

Rail Delivery Group

Response to:

Competition & Markets Authority

Competition in passenger rail services in Great Britain

Date: 16 October 2015

Rail Delivery Group response to CMA Consultation on competition in passenger rail services in Great Britain

Name: RDG

Organisation: Rail Delivery Group

Address: 200 Aldersgate Street, London EC1A 4HD

Business representative organisation

Introduction: The Rail Delivery Group (RDG) was established in May 2011 to lead the industry in delivering a higher performing, more cost effective and sustainable rail network for Britain's rail users and taxpayers.

The RDG brings together the chief executives of passenger and freight operator owning groups with Network Rail. RDG develops policies, strategies and plans for the coherent management of the rail industry and advances the provision of a safe, efficient, high quality rail service for users and taxpayers.

The RDG mission is to promote greater co-operation between train operators (passenger and freight) and Network Rail through leadership in the industry and by working together with Government, the supply chain and stakeholders.

It is committed equally to the long-term health of the railway as well as the need to see improvement in the shorter term.

It does this by developing strategies for the industry to put into practice and by proposing solutions for policy makers to implement.

1. Overview

The Rail Delivery Group (RDG) is committed to the long-term health of the railway as well as the need to see improvement in the shorter term. We do this by developing strategies for the industry to put into practice and by proposing solutions for policy makers to implement.

We therefore welcome the opportunity to respond to the Competition & Markets Authority's (CMA) discussion document regarding the different models for competition in passenger rail services in Great Britain.¹ We understand the CMA is seeking to assess whether greater on-rail competition is feasible and desirable in terms of delivering benefits over the existing model of competition.

The analysis and options set out in the CMA's discussion document are a useful contribution towards evolving the model of competition within the rail sector. We believe the report will contribute to the current debate and help identify changes that could deliver further benefits and contribute to the wider UK growth agenda.

We welcome the CMA's recognition that this is a long-term process, and consider that timing and holistic decision making are critical within a mixed-traffic and multi-market network.

This RDG response therefore focuses on the assessment framework for considering any change; outlines the industry's aims and objectives; and considers other potential options for reform.

In addition, we highlight the success of the UK rail industry and acknowledge the potential for further improvement.

We have welcomed discussion with the CMA on these and other points and have chosen not to provide comments on the specific options set out in the discussion document because we expect that these will be addressed by RDG members in their responses.

2. Industry objectives

The RDG considers it important that any model of competition developed should aim to support a rail service that is consistent with the objectives which the rail industry is seeking to achieve which are as follows:

- Deliver service quality and capacity requirements for passengers and freight;
- Fund investment, through a sustainable funding model;
- Maximise economic return from the industry as a whole;
- Promote dynamism and innovation;
- Encourage an aligned approach between different segments of the industry;
- Provide a stable and predictable environment for commercial businesses to enter and operate satisfactorily in the market; and
- Enable wider economic growth and regeneration.

These objectives are important when appraising and determining the appropriate operating framework for the industry and we recommend that these are included in the CMA final report and accompanying impact assessment.

¹ CMA (2015), 'Competition in passenger rail services in Great Britain', A discussion document for consultation, 17 July.

3. An assessment framework for considering any change

In the RDG response to the Department of Business, Innovation and Skills consultation on the Government's strategic steer for the CMA (14 August 2015) we set out the value for consumers and taxpayers of early impact assessments, the need to adhere to Better Regulation principles, the requirement for an evidence-based approach and the importance of strong stakeholder engagement. These are equally relevant for this CMA discussion regarding competition policy and we recommend this approach is followed for this study.

In order to determine the most appropriate model of competition for the industry, we believe that it is important to evaluate the options against one another, using a comprehensive set of assessment criteria that recognises the specific challenges of the rail industry. This will help in understanding the relative benefits and costs of the different options, and in determining the degree of benefits (and disadvantages) of changes to the current model.

The RDG considers that the options should be evaluated against industry objectives (set out in section 2) and against criteria which determine the extent to which any model of competition:

1. Meets passenger needs
2. Promotes efficiency
3. Prioritises safety
4. Can be practically implemented (including timescales and transaction costs)
5. Delivers wider economic and societal benefits for funding investment in rail

In the rail freight sector we note that the report highlights the significant benefits generated by on-rail competition, including improved staff productivity and increased private sector investment, which has kept prices down and improved service standards. Whilst the report recognises the differences between the structure of the freight and passenger rail sectors it could be beneficial to evaluate what lessons can be learned from the structure of the rail freight sector.

We believe that an assessment of the various options against these criteria should be incorporated into the impact assessment that we understand ORR is carrying out with the CMA. The RDG would welcome the opportunity to support and develop this impact assessment.

4. Options for reform in competition policy

The CMA sets out four potential options for models of competition in the industry. This response does not discuss the merits of these four options; instead this may be covered by RDG members in their individual responses, recognising the differing priorities of member organisations.

The RDG, however, has identified other options which are not included in the discussion document and which should be considered going forward:

- **Improvements in competition for the market.** The CMA notes that 'franchises have a limited ability, and muted incentives, to respond to customer preferences, because of detailed franchise specification and risk-sharing mechanisms.' This could strengthen the case for operators to have more opportunities to respond to passenger requirements through greater flexibility in franchise specifications or adjustment mechanisms in franchise agreements. This is already being progressed with the DfT and other authorities, but could potentially go further.

- **Improvements in the alignment of incentives in the charging regime and access rights process.** These are already being considered by ORR and by RDG through the Review of Charges and Review of Access Rights policy and could make a major contribution to consumer benefits.
- **Smart ticketing and further changes to fares regulation,** which currently constrains a more market based approach.
- **A continuation of the status quo** should be considered as a counter factual.

The CMA may wish to consider these options alongside those identified.

The industry has also been successful in balancing the different uses of the railway and the distinct needs of different sectors, such as commercial, Public Service Obligations (PSOs) and freight. The CMA discussion document helpfully recognises that the industry is not homogeneous, and notes the distinction between commercial rail sectors and those sectors which are related to the delivery of PSOs.

Going forward, there may need to be different approaches or arrangements for competition policy for the different sectors rather than adopting a one-size-fits-all approach. The RDG notes that the CMA recognises this when discussing the applicability of its highlighted options. In particular, while the DfT and other authorities may have a continued role in the provision of non-commercial but socially valuable services through PSO contracts, the government could have less involvement in the commercial parts of the industry. We consider that the government's role in this regard could be appraised by the CMA.

5. The success of the UK railway and industry development

Over the last few decades the rail industry has undergone a number of changes. These have been largely evolutionary and have driven significant benefits, including:

- Growth in freight and passenger traffic and revenue;
- High levels of passenger satisfaction;
- Best safety record among major railways in Europe;
- Major investment in infrastructure, stations and rolling stock;
- Reduction in cost to the taxpayer.

We have set out the wider contribution of rail to the UK economy in a report produced with Oxera² dated July 2014. Also, we direct you to the annual data set produced with KPMG³ (published summer 2013, 2014 and 2015). In addition, 'Keeping the lights on and the traffic moving'⁴ is a paper published in May 2014 that sets out the value of rail freight to the UK economy.

The current industry model has allowed for the development of some competition in the market through the entry of open access operators, at the same time the sector has faced competition from alternative modes of transport, such as air and road – rising passenger numbers and revenue are evidence of success in this regard. However, as discussed, RDG welcomes consideration of how alternative models of competition can help the industry evolve further and increase these benefits in the longer term.

² <http://www.oxera.com/Latest-Thinking/Publications/Reports/2014/What-is-the-contribution-of-rail-to-the-UK-economy.aspx>

³ http://www.raildeliverygroup.com/files/Publications/2015-09_rail_industry_dataset.pdf

⁴ http://www.raildeliverygroup.com/files/Publications/2014-05_keeping_the_lights_on.pdf

There are currently a number of potentially significant changes and reviews occurring in the industry, including: the Office of Rail and Road's (ORR) review of the structure of charges, reviews of the structure and funding of Network Rail, government's plans to direct further funding through train operators and devolution of the rail network. There are also other major developments in the industry, such as electrification and the construction of HS2.

The timing of the CMA's review therefore provides an opportunity to ensure that all of the elements of the industry are considered together to provide a consistent and aligned approach going forward. It is important that any changes occur in an appropriate order and reasonable timeframe. For example, the CMA's discussion document will help define the relevant states of the world that the charging regime, which is being considered as part of the ORR's review of charges, will need to address. Increased devolution of the specification, funding and procurement of local services also needs to be incorporated into the discussion of future models of competition to future-proof any proposed structural changes in the industry.

Additionally, we have prepared a log of potential misunderstandings or errors which our members have identified within the discussion document and will submit these separately for your review and clarification ahead of publishing your final report.

6. Conclusion and next steps

We acknowledge the goals that the CMA is seeking to achieve in its discussion document on competition in passenger rail services. There has been significant progress in the rail industry in recent years, and the CMA's contribution is helpful in considering how further advancement can be achieved. Any change to the current model of competition should be assessed against how it can help deliver the aims and objectives outlined in this response including capacity allocation, and needs to be in alignment with the other changes and reviews occurring in the industry at this time.

The RDG would welcome the opportunity to engage further with the CMA and other parties in this process, and in particular, to provide support to the impact assessment being undertaken. We would be very pleased to discuss this response and/or other points further.

For enquiries regarding this consultation response, please contact:

Jonathan Chatfield
Manager, Regulation
Rail Delivery Group

Rail Delivery Group
2nd Floor, 200 Aldersgate Street
London EC1A 4HD

Clarifications, potential errors or misunderstandings in CMA discussion document 'Competition in passenger rail services in Great Britain'

This document sets out a short list of clarifications, potential errors or misunderstandings that RDG members have identified in the CMA's discussion document. These are listed according to paragraph number in the CMA's document. The CMA may wish to explore or investigate these before issuing its conclusions and recommendations. We would be happy to discuss these further with the CMA.

- Paragraphs 1.28; 3.14-3.18. The CMA discusses planned capacity increases and enhancements, and projects for which funding has already been committed. Given the ongoing rail reviews, it is important for the CMA to consider whether the assumptions about capacity enhancements and funding are still applicable.
- Paragraph 2.52. The document suggests that competition does not begin afresh for each contract and customer; however, the CMA may want to reflect on how this does occur through the franchise bidding process.
- Paragraph 4.52 (final bullet). We believe that the Wakefield Kirkgate improvement plans were spearheaded by Groundwork Wakefield and partner funded by Network Rail, Wakefield Council, West Yorkshire Combined Authority, Railway Heritage Trust, Grand Central, Northern Rail, European Regional Development Fund, Garfield Weston Foundation and Headley Trust. Additional funding was secured from the Station Commercial Project Facility and National Stations Improvement Programme, which are administered by Network Rail.
- Paragraph 4.123. Megatrain is one example of an innovation from a franchised train operator and we believe there are other examples which the CMA may wish to include for balance.
- Paragraph 5.3. We believe that the government through the franchise agreement controls some elements of the cost of franchise operations such as the community and customer fund for non-commercial schemes; sustainability and environmental monitoring requirements; innovation fund; and the services they specify (which may not be commercial).
- Paragraph 6.4. It would be useful if the CMA could clarify what it means by a 'level playing field' in this particular context.
- Paragraph 6.30. The CMA indicates that the Capacity Charge reflects scarcity. However, the purpose of the Capacity Charge is not to reflect scarcity. Instead, it recovers Network Rail's additional performance regime costs resulting from increased traffic on the network.
- Paragraph 6.33. We believe that the Chiltern upgrade work was specified through their franchise agreement, rather than brought about by competition in the market. However, we do understand that their investment business case was based on increased revenue including increasing market share relative to competing rail operators.
- Paragraph 6.38. It is relevant to note that whilst cap and collar franchises are no longer being let, operator margins are low with profit sharing mechanisms cutting in at low levels of turnover.

- Paragraph 6.48. The reference to Schedule 8 incentivising operators ‘to plan’ their services in a way that will not disrupt others could be better phrased as incentivising operators ‘to operate’ their services in a way that will not disrupt others.
- Paragraph 6.57. It would be helpful for the CMA to clarify what is meant by the sentence that Network Rail could ‘take a more active role in managing the timetable’.
- Paragraph 6.78. We would advise caution in drawing definitive conclusions from the East Coast Main Line around significant franchise premiums, given the footnote explaining how the two franchises cited both terminated early.