemes;
- **Developers** – linked to housing developments or commitments as part of any planning consent, rail projects have been known to unlock stalled housing development (as with Aylesbury Vale Parkway which was linked to 'Berryfields' a 3,500 home development); and
- **'Station Investors'** (which may of course be local authorities or developers) – who, through the recent changes in Station Access Conditions, may seek to establish an investment or participation in a railway asset by virtue of an initial investment of over £50,000.

The services provided to these Customers are typically related to a number of specific transactions:

- Engagement of NR in the provision of services to enable scheme progression and ultimately delivery (including design approvals, access to the railway) through template agreements;
- Property agreements, which may include access over, under or through NR property, for either the short or medium term, as an enabler to development linking the railway to surrounding infrastructure (typically highways or transport interchanges); and

- Land transactions, where land can change hands to streamline boundary definition, and to provide protections for railway / other land uses into the future.

Network Rail Delivery of Services (also Q15)

For third party investment in the network, from the customers outlined above, a much clearer and simplified process is required which provides a simple roadmap of deliverables at each GRIP Stage. The current 'Route to Gold' process for designers has its problems (as noted elsewhere) but is headed in the right direction but this needs to be enhanced to accelerate the approvals process at GRIP 3, GRIP 4 and GRIP 5.

Current NR commercial policy on Station Assets can be a barrier to third party investment. For example where a new car park project is to be funded 100% by a local authority and could be acquired under an Asset Purchase Agreement by Network Rail (or simply handed over) but Network Rail is instead intent on applying First Reserved Rent through its Lease with the TOC effectively taking the majority of the value of car park receipts for an asset it has not funded. As a result of this schemes may have to investigate other, potentially less efficient, land ownership mechanisms to enable the scheme to proceed.

Section 4.4 of the report suggests that Local Authorities are not direct customers of NR. They are, and in our experience are discriminated against in term of Network Rail resources in favour of in-house maintenance, renewals and regulated output projects. The culture of Network Rail being 'not funded for enhancement' still exists in certain pockets, which leads to the need for enhancement projects to fund existing railway deficiencies, expanding the scope of enhancements to potential unaffordability (for example the replacement of whole station CCTV systems to provide a couple of extra cameras). The solution to this may be to identify more clearly delineated project teams who manage and coordinate enhancement projects, as partly already exists through the NR Infrastructure Projects organisation but further empowerment would be necessary to make fully effective.

The possibility for scope creep, including gold plating or preferential engineering, still exists pre-delivery at design and approval stage which inevitably relies on route resources at RAMS levels to sign off the requirements; this materialises in Network Rail insisting on more works being provided than absolutely necessary in order to achieve scheme design sign-off.

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

The entry point for customers is often unclear, the potential forms of engagement are many and complex, and it is difficult to know where to start.

There is often a disconnect between the speed at which Network Rail can or is prepared to commit to delivering scheme development, saddled as it is with various internal approval processes, and the desires of third parties to deliver schemes in a timely way. This can be the case even when the third party promoters have assembled sufficient funding to develop the scheme; one recent example is where a 'kick-off' meeting for a £15m third party funded scheme was held in December 2014, and signing of agreements for commencing development of the project is now not expected until 2016.

A lack of responsiveness to the customer's programme requirements and time constraints, can lead to subsequent problems in relation to funding, where funding is or becomes time barred (as is the case with ERDF programmes and more recently LEP funding allocations).

Our experience also suggests that many local authorities have actively avoided rail investments in the past on the grounds of the difficulty in engaging not only Network Rail but also TOCs and FOCs, and the risks to them – financial, political and reputational – associated with cost escalation and programme delay wholly in the control of the rail industry, and de facto, out of their own control.

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

Yes. As noted multiple times in the scoping document, the shape of Network Rail, its functions, how it is organised and funded, where and how accountability is implemented are all intrinsically linked.

Local Accountability Structure

Nationally important enhancements (HS2, electrification generally) must be managed centrally, albeit with feeder inputs from local teams, to enable synergies to be achieved or more pertinently intrusion and disruption avoided.

The ideal scenario in relation to other enhancements would appear to contain the following facets:

- A portfolio of enhancements that are agreed locally (or regionally) that tie into local transport objectives and deliver local or regional improvements;
- A package of funding which links DfT funding (for nationally agreed and funded schemes through the IIP, HLOS etc.) to LEP, local transport authority, local authority, and in some cases business funding (CIL for example) for locally promoted schemes;
- A Project Funders Board, where progress on all projects is reported and decisions are made in relation to scheme development where required (which may include reprogramming or providing additional finance) or delivery (which may include delivery route that is not via Network Rail if that is demonstrably more efficient), but where the decisions are made locally;
- Sub-Groups for strategy planning, project implementation, impact assessment and communication as appropriate.

Representation from all customers could be made: DfT local reps, LEP and LA, LTA members, train and freight operators.

It is felt this would be more able to hold Network Rail to account for its actions and its performance on enhancement delivery.

Strengthening of Sponsorship Role / Third Party Relationships

Network Rail appoints Sponsors for schemes; these are extremely important roles and are intended to support third party schemes / third party engagement on Network Rail schemes, but the individuals themselves often lack the authority within Network Rail necessary to truly represent the third party's interests.

Having such a representative, who understands and communicates Network Rail's perspective on schemes but also who is able to communicate to Network Rail the customer's reasonable requirements and be empowered to ensure that they are taken seriously, prioritised appropriately, and effectively delivered, would massively enhance Network Rail's reputation for supporting third parties, and potentially enhance and increase the level of investment provided.

One alternative model might be to engage additional, specific individuals responsible for managing third party investment who would meet with LAs, LEPs and represent NR at relevant meetings. These

individuals would then be responsible for encouraging as well and managing third party investment; something that would be attractive to spread the funding load beyond Central Government.

Funding via TOCs?

Making more funding of Network Rail come via train operators may be counter-productive without changes to the franchise agreements (including term), since train operators by the nature of current franchise arrangements have constraints on time horizons which may lead to short term positions being taken to the detriment of longer term strategies; dictated by the need to maximise value for owning group shareholders.

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

There is a danger that the only perceived incentive is profit, and this would tend to then suggest private sector engagement is fundamental to an improvement in delivery.

However, any new incentive would need to be considered alongside and aligned to the objectives set; and as noted in the scoping document the recent shift from an output delivery objective (CP5 ORR objective) to a capped funding constraint (Hendy) will already be impacting on the various incentive mechanisms that already exist, either within Network Rail organisationally or as overseen by ORR.

Outcome Delivery Incentives are used in other industries, but these rely on a detailed understanding of the cost make-up of any specific outcome, and it is not clear whether either Network Rail or ORR has reached this point; as illustrated by the recent need for an ECAM adjustment measure.

It is only through a detailed scrutiny of each project outcome, the cost of delivery of said outcome and a full lessons learned and feedback process, that a full understanding of how costs are incurred for enhancing the railway can be achieved. It is not clear that such a process exists.

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:

- physical, political or economic geographies?
- service type, e.g. commuter services, inter-city services and regional services?

By reflecting the political and economic areas more closely, common goals and objectives are more likely to be reached and agreed, with potential cross-border rework and conflict reduced (for example on schemes reflecting different disciplines, such as re-signalling schemes and track renewals). Local stakeholders would be managed better and more customer benefits seen.

Conversely there is a risk that areas become segregated and wider railway benefits are lost; for example best practice, consistency and supply chain benefits. There is also a risk of adding in more levels of management when acting on both a national and a local scale.

The advantage of creating a more focussed approach to service type would be to identify the different challenges faced, and be able to respond in a more market focussed way, and in relation to regional services to impact on economic growth. An issue with this approach, however, is that each service type is intrinsically linked somewhere on the network, and any silo approach to service types may lead to more focus being applied to the most financially profitable (or costly from Network Rail's perspective) rather than those for the good of the local population (e.g. small stopping services). Such a conflict, as exists for example on the West Coast Mainline between Virgin and

London Midland services, and the prioritisation that applies to each, needs to be managed in a way that best suits the passengers requirements rather than the commercial incentives.

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?

Routes should be able to set their own objectives, agreed with the relevant local stakeholders and the ORR. This allows for a better comparison for performance across the routes, taking into account their individual challenges.

Innovation is also led from the centre, often hampering the success of certain technologies because a 'one size fits all' approach has not worked.

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

- NSC (ballast, rail, sleepers, signalling equipment)
- Strategic plant (tampers, cranes) are expensive to buy and operate, so it makes sense to share these as a national resource
- Signalling contractor resources are scarce, and should be procured at a national level and project managed locally

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?

Centre

- Centralised reporting / visibility of route performance
- Standards management
- Safety
- Resource management

Route

- Objectives
- Funding sign-off
- Project performance reporting
- Innovation
- Project and commercial management of enhancements
- All operations and renewals activity

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

SLC Rail takes a lead role on behalf of its third party customers in enabling them to understand and interpret the language, processes and behaviours of Network Rail and the rail industry as a whole, and to engage with them effectively.

A more outward facing, customer-responsive Network Rail would be welcomed by ourselves if this facilitated schemes, and projects being developed and delivered more swiftly and more cost effectively.

At the same time we are under no illusions that major structural change in the rail industry may, of itself, generate the familiar problems of 'reorganisation' in terms of corporate navel gazing, loss of skilled people, and organisational uncertainty during the process.

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

Note: the presumption underlying questions 13-16 is that Network Rail is the deliverer of enhancements. The Investment Framework has been set up specifically to enable and encourage third party scheme promoters to deliver their own projects, through engaging Network Rail in an asset protection capacity rather than as scheme implementer.

Strengths

- Planning by Control Period allows for a 5 year 'extract' of a longer term strategy to be planned and procured, providing work bank / stability to contractors and project management teams
- Ability to smooth national resource profile to meet a programme of works

Weaknesses

- Smaller packages of work are often neglected in favour of larger national plans, or at best schemes have to wait until the larger schemes have developed sufficiently far to understand any potential impacts, stifling scheme progress to the point that all associated projects are only able to progress at the speed of the slowest developing scheme (normally the biggest one)
- Large reviews are required when programme problems occur, because Network Rail is unable to itself change quickly (for example the Hendy Review was required as a stimulant to re-profile expenditure, albeit the problems were of national significance in this case rather than those that could be managed internally)
- Railway planning / Control Period process does not line up with franchising timescales / cycle, this means that maximum benefit realisation is not possible, and maximum compensation costs for disrupted incumbent operators are sought, leading to project outturns that result from lowest payback, highest cost scenarios
- Planning cycle does also not align to local authority, Local Enterprise Partnership and local transport authority timescales (LTP etc.) meaning any link is potentially mistimed and/or lost between the infrastructure impact and the economic need

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

Strengths

- Framework contracts provide a convenient procurement route for contractors, which typically speeds up the process of schemes
- Link between enhancement delivery and the various works delivery teams within Network Rail should lead to synergies of delivery where enhancements and renewals can be delivered alongside each other

Weaknesses

- Lack of competition for Network Rail on scheme / enhancement delivery, and where competition does exist (for example when a local authority attempts self-delivery of an enhancement scheme) Network Rail retains the ability to significantly influence the outcome of that project

- Contractors are being asked to manage projects at an early stage (GRIP1-3) under the banner of 'early contractor involvement', however there are question marks over whether contractors (construction delivery experts) are best placed to manage the planning and development of new schemes;
- Additional cost within the delivery structure, with layers of management resources, overheads and profits within the delivery model; and
- No check that the enhancement has achieved what it meant to achieve, or benefits realisation planning and subsequent reporting.

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

It has been recognised for some time that GRIP is too onerous a process for smaller schemes; but nonetheless GRIP continues to be a requirement for these schemes when delivered by third parties.

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?

Highways England carry out large programmes utilising Joint Ventures. The work is split into large defined packages. The work is awarded in sequence based on the performance (time, cost, quality) of the joint ventures. This promise of more work keeps the suppliers engaged throughout the programme whilst also moving to create efficiencies.

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

Some thoughts on key structural features:

- Clear and transparent responsibilities and obligations with as few interfaces, and thus management resource requirements and areas for conflict / dubiety, as possible – organisations, routes, however structured, need a 'guiding mind' responsible for setting challenges, maintaining pace of development and responsible for financial control;
- A clear accountability, including to local as well as national stakeholders, is fundamental to regaining understanding, trust and buy in to a growing railway;
- A clear understanding for all of the charging mechanism for provision and operation of the network and its infrastructure;
- It must be an enabler of investment in the railway, not simply via Government, but also via third party scheme promoters, and investors;
- Different models / approaches may be appropriate depending on different routes and geographies, there should be a revisit to the advantages of NR Route/TOCs alliances such as trialled at SWT – the notion that this one did not wholly succeed should not mean giving up on them generally;
- Network Rail should work to achieve a corporate understanding of the end user – its staff, at senior and front line level, need some level of exposure to the end user, whether passengers or freight, to better be informed of the impact of any decisions made.

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

One of the major barriers to any restructuring is the level of understanding of existing assets (including contamination), which affects the ability to transfer risk for existing asset condition to a third party.

In addition, as noted elsewhere, GRIP could be made less onerous for smaller schemes; and clearer for enhancement schemes generally.

Route to Gold

Also, as noted elsewhere, the "Route to Gold" process needs review and overhauling. Designers' aspirations for gold status are high; however achievement of the benefits of gold status rarely materialise, because of Network Rail's lack of trust of the designers once they have reached this status (Route to Gold basically enables a designer to act as acceptance body on its own designs once gold status is established).

In addition, as part of the process Network Rail logs the type of design comments against each supplier/designer (severe comments can lead to a call-in). This has led to a naturally risk averse attitude to design submission, whereby designers prefer to make an informal design submission to elicit initial comments and to ensure designs will not be rejected or receive substantial comments, before any formal submissions are made to Network Rail. The contractual commitment on third party schemes (as outlined in the Asset Protection Agreement) already involves 5 weeks' notice to Network Rail before a design submission is to be made and then allows a further 5 weeks for Network Rail review of each submission; thus the insertion of a further design submission step simply elongates the time taken to get designs approved.

CSM / Interoperability

The application of CSM and interoperability regulations needs to be considered.

The fact that interoperability regulations apply equally (and fully) to branch lines as well as main line operations does not reflect the reality of where true interoperability may actually be required. Any process of derogation or exclusion from the interoperability regulations should be made easier to achieve other than on key arterial routes such as WCML, ECML and GWML.

In relation to CSM application, this appears to be continuing to evolve. One thing that is clear is that CSM simply replicates what should otherwise generally be done anyway in project delivery (including compliance with standards and various link-up audits and approvals for suppliers). CSM drives the need for secondary checking on most project aspects, on top of the various existing layers of checking that takes place, driving time and process into scheme delivery.

Station Investor

The role of Station Investor was established in 2013.

For many laudable reasons (including financial protection of DfT and the taxpayer) the obligations and financial implications of becoming a Station Investor have been structured to include an indemnity to Network Rail, the SFO and any station users against additional costs arising from the changes being made / funded by the Station Investor.

However, the indemnity requirements apply equally to an investor proposing to put a cycle rack on a station or to improve the toilet facilities, as they do to an investor who wishes to knock-down the existing station and rebuild it and or double the size of the existing station facilities (e.g. Coventry Station Masterplan). When a positive business case exists, and where a third party is willing to inject tens of millions of pounds into enhancing the railway it seems unreasonable to require them to then have to underwrite the operational costs of the facilities for five years after they are completed, particularly when the benefits of the investment made may well be felt by the railway for up to a

hundred years (depending on asset life), and there is no path for recovery of any of these benefits for the investor.

Timetable Development Process

Where a third party project requires changes to the passenger timetable the bar is placed far higher for a third party than for a TOC; by virtue of it being outside the rail industry contractual and commercial structure. More often than not full performance modelling is required to demonstrate to the various parties that the intervention can be made without detriment to overall performance robustness. Such scrutiny and oversight is not required for 'in industry' change.

Recognition of Value Added

Network Rail are very unwilling to recognise the long term maintenance benefits of any third party schemes, and this needs to be rectified. A recent project example is where a scheme scope includes removing two foot crossings, reducing costs and improving safety, but no financial credit has been considered despite requests and pressure to do so.

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?

Control Period Timescales

As mentioned elsewhere, the need for timescale alignment across the various planning and franchising processes is fundamental to achieving a collective understanding of direction of travel. Franchisees cannot bid without certainty because the Government does not want to fund the risk attached to uncertainty through the franchising process (e.g. GTR being a service only franchise due to the nature of change expected over that railway over the next few years due to disruption and as consolidation takes place). Of course, as noted elsewhere, this would require franchising policy to mirror railway planning timescales and vice versa, which may be difficult to achieve).

Most recently, the Hendy report stated that development time (and presumably budget) for projects expected to be delivered in CP7+ would be allowed for in CP6 for specific projects; however, this provides no greater certainty that these schemes will happen, and the reality is that nothing substantive will happen with these schemes until 2019.

Where there are a series of projects are being developed over phases, linked to and relying on strategic schemes (for example NUCKLE has four phases over the next 5+ years), it is almost impossible to plan for later phases without having the confidence that, or understanding the programme for implementation of intrinsically linked schemes (such as 'electric spine'). The periodic review process could be improved by spanning three Control Periods, or 15 years, with degrees of certainty attached to each, getting lower into the future. This is possible for schemes like HS2, where future development can be plotted to enable the timing of feeder, fed by schemes to be aligned. There would appear to be no reason why the railway planning could not develop along similar lines, if split into bite-size chunks, such as regional economic areas.

Consultation and Engagement

The development of plans for a control period could be improved through more extensive consultation and engagement of third parties, to ensure the level of enhancement matches local needs, to understand whether the prioritisation of projects matches economic development needs, and to enable alternative funding routes to be explored where required to balance the books, or to kick-start the projects.

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

- Overall efficiency of delivery model
- Links to economic growth, jobs and GVA
- Integration / compatibility within and outside the railway
- Transparency (a holistic view of the costs / programme)
- Clarity of roles, responsibility and authority
- Defined accountability
- Management effort and overhead costs of delivery

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?

In the current environment and with the current classification of Network Rail, the RAB is not a relevant concept.

The linking of Control Period 5-year expenditure requirements to the RAB also has its problems, since unlike other industries where RABs are successfully operated, the charges arising from an increase in the RAB (in the railway through track access charges, in other sector through usage based charges) are not passed on to the end users, but rather the end users are held harmless by the NNLNNG arrangements within franchises.

Part of the problem is that franchisees cannot be asked to fund additional charges arising from a new Control Period, linked to enhancement that were unknown (and therefore unpriced) when the franchise was entered into, and also within the relatively short life of a franchise where the payback against additional charges may not be realisable. The only real way that this problem could be overcome would be to provide longer term franchises, through which the cost – value offset may be achieved, but this is unlikely to be implemented due to current government policy of 7 – 10 year, largely service-based franchises.

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

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

A number of successful private and publicly funded railway schemes exist. Examples of these are projects developed, delivered and owned by Chiltern Railways / John Laing (Warwick Parkway, Coleshill Parkway, Aylesbury Vale Parkway) financed from a mix of debt and equity; and Centro and Worcestershire County Council (Bromsgrove and Worcestershire Parkway) financed from prudential borrowing.

These schemes, and others such as IEP depots, prove that innovative and radical mechanisms do exist for third party delivery and ownership of railway infrastructure on the national rail network, as opposed to bespoke networks (such as HS1).

As an increasing proportion of funding is made available through locally allocated and prioritised sources (LA, ITA, LEP funding sources), as the ability for fund raising, via CIL becomes more prevalent, and as authorities start to appreciate that prudential borrowing may be a route to financing schemes, the potential for these funding sources to expand over time is huge.

The challenge for any investment scheme where finance is involved, whether public or private sector provided, is to seek to assign the highest contribution towards repayment to the biggest beneficiary. On railway schemes this is typically the fare paying passenger and the local economy, including residents and businesses. Having an understanding of the financial benefits outcome (e.g. increased TOC revenue) allows an assessment of affordability, and this quickly leads to an assessment of finance that can be provided, in literally any scenario where a positive financial outcome is expected.

On station and car park schemes this is relatively straightforward to calculate, even taking account of the franchisees attitude to risk, and allows a financial structuring to be developed around any surplus income position created.

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?

The Chiltern route regeneration led by Chiltern Railways between 1996 and the successful opening of the Marylebone to Oxford route in October 2015 illustrates firmly the virtues of long-term incremental development of railway routes linked to the economic development of the regions they serve. The investor, in this case Chiltern itself and its successive owners – 3i, John Laing, Deutsche Bahn – directly related and integrated its investments and risks to the end-game: providing a better railway service to existing and new passengers, and gaining more new passengers from which revenue is generated sufficient to pay for those investments through the uplift in fare box.

New train services to higher frequency and capacity are the driving factor – ultimately the product the rail industry sells to its customers – from which investment decisions in infrastructure and signalling, stations and car parks, rolling stock and depots followed. Thus, key on the Chiltern franchise, is that it is the understanding of the opportunity for growth that has driven the investments made.

By contrast 'infrastructure-specific' investments – such as the £75m investment in the Oxford-Worcester line upgrade in 2011 had no train service and passenger focus, and did not require any risk holding by the TOC selling the service to the public. Unsurprisingly no significant structural change in the offer to the passenger was achieved at that time (only limited additional train services were operated once implemented) leaving the key upside being performance related benefits alone.

Chiltern has managed its investments in a number of ways, the most significant have been i) direct funding through its holding company for specific long term assets (for example Warwick Parkway and depots) ii) via a DBFT structure for one of the Evergreen phases, and ii) through agreeing a track access charge uplift to fund investment on the RAB for BIOX.

DBFT is as applicable now as it was then; by essentially agreeing upfront the amount to be paid for the infrastructure provided the risk of providing the infrastructure is transferred to the DBFT party. This is exactly the way in which bespoke Government funding (for example New Stations Fund) operates, the scheme promoter takes delivery risk and Network Rail makes a fixed payment for the asset once completed.

Longer term franchises would also provide the opportunity for off-balance sheet funding of infrastructure assets of all classes (clearly track is more difficult than car parks to fund due to the respective risk profiles), but a twenty year franchise would allow this to happen (giving time for a 15 year fund agreement plus an equity tail). Indeed, short term franchises also provide a funding

capacity through the 'franchised assets' process, by its nature this is more complex for assets with a life of greater than 3 years.

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?

There are number of factors for private sector capital: manageable size of investment, clear and simple mechanism for allocation of revenue, understandable risk allocation between the various interacting and interfacing parties, clear security over (and potentially access to remove) the assets funded, and an acceptable risk level that can be taken through debt and equity risk committees.

Clearly a number of barriers exist in the railway to making this easy: railway operates as a system with the major assets (track, signalling) inseparable from the whole, track and train and people interfaces, complex revenue allocation systems, high levels of inherited and residual risks (particularly asset condition and contamination), high transactional costs of disaggregation (including rates).

Some of the potential ways in which private sector capital could be introduced are outlined in the answer to 24 above.

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.

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?

See answer to 24 above.

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

In addition to the various points made elsewhere, the following:

- Risk sharing / allocation between third party and Network Rail in terms of costs and programme;
- Network Rail to be made more accountable to the 3rd party for failure to deliver;
- Transparent procedures that demonstrate that 3rd parties receive parity of treatment, prioritisation;

Risks and implementation

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