NetworkRail

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Dear Richard

ORR Business Plan Consultation (Financial Year 2013-14)

Following ORR's industry conference on 7 February 2013, Network Rail welcomes the opportunity to respond to ORR's consultation on its Business Plan for 2013-14. We thank ORR for the extension of time that it has afforded us to respond to this important consultation. No part of this response is confidential and we are happy for it to be published in full.

In general terms Network Rail is satisfied that ORR's draft Business Plan sets out the right balance of activity for the next year. We have a number of comments to make in relation to ORR's consultation and for clarity our comments are set out under the five strategic objectives outlined in ORR's Business Plan. We comment separately on ORR's proposed budget for 2013-14.

Securing value for money from the railway for users and funders

The 2013-14 financial year is a critical year for the railway in that it will see the completion of the Periodic Review which will in turn determine Network Rail's outputs and funding for the next five years to 2019-20.

We appreciate and expect that over the course of the next financial year, considerable effort will be expended in assessing Network Rail's Strategic Business Plan and in making your draft and final determinations. Successfully completing a Periodic Review is a significant undertaking and it will be important that the review sets an appropriate regulatory framework, with associated targets and incentives for CP5. It therefore seems entirely appropriate that delivering the Periodic Review and creating appropriate incentives for CP5 is ORR's principle output under this objective this year.

We share ORR's view that the outcome of the Periodic Review should reflect what customers and society want, allow ORR to hold Network Rail to account but not stifle innovation. We welcome ORR's focus on growth, and on making unfocussed subsidy more transparent. This is turn will help to create a more 'normal' market and allow ORR to step back from formal regulatory control. We comment on this final point in more detail later in this response.

We note that one of ORR's stated priorities for 2013-14 is to 'create a framework...that facilitates sensible decisions on trade-offs'. This is an important area of work – particularly

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when considering performance, costs and capacity issues. We agree that this is a critical area of work that should be progressed as part of the effective delivery of the Periodic Review.

A drive for a safer railway

We welcome ORR's continued drive for a safer railway. Safety is Network Rail's number one priority. Our commitment to achieving excellence in our health and safety culture, management and risk control is aligned with ORR's. We therefore agree that a significant proportion of ORR's front-line inspection activity should be focussed on high-risk activities and in ensuring that the industry acts in response to known safety issues.

More generally, ORR has now acted as the combined safety and economic regulator of Britain's railways for the past seven years. During this time, ORR has taken some positive steps towards 'joining-up' its economic and safety functions but to an extent it often feels as if these activities are distinct from each other. We therefore believe that during 2013-14 ORR should do more to ensure that these functions are complimentary as opposed to conflicting or 'stand alone'.

Supporting a better service for customers

What role ORR should play in terms of supporting a better service for customers formed a cornerstone of the discussion at ORR's consultation conference on 7 February 2013. There are clearly divergent and often conflicting views about what role ORR should play in this space. Regardless of this debate, we believe there is a clear need to avoid duplicating work which is currently undertaken by other industry players and to ensure respective accountabilities are clear. For example, in its Business Plan ORR proposes to 'conduct new research to understand the aspects of rail services that customers most value…and consider customer research in to ticketing complexity.' On the face of it much of this planned activity seems to duplicate Passenger Focus' existing role and its stated mission to get 'the best deal for passengers' through evidence-based campaigning and research'.

In terms of specific recent activities to support a better service for customers, Network Rail was broadly supportive of the modifications to our network licence which imposed further accountabilities on the industry in terms of the provision of customer information (particularly during times of disruption). We believe that this was a positive step forward and has there has been in marked improvement in how the industry interfaces with its customers when reacting to disruptive incidents.

Notwithstanding this, we believe that any changes or transfer in regulatory responsibilities i.e. the proposal to move accountability for the regulation of Disabled Persons Protection Policies and Customer Complaint Handling obligations from DfT to ORR should avoid the risks of double jeopardy (e.g. through regulation by both ORR and government); arbitrarily shifting goal posts (e.g. by changing the arrangements after letting a franchise without providing for appropriate compensation); and creating a continuous regulatory ratchet effect (e.g. where regulation is introduced in response to a specific issue but where reducing unnecessary regulation is difficult). These issues are fundamental to the credibility and effectiveness of the regulatory and contractual regime and any change in responsibilities should take these matters seriously so that they do not create additional regulatory risk or other unintended consequences.

As Network Rail stated in its response to ORR's consultation 'A greater role for ORR regulating passenger franchises in England & Wales' there are strong benefits to rail users and taxpayers from improved alignment between industry parties and greater flexibility for them to meet government requirements in the most efficient way. However, any changes in regulatory responsibilities between ORR and government should be judged in this context and the benefits should be evaluated robustly against what can be achieved within the existing allocation of responsibilities. In particular, careful consideration should be given to the need to provide stability and confidence to the industry and to avoid unnecessary risk whether this is actual or perceived. Inappropriate or badly implemented changes in regulatory responsibilities have the potential to make the current railway more expensive and therefore any change should be evolutionary.

Promote an increasingly dynamic and commercially sustainable sector

In short, we entirely welcome ORR's objective to support sustainable economic growth by promoting innovation and efficient long term investment through the appropriate development of effective markets, and, where necessary, regulatory intervention.

At its industry conference ORR indicated that a key indicator of its success would be a need to regulate less and allow the rail sector to operate more normally. We agree and we welcome ORR's focus on growth, and on making unfocussed subsidy more transparent.

To achieve this objective, we believe that ORR must make sure that its approach to regulation is targeted and focused and does not import any undue regulatory risk – which is a key issue for businesses in the railway and for their investors.

We strongly support changes in regulation and franchising which result in a broader specification of what government wants from the industry, greater flexibility to enable the industry to deliver these requirements efficiently and improvements which encourage better alignment between industry parties. Critically we must strive together to simplify and improve understanding of the regulatory regime.

A regulatory regime that is focussed on dealing with issues of material concern (as opposed to micro-managing individual industry issues) is key to achieving an appropriate balance between these risks and the more obvious interests of taxpayers and rail users. We believe that ORR should only intervene where it can add value and its influence can make a difference. At the very least, this reinforces the need to avoid unnecessary change, for changes to be evolutionary rather than revolutionary, for a strong focus on key principles, for robust impact assessment and for effective communication. The growth of Britain's railway industry over the past decade is an outstanding success story. There is more that must be done, for example, in terms of achieving industry efficiencies, but we believe that the industry, through its existing channels, including the Rail Delivery Group is well placed to deliver the change and reform that is needed.

If the industry acts responsibly Network Rail believes that ORR should be willing to step back from formal regulatory control – a point that we made in our recent response to ORR's consultation on the regulation of land disposals. We are keen to see wider application of this approach and with this in mind we were hoping to see some more emphasis in ORR's plan on the need to encourage and support alliancing arrangements between Network Rail and its customers which we believe will be an important enabler in terms of delivering a more dynamic and commercially sustainable sector.

Be a high performing regulator

ORR's stated objective to be a high performing regulator is obviously welcome as is ORR's commitment to make efficiency savings in the next financial year. Network Rail believes it is essential that it has a capable and confident regulator which is able to make difficult decisions, to hold it to account where necessary and to help it to highlight key choices where appropriate. We believe that over the course of the next year, both Network Rail and ORR should reflect on the discussions that have already taken place about the motivation model – with regulation seeking to empower effective delivery by our people in collaboration with our customers and suppliers. We recognise that both Network Rail and ORR need to change to make this happen. We need to make sure that our respective organisations are focussed on having the right conversations, in the right way at the right time. The changes that ORR is making to its regulatory escalator will no doubt help us achieve this but we must remember that this is only a tool and is not a substitute for open, honest and transparent debate about the challenges that Network Rail and the wider industry faces. We are keen to focus these conversations around our long term strategic themes.

The capability review that was undertaken by ORR last year was important. We recognise that ORR has taken steps to address the issues identified in the review and has strengthened its top-team with the appointment of a new Chief Executive, a new Director's of Railway Markets and Economics, a new Director of Railway Planning and Performance and a new Strategy Director. We strongly welcome the appointment of high calibre individuals to the ORR.

Notwithstanding this, a key issue for consideration with any major organisation change will be the competences and capability required throughout the organisation both to manage change and to discharge any changed responsibilities. As we have previously stated the integration of safety and economic regulation has been positive but it has inevitably raised significant challenges for ORR. The capability review undertaken by ORR was a positive step but any significant increase or changes in ORR's responsibilities would undoubtedly necessitate further consideration of these issues. As with other organisation changes the scale of the challenge should not be underestimated.

Aside from its Executive team, we believe that the capability of ORR's entire office will be a critical enabler of its aim to be a high performing regulator. In this regard we note that last year's capability review recommended that:

"More technical and engineering capability should be brought in-house and the use of Reporters reserved for resource peaks and specialist advice. The credibility of ORR will increase if the industry knows it has a greater breadth of respected and experienced people."

Unfortunately, we have yet to see any evidence that the implementation of this recommendation is being progressed. Independent Reporter spend has increased consistently and substantially during each of year of this control period and has almost tripled since 2009-10. In 2009-10 Network Rail incurred costs of £1.3m relating to Independent Reporter activity. This year that is forecast to increase to circa £4m. Thus, whilst we commend ORR on its desire to reduce its direct costs, the overall picture in terms of the 'cost of regulation' is somewhat different when the costs of the Independent Reporter are taken in to account. From Network Rail's perspective, we believe that ORR should be focussed on how to reduce the overall cost of regulation as opposed to solely its own direct costs.

We of course recognise that ORR will want to assure itself about the credibility of our plans for the next control period and that much of the recent Independent Reporter activity has been focussed on assessing these plans, which has in turn put a strain on ORR's 'in-house' resource. However, we are concerned that ORR appears to be increasingly reliant on the Independent Reporter to provide assurance and is not building or retaining its own capability. Longer term we believe that this could affect ORR's credibility. We would therefore urge ORR to assess whether the current mix between Independent Reporter and 'in-house' activity is appropriately balanced.

Budget matters

In terms of specific 2013-14 budget matters ORR's Business Plan states that it has identified efficiency savings across its activities which will result in a 4 per cent reduction in ORR's annual cost in real terms next year (although we understand (following ORR's recent workshop) that ORR has since revised this figure to 3.5 per cent).

Whilst the negative refinement to committed efficiencies is disappointing any savings are of course welcome, particularly at a time when the industry that ORR regulates is committed to stretching efficiency improvements over the course of the next control period.

Separately, we note that ORR's Business Plan only confirms its proposal to work within a reduced budget envelope for 2013-14. We believe that it should be entirely possible for ORR to make efficiency saving throughout CP5 (without compromising its strategic objective to be a high performing regulator) particularly as ORR's volume of work might reasonably be expected to reduce after the current Periodic Review has been concluded (notwithstanding the commitment to undertake an early review of the structure of charges for CP6 to inform the next periodic review. We would therefore encourage ORR to consider the scale of efficiency savings that it might be possible to make over the course of the next control period and beyond in its longer term regulatory statement that we understand ORR will be consulting on later this year.

Yours sincerely,

Paul Plummer