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# **Developing Britain's railways: serving customers, improving delivery and the role of independent regulation**

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**Speech to the Westminster Energy, Environment and Transport  
Forum, on developing the UK rail network  
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It is a pleasure to give this talk this morning, which I hope will help to set some of the background for your discussions today on the future of the rail industry.

Britain's railways are a great success story. The industry has seen sustained rises in demand from passengers and freight customers in the last decade, and has generally seen rising customer satisfaction, against a background of accommodating more trains on a network which is close to capacity in many places. Britain has the fastest-growing rail sector in Europe, and consistently scores among the highest in key aspects of passenger satisfaction. Though we must robustly guard against complacency, Britain also has one of the very best recent safety rail records in Europe.

As I will discuss, this success and growth brings with it its own challenges. I will talk about these challenges, and how the industry needs to respond. First, I will explain briefly what the Office of Rail Regulation (ORR) does, how we work, and why it matters.

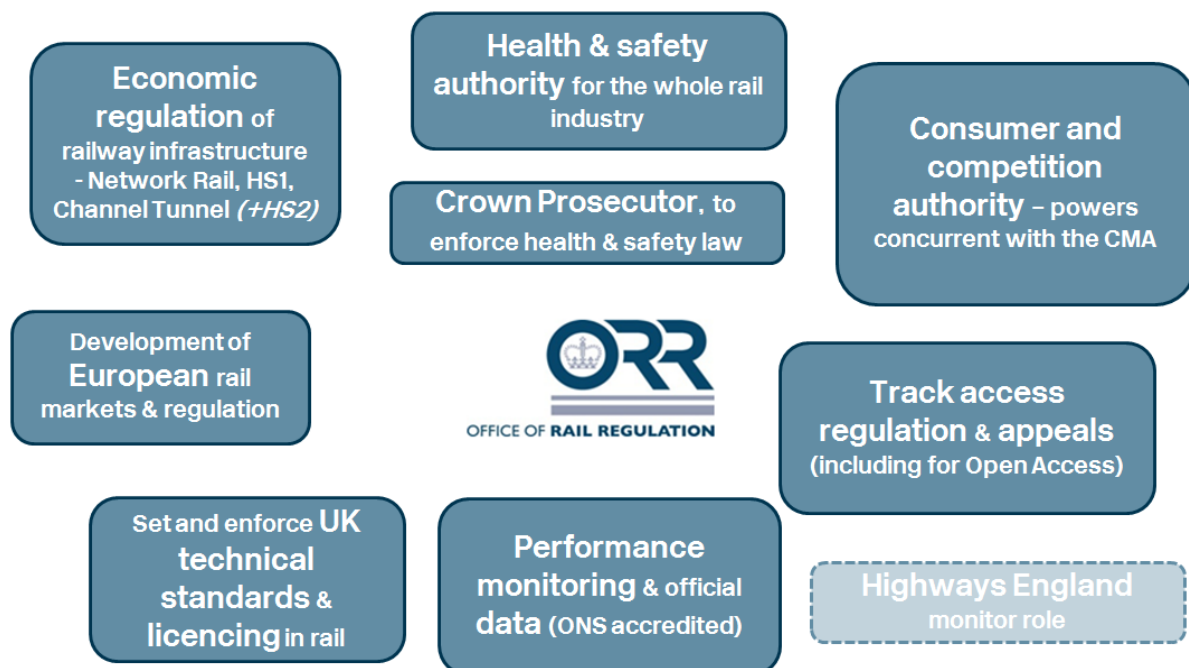
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## An expert, independent regulator for the railways

ORR is the economic regulator for railway infrastructure, the health and safety regulator for the rail industry as a whole and the industry's consumer and competition authority. We are also the national safety authority in European terms. From April, ORR will take on an additional responsibility for monitoring the development of the strategic road network.

**Chart 1: A combined economic and safety regulator for the railway industry: Functions of the Office of Rail Regulation**



Source: Office of Rail Regulation

In rail, there are a number of specific elements to our role:

- We are the economic regulator for the railway infrastructure, covering Network Rail and HS1.
- We aim to strengthen incentives for the whole industry to work together to drive greater efficiency from the use and maintenance of existing railway capacity, and more cost-effective investment in the network.
- We are also the health and safety regulator for the rail industry as a whole (including main line, metro, tramways and heritage railways).

- We are responsible for enforcing the law and ensuring that the industry delivers continuous improvement in the health and safety of passengers, the workforce and public, by achieving excellence in health and safety culture, management and risk control
- We are also the rail industry's consumer and competition authority, which includes policies and CoP's on complaints handling, accessibility, ticketing and fares.
- We are the appeal body for various forms of dispute within the industry – often being asked to help to solve problems before they become formal disagreements, helping the industry to work effectively and efficiently;
- We provide transparency- expert insight into how the industry works and what it can deliver; and through our reports, analysis and publication of data we shine a light on the industry's performance and efficiency so that it is open to scrutiny by the public, politicians taxpayers and rail users, and so it can be held to account.
- Finally in rail, our remit also extends to:
  - providing independent advice to Parliament, government and industry about the future of the railways; and
  - working with other regulatory authorities in the UK and rail authorities across the world to develop best-practice standards in railway regulation

We take a strategic approach to applying our expertise across these varied roles. We therefore plan our annual activities in the context of our long-term vision for the railway, and in pursuit of our six strategic objectives as an independent regulator.<sup>2</sup>

We work in an integrated way bringing our teams of experts together to collaborate on finding solutions to the challenges facing the industry. We

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<sup>2</sup> For more information on ORR and its role, please see our website: [www.orr.gov.uk](http://www.orr.gov.uk)

believe this approach brings significant benefits to the rail industry, to funders and consumers, and will benefit highways development as well.

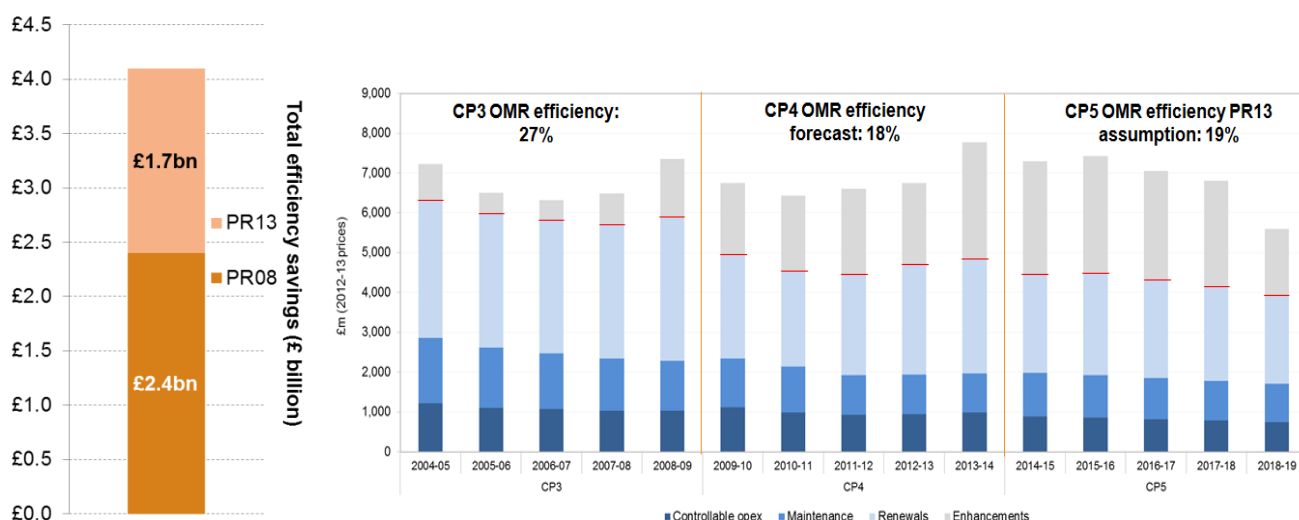
## An effective model of regulation

The UK needs a railway that is safe, efficient, meets the needs of passengers and is flexible and responsive to change. The model of five year planning and delivery that ORR applies, which delivers a credible focus on whole-life costs, has been proven to be an effective and efficient way of regulating long-term capital assets whether they are in the public or private sectors and regardless of the source of funding. This model has delivered substantial benefits:

- Over the last decade Network Rail's efficiency has improved by nearly 40 per cent, and ORR's latest review will see the company close the gap with the most efficient European rail infrastructure operators by 2019.
- These reductions in the day-to-day costs of the railway have freed up resources to reinvest in a better railway.
- Notwithstanding recent challenges, punctuality has improved and with it, customer satisfaction.
- Britain's recent rail safety record is good, and we challenge the industry to retain its place among the safest railways in the world.

Government will continue to want to procure rail projects and services into the future, and it is important that it is a sophisticated and informed purchaser. ORR supports this by providing appropriate and expert challenge within the system, to help control costs and hold Network Rail and others to account for delivery.

**Chart 2: Savings of over £4 billion of taxpayers' and customers' money identified since 2004 in ORR's Periodic Reviews of Network Rail. A further 19% reduction assumed over the current control period to 2019**



Source: Office of Rail Regulation

## ORR is independent and accountable

The independence and accountability of a body like ORR is important if we are credibly and visibly to put customers' interests first. We ensure that there is fair and equal treatment between companies in the sector – for instance in access to the network and in objectively resolving disputes - which is essential for continued investment and competition, and allows a stable longer-term view to be taken. It helps to give confidence to government to invest, but also to private investors and businesses in the industry – for example in the supply chain, in rolling stock, and the privately-owned HS1 network.

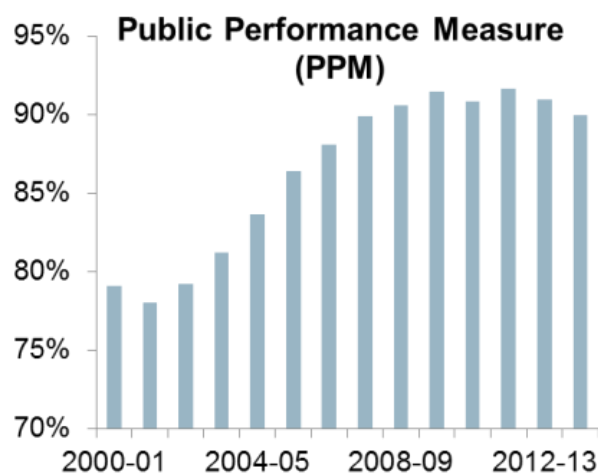
We are here to help inform the difficult trade-offs expertly, with use of evidence and analysis. Accountable to Parliament, we guarantee transparency and public accountability, shining a light on how the system is delivering, and on how it is using customers' and taxpayers' money. We also take a joined-up approach between England, Scotland and Wales, while supporting the different priorities of the governments in each country.

## Why does this matter?

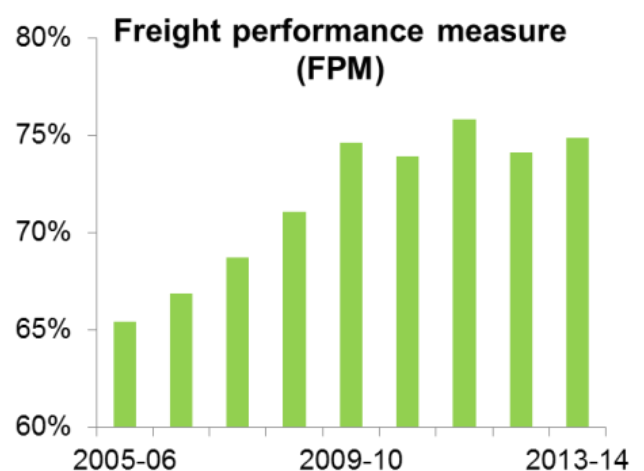
The success of rail over the last decade in attracting growing passenger numbers, more freight traffic and providing new train services brings with it real challenges. It is harder to maintain performance and to meet customers' rising expectations on a more congested network. And while the industry has attracted investment from government in new and improved capacity, it is a major challenge to deliver major complex projects on a live network while meeting obligations to today's customers. There present risks to hard-won improvements in the industry's performance and efficiency.

**Chart 3: ORR has set stretching performance targets in the past 5-10 years and has overseen record levels of punctuality for passenger and freight against a backdrop of sustained growth in customer demand**

Between 2001-02 and 2013-14 the Public Performance Measure (PPM) of passenger trains that arrive at final destination on time has increased from 78% to 90%.



Between 2005-06 and 2013-14, freight punctuality has increased from 65% to 75%.



The value of a joined-up approach is that the challenges of ensuring the safety, the efficiency and the performance of the railway are overlapping and often have common causes and remedies. ORR adds value by combining the regulation of these functions together with a sharp focus on the interests of the railway's customers.

**Chart 4: ORR's combination of functions means that we can efficiently bring a range of expertise to drive better results from the industry**



A benefit of being both independent and joined-up is the ability to build an expert multi-disciplinary professional team to drive better regulatory outcomes. We bring together experts in a number of specialist areas to deliver better regulatory outcomes for the industry, its funders and especially its railway users. The ORR team includes:

- Commercial and financial expertise in rail markets.
- Regulatory economists with cross-sector expertise in regulation of network monopolies.
- Multi-disciplinary engineering teams, expert in rail infrastructure performance and costs.
- Consumer and competition regulators.
- Health and safety inspectors, risk experts and prosecutors.
- Industry-leading legal advisors on UK and European rail statutes.

While pressing for better results and delivering efficiently, we have also reduced our own costs consistently in real terms over the last five years – cutting the cost of ORR, while also finding ways to cut red tape.

We firmly believe, based on the evidence of past failures, that there is no trade off to be made between an efficient railway and a safe railway, and we take a

joined-up approach to regulating for both objectives. For example, in our most recent periodic review of Network Rail, as well as setting efficiency targets, performance requirements and scrutiny of project delivery, we focused on the imperative that the railway remains safe for its passengers, workers and the public. Our experience is that effective safety management supports management of business delivery risks and can improve efficiency. Equally experience shows that compromising on safety will undermine all other objectives for the railway. Joined-up, independent regulation helps to make sure that efficiency, delivery and safety objectives are not just reconciled but are mutually reinforcing.

## Setting funding and targets for the industry: how the periodic reviews work

Ultimately as key funder, it is the governments in London, Edinburgh and Cardiff who decide **what they** want from the railways and the **level** of investment they want to make to enable this. Of course as customers pay a higher share of the railway's costs they too must have a greater say in setting expectations on what they get for their money, and we are developing better ways to do that for our next 5-year periodic review.

Through the periodic review process, we determine:

- the **outputs** that Network Rail must deliver in the next control period (building on the governments' High Level Output Statements), including passenger performance and enhancement programmes;
- the **funding** that Network Rail needs, to deliver the outputs efficiently;
- and wider sector **incentives** and the financial framework.

Each control period covers 5 years:

- PR13 covers Control Period 5 (or CP5) (2014- 2019)
- PR18 covers CP6 (2019 – 2024).

Our final determination for PR13 laid out an ambitious plan – challenging but achievable- for the rail industry, including:



- £12bn of investment in a better railway with more capacity;
- £1.7bn savings – a 19 per cent efficiency improvement - from Network Rail's plans, delivering a good deal for passengers and closing the gap with Europe's best rail infrastructure; providers
- delivering a safer and more resilient railway through £109m to achieve a 25% risk reduction (through closure of 550 at risk level crossings); £200m for track worker safety; and £560m for to tackle a backlog of renewals of civil structures like bridges and tunnels;
- regulatory targets for asset management that drive a switch from a 'find and fix' culture to one of 'predict and prevent';
- new performance targets, designed to deliver a better deal for passengers and freight customers through less disruption, fewer cancellations for long distance trains and a minimum of **9 out of 10 trains** to be on time;
- and support for the freight network to improve capacity reliability and efficiency for growing freight on rail.

## Delivery in the first year of Control Period 5

We are in the first year of the new control period, CP5, and our Monitor report for the first six months of CP5 was published in November.<sup>3</sup> It found that:

- good progress had been made in reducing safety risks at level crossings;
- national train punctuality was 0.7% short of the level expected (89.1%) and that what progress Network Rail was making against its performance recovery plan was not having the desired effect on punctuality. We subsequently requested the plan be adjusted appropriately;

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<sup>3</sup> Office of Rail Regulation: Network Rail Monitor, Q1-2, 2014-15 (November 2014) <http://orr.gov.uk/what-and-how-we-regulate/regulation-of-network-rail/monitoring-performance/network-rail-monitor>

Chart 5: An overview of the output, finance and efficiency requirements established in ORR's 2013 Periodic Review

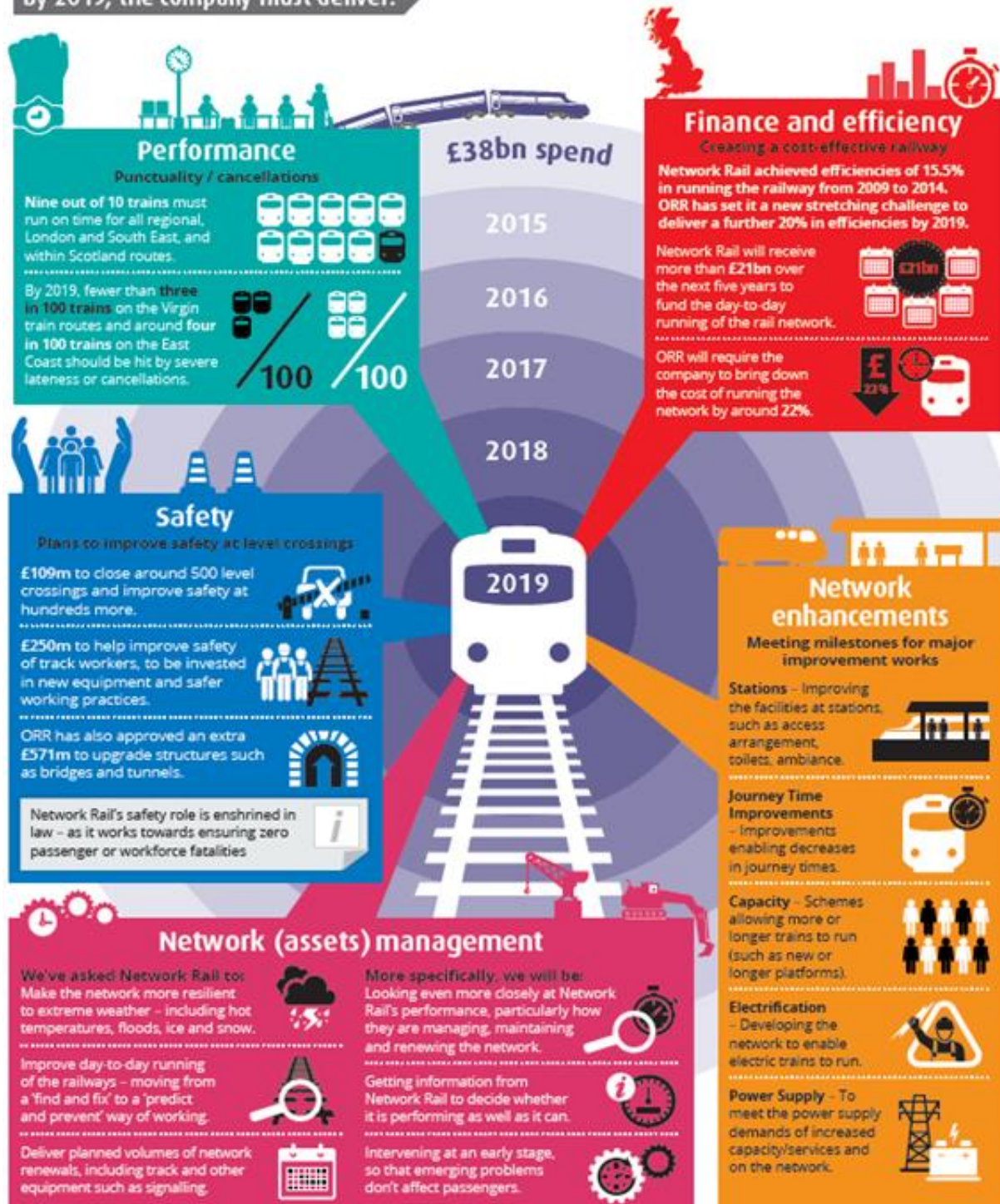
## What does Network Rail need to deliver by April 2019?

Network Rail will spend an estimated £38bn to deliver plans for safety, performance and value on Britain's railways, between 2014 and 2019

The independent rail regulator is closely monitoring the company's progress.



By 2019, the company must deliver:



- performance on train cancellations was behind schedule with 13 of 18 franchisees missing their target;
- Network Rail had delivered less work than planned in maintaining and renewing the network with a lack of reliable data impacting its ability to work effectively. We subsequently sought assurances that work would be recovered later in CP5 and data quality improved;
- following successful delivery of enhancement projects in CP4, we have seen Network Rail's performance on enhancements slipping in the first months of CP5- with 11 of 44 regulated targets being missed. In response to this we have asked the company to tell us how it is going to recover the position;
- Network Rail forecast that it would spend £112m more than we assumed in 2014-15- though this is small in the context of a £38bn programme across 5 years, and they have flexibility to bring forward spend where this is more efficient offers earlier or surer benefits to customers.

We are continuing to work with Network Rail to make sure the necessary improvements to their processes and performance are in place so that it can get back on track and deliver across the overall control period. It is very important to remember that our Monitor in November reported only on the first few months of a five-year period, and while it helps us to understand where Network Rail is on course and where risks are emerging, it needs to be seen in the context of delivery over the whole five-year period.

This is a significant challenge for Network Rail, and it is vital they deliver for their customers. But what can be lost though in the focus on short term statistics is the overall benefits that progressive and efficient regulation can bring and has brought to the Britain's railways.

## What is the value of economic regulation?

There is competition for tighter public funding both now and in the future and this requires that the rail sector become more efficient and, importantly, shows that it is becoming more efficient

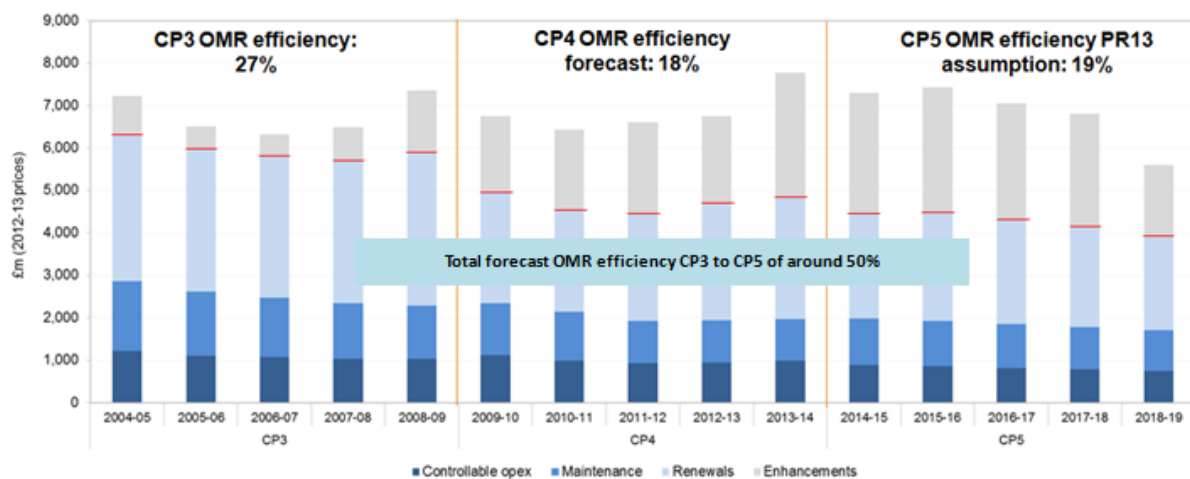
We have set progressively challenging efficiency targets for Network Rail and this has helped force change

By the end of 2018-19 Network Rail should have improved its efficiency by around 50% since 2004 – effectively freeing up funds which governments in London and Edinburgh have chosen to reinvest in improving the network to meet growing demand and provide better services.

At the same time, we have seen performance improvements, with the public performance measure (PPM) increasing from 78% in 2001-02 to 90.9% in 2012-13. This shows a 13% increase in the number of passenger trains which arrive on time at their destination.

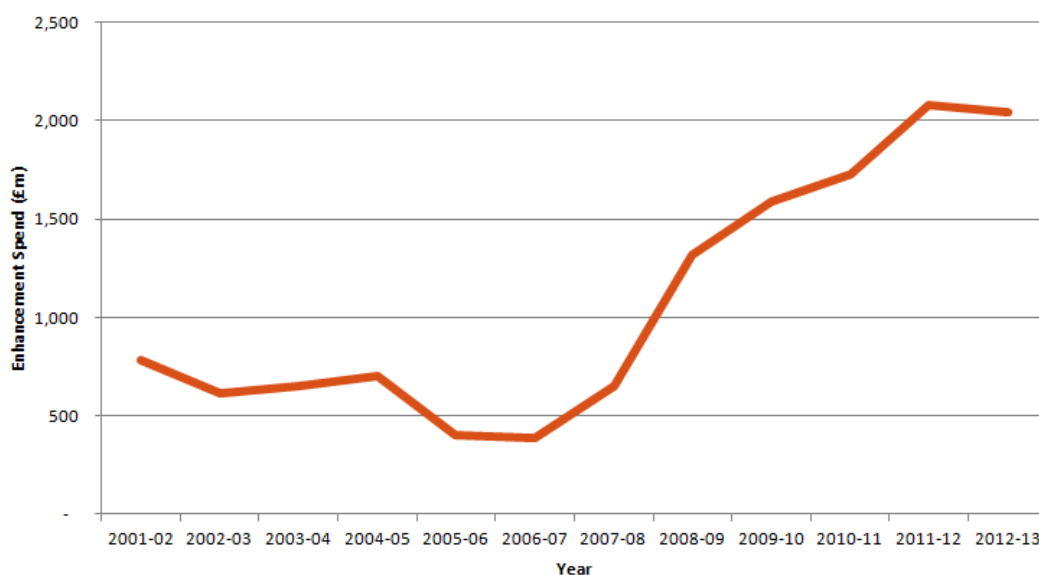
We have also borne down on infrastructure costs/efficiency, resulting in costs being brought under control and projected to fall further, giving Government confidence to invest in network enhancements. Network Rail's spend on enhancements in the last 12 years – with a consistent and transparent regulatory monitoring of delivery – has increased by 160% from around £790m in 2001-02 to £2050m in 2012-13.

**Chart 6: Network Rail operating, maintenance and renewals costs; and enhancement spending, 2004-05 to 2018-19: improved efficiency frees up funding for network growth and improvement**



Source: Office of Rail Regulation

**Chart 7: Network Rail capital spending on network capacity growth and improvement ('enhancement'), 2001-02 to 2012-13. £ million, nominal prices.**



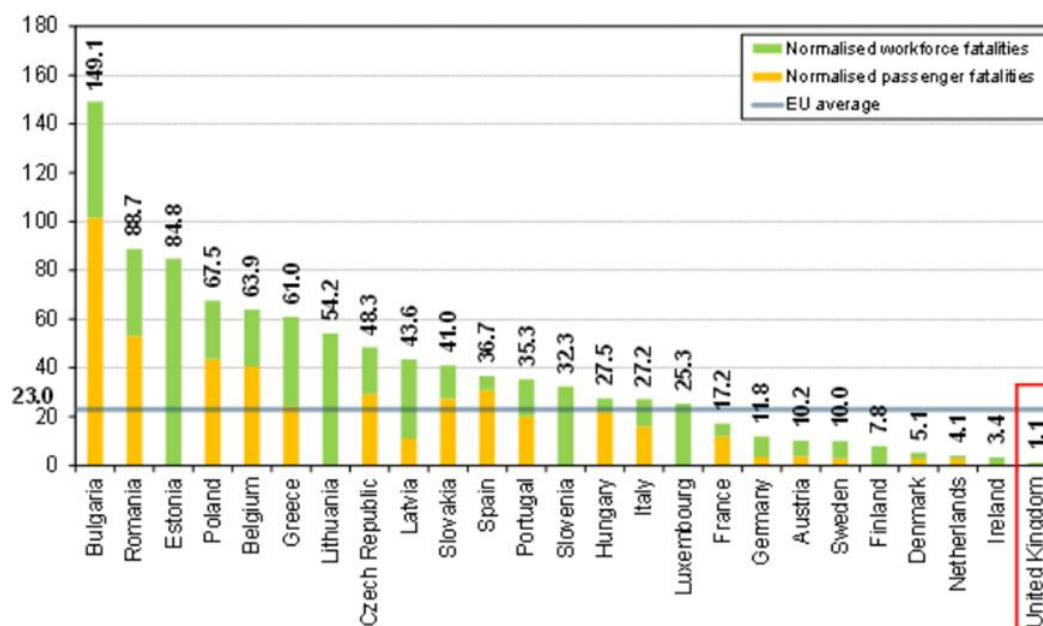
Source: Office of Rail Regulation

## The value of safety regulation

Safety regulation is a critical part of ORR's role. Confidence in rail is underpinned by a good recent safety record, based on steady improvements in safety and a reduction in underlying risks. We are now amongst the best in Europe, though we cannot afford to be complacent

Part of the future challenge we face as a regulator is to ensure that innovation and efficiency do not compromise safety. One method is for us to have early involvement at the planning stage, for example we now have a MOU with HSE for Crossrail and HS2, which allows ORR to be more involved in the design of future railway infrastructure.

**Chart 8: Comparative safety across Europe fatalities per million train kilometres, 2008-2012**



Source: European Rail Agency, and Office of Rail Regulation, Health and safety annual report, 2013-14

It is also important to have a really strong vision for zero fatalities if the rail industry is to continue on the path of an ever-decreasing health and safety risk – much of this depends on having the right management culture which



increases the likelihood of compliance and thereby the likelihood of the control of risks on a daily basis.

## Improving the experience of passengers

We have seen huge rail passenger growth in Britain over the last twenty years and passengers deserve a better deal. They have to be at the heart of our approach to regulation and we have focused in some key areas of passenger concern to ensure that this is the case:

- **Complaint handling policies** – we’ve published a regulatory statement to set out our approach to KPIs and will be monitoring progress against this, whilst revising policy guidance to draw out best practice
- **Disabled People’s Protection Policies (DPPPs)** – we’ve issued new guidance to TOCs to help them meet DPPP standards and will be reviewing their compliance and driving improvements
- **Passenger information during disruption (PIDDD)** - we have formally requested sight of the TOCs plan for comment and agreement, after which ORR will monitor progress as part of license compliance.
- **Ticketing Code of Practice** – this is designed to ensure passengers get the information they need to make informed decisions when choosing and buying tickets
- **Rail retail review** - intended to facilitate competition and innovation in the retail market for ticket sales to make sure customers can get a better deal

## Looking to the future: what could we do differently to improve value for money and meet customers' expectations?

It's an exciting time for the rail industry – we're seeing a high level of investment and numerous projects, from HS2 to electrification, which will improve the railways for our customers, as well as opportunities from digital signalling systems to transform the way rail infrastructure operates. At the same time, increased funding brings increased scrutiny and we are all being challenged to think differently about how the railway will look and operate in the future.

Factors such as the current shift to more local decision-making on transport issues and the increase in capacity that HS2 will bring, are challenging us to think carefully about how we may choose to set future output measures to underpin delivery or incentivise new ways of working.

We are already thinking about what this means for our next Periodic Review in 2018, which will cover the five years to 2024. Building on work we started in PR13 looking at potentially significant regulatory changes such as:

- What role can **Network Rail's routes** play in the way the infrastructure is managed and regulated? How can comparisons between routes help us to judge NR's performance, capability and potential overall?
- Can a greater focus on NR as **system operator for the network** lead to better decisions around the use and development of capacity, performance and investment? A system operator could take an enhanced role in developing and delivering robust timetables (short term), maximising the capacity of the existing network (medium term) and the strategic planning of technologies for managing the network and enhancements (long term).
- How can regulation and the **flow of funds in the industry be changed to improve and align incentives**? We know that large fixed charges, a big grant direct from government and clauses in franchise contracts undermine incentives for Network Rail and train operators to improve



whole-system efficiency costs or capacity use. How can we make this better? The reclassification of Network Rail to the public sector potentially creates an opportunity – for regulator and government - to resolve parts of the problem.

- A change to the way the industry is funded could involve **revised charging arrangements so that subsidy for socially-desirable services flows directly to the services government (national or local) wants to support** (ie to freight and passenger train operators), and Network Rail's charges reflect the direct costs of using the network. This way operators would have more reason for thinking innovatively about how to deliver for their customers, and for reducing the cost of infrastructure; and Network Rail would have a stronger incentive to deliver reliably and responsively for its customers. Changing the flow of funds sounds dull but has potentially profound effects on behaviours and the focus on customers and efficiency across the industry.

These are big ideas, and big challenges. They could substantially change the way the industry operates. They could make the industry more commercially self-sustaining, and allow it to become more responsive to customers' needs and expectations. They could allow delivery and service decisions to be devolved so that the industry has an even sharper focus on serving its customers, rather than centralising decisions on what customers ought get for their money in Whitehall.

In the industry, in government and in the ORR we are all under pressure to operate in a more efficient and effective way. The whole sector needs to work together to demonstrate value for money and to show that the customer really does come first.

**Richard Price**  
March 2015