



Holding HS1 Ltd to account in CP3 – interim policy for stations funding

DfT published its PR19 Final Decision in October 2019 with a commitment to working with HS1 to agree on evidence and reporting that will support future reviews.

In taking on responsibility for periodic review of HS1 stations under the stations leases, we will seek to ensure that this work continues and remains aligned with the principles of regulatory best practice. We welcome commitments made by HS1 Ltd and its contractors to providing the required information to enable that to happen.

There are various ways for HS1 Ltd to demonstrate that its plans meet the Life Cycle Purpose for each station, and wherever possible the information that it already produces to operate its business should be used to meet these requirements. However, there may be instances where we may require further analysis, and would expect to be able to agree a method for demonstrating compliance between us, including the use of benchmarks and comparators as necessary. We are committed to continuing to work with stakeholders to ensure that these methods are appropriate and proportionate.

Aim and objective

We regulate HS1 stations in accordance with the terms of the HS1 Stations Leases dated 30 September 2010 between HS1 Ltd and the Secretary of State (the Stations Leases). In addition to our role under the Stations Leases, we also have responsibilities under the Concession Agreement between the two parties, and under The Railways (Access, Management and Licensing of Railway Undertakings) Regulations 2016 (the Regulations).

Our approach to holding HS1 Ltd to account in CP3 aims to strengthen or create incentives to:

- identify opportunities for innovation or research and development which support HS1 Ltd's achievement of the Life Cycle Purpose for each of its four stations;
- encourage effective, transparent, inclusive and well-governed stakeholder engagement by HS1 Ltd; and
- if necessary, take direct regulatory action to resolve concerns as early as possible to minimise the impact on operators, passengers and freight customers.

Approach

Our approach to holding HS1 Ltd to account is informed by principles of regulatory best practice. In particular, our approach will be:

- Risk-based – this means that we will focus our resources where we consider the risks are greatest.
- Targeted – we will target our detailed monitoring and escalation activities at those areas where an issue, such as a potential non-compliance, has been identified and is material. This is with a view to reinforcing accountability and appropriate incentives on HS1 Ltd.
- Proportionate – so that any actions we take reflect the scale and nature of the problems we are seeking to address and the likely costs and benefits to different parties of taking action
- Transparent – so that we are clear with stakeholders about our view of HS1 Ltd's performance, we will state where we have any concerns and what action we are taking.
- Predictable – we will provide a stable and objective regulatory environment enabling affected stakeholders to understand our approach to making decisions.

We are taking a proportionate approach to monitoring the increased delivery challenge of renewing aging assets. In particular, we wish to monitor and report on how HS1 Ltd is meeting the incentives set out for it by DfT at PR19 by focussing on:

- asset information;
- financial reporting, including the calculation of efficiency;
- use of risk and contingency provisions;
- the delivery of efficiencies set out in its 5YAMS.

What we will publish

The scope of our reporting will vary depending on the coverage, quality, accessibility and timeliness of HS1 Ltd's own reporting. Where it is strong, we have the scope to reduce our reporting and vice versa. As a minimum, we expect to always publish an annual report of HS1 Ltd's performance on route and stations.

Monitoring and assessment

Asset Information

DfT's Final Decision required HS1 Ltd to improve its monitoring of assets and production of asset information with a view to better forecasting future renewals. We intend to continue to monitor HS1 Ltd's progress towards this goal through quarterly and annual reporting on its asset knowledge.

Financial performance and efficiency

We will monitor HS1 Ltd's financial performance using a range of qualitative and quantitative information, from sources including a combined asset management annual statement (AMAS) for route and stations. We expect the AMAS to provide transparent narrative on:

- whether HS1 Ltd has achieved financial outperformance (that is, Life Cycle Works Savings) against the forecast renewals spend, and the resultant payments due to funders under the Stations Leases:

- portfolio efficiency: a comparison of expenditure on renewals activities undertaken by HS1 Ltd against the value of the outputs on a like-for-like basis over time;
- an assessment of how the cost efficiency compares to the targets set in the PR19 Final Decision, as well as contemporary indicators/benchmarks from within (and outside) the industry; and
- a quantitative and qualitative assessment of risks, both what they are and how funding has been used efficiently to meet the risks.

We expect HS1 Ltd to provide the following information for our monitoring of the escrow account:

- timely and transparent information on its investment decisions during the control period for stakeholders; and
- analysis to show the investment decisions made over the year, that is, how it traded-off liquidity (access to funds) and returns.

Risk-based approach

The scope and extent of our routine monitoring may vary over time as different issues become more pressing for HS1 Ltd. We will make decisions on our approach to monitoring based on factors such as performance against commitments, ability of stakeholders to challenge and hold HS1 to account and the strength of HS1 Ltd's own governance and assurance arrangements.

Escalation

If we identify areas for improvement or concern with HS1 Ltd's performance through our monitoring, we will use a staged escalation approach. The aim of this approach is to resolve issues before they result in enforcement action under the Stations Leases and the Concession Agreement. However, if early resolution is not possible or if there is sufficient evidence that HS1 Ltd is not or is likely not to meet its obligations, we will consider taking enforcement action as set out in the Stations Leases and the Concession Agreement.

This section sets out the escalation stages we will consider if we identify an issue.

Further information

In order to investigate and resolve concerns as promptly as possible it is likely we will request further information from HS1 Ltd and stakeholders, where appropriate. Collecting this information is likely to be in addition to our regular monitoring requirements.

HS1 Ltd-focussed action to resolve

Upon identifying an issue and our expectations for resolution, we will set out and publish our concerns and the actions required to HS1 Ltd. This may provide HS1 Ltd the opportunity to de-escalate our concerns by achieving the desired outcomes quickly. However, we expect HS1 Ltd to act promptly to cascade the relevant actions to those responsible for delivery and ensure that relevant stakeholders are briefed and progress is reported back on.

Public commentary and hearings

The next stage of escalation is that we may decide that the results of our investigation can be published to provide public accountability of the issue. By producing a commentary, and/or correspondence with HS1 Ltd, we plan to make any issues and necessary actions clear and transparent for those affected.

We may choose to hold a hearing between HS1 Ltd and stakeholder affected parties to gather evidence and explore the issues further to enable swift resolution where possible. Hearings will be 'on the record' and we expect to publish a written record of proceedings on our website (respecting commercial confidentiality).

Requiring a formal improvement plan

To resolve concerns in a reasonable timeframe, we may during or in conclusion to an investigation write to HS1 Ltd calling on it to establish a formal improvement plan. This is a further escalation, which recognises new processes are required to fill gaps. This approach may facilitate stronger stakeholder engagement and could help to address performance problems without the need for further escalation.

Possible outcomes from progression through escalation stages

1. Close down – deciding no further action is needed and reverting to routine monitoring.
2. Secure early action and monitor progress – HS1 Ltd provides evidence it is doing everything reasonably practicable to resolve and address the issue(s), but we require further work to be completed, for example through an improvement plan. This is then monitored based on our targeted and risk-based monitoring. The investigation could be restarted if additional and/or new concerns are raised.
3. Contravention or likely contravention of provisions within the Stations Leases – we conclude there is a “case to answer” so issue a letter to HS1 Ltd to confirm this. This sets out the evidence and next steps in the escalation of the issue that is steps leading to enforcement. This provides HS1 Ltd an opportunity to formally respond to our findings, prior to ORR’s Board considering the matter.