Rob Plaskitt
Head of Access and Licensing
Office of Rail Regulation
One Kemble Street
LONDON
WC2B 4AN

10 April 2015

Dear Rob,

**Comments on the DfT advice paper to the ORR regarding the GNER Section 17 applications.**

**Introduction**

I should initially point out an immediate concern that the document is classed as '*DFT advice'* on the ORR website. In such a highly controversial and competitive environment to have a document produced via consultation from an affected party shown as 'advice' is not reassuring – even more so when such 'advice' contains a significant amount of unreasoned assumptions, errors, and misleading information.

The Annex provided refers to the GNER Section 18 application for access rights – when in fact GNER's applications are Section 17 applications.

This note provides comments on the letter from Claire Perry to Anna Walker and the attached Annex prepared by DfT officials and SDG. Comments are provided, in the paragraphs below, firstly on the letter itself and then on the Annex. In relation to the latter, we comment first on the train service assumptions that underpin DfT's analysis and then on the issues covered in the Annex:

- A: Financial Impact on DfT budget;
- B: Impact on IEP Business Case;
- C: Impact on future intercity rail investment;
- D: Impact on passengers and franchise services;
- E: Performance considerations;

As we have only seen a heavily redacted version of the Annex, our comments are necessarily restricted to methodology and assumptions. In order to further clarify these, it will be important to see the technical reports that provide more information.

**The DfT Letter**

Claire Perry's letter is very positive in stating that she "*firmly welcomes*" the benefits to passengers from open access. She also states that DfT's analysis does not capture "*the direct passenger benefits or the wider economic and regional benefits*" of open access (however the Annex does purport to capture passenger benefits). By asking the ORR to balance the interests of passengers, communities and taxpayers she is, in effect, inviting them **not** to give undue weight to the DfT analysis. From an open access viewpoint this is very positive. However we do not know, but can suspect, what pressure is being put on ORR by DfT officials behind the scenes.

**The Annex – Train Service Assumptions**

This section provides general comments on the train service assumptions used by the DfT in its analysis. The recent Network Rail ECML 2020 capacity timetable assessment produced in December 2014 has undermined those assumptions and gives positive opportunities for the delivery of additional services.

The timetable can accommodate 2 'fast' Edinburgh services alongside a stopping service (3 services in each hour) – and Network Rail has validated the running time proposed by GNER, albeit slightly slower at 3h 44m as opposed to GNER's 3h 43m. Flighting of services (as proposed by Network Rail) operated by different companies is no disbenefit to passengers, but does help Network Rail to make optimal use of the infrastructure.

The Annex also mentions potential loss of connectivity on a number of occasions. The use of this phrase is totally misleading, as potential loss of connectivity is not the same as potential loss in frequency, although even that is incorrect as there will be no frequency reduction in what is operational now - unless ICEC decide to amend their pattern.

However GNER proposes to improve connectivity between Stevenage and Scotland, where currently (and proposed by ICEC) no weekday northbound services exist, and between London King's Cross and Scunthorpe/Grimsby and Cleethorpes - between London King's Cross and Ilkley and a new East Leeds Parkway station. Open access has a positive history in restoring connectivity to towns and cities long overlooked by franchised operators. ICEC seems to be following the lead of National Express East Coast in just looking to serve new markets that others have developed.

In relation to the Edinburgh application, DfT has assumed that the GNER service would replace the fast ICEC train between London and Edinburgh. The latter would be diverted to serve York and Huddersfield in alternate hours. The Network Rail report has shown that there would be no requirement to replace an ICEC Edinburgh service. This threat of course enabled the DfT to then 'value' the loss of the non-operational IEP, which is commented on later.

In fact the analysis of our work (alongside the Network Rail long distance demand forecasts) shows clearly that the GNER additional services will be required to cope with the 370% Edinburgh London growth forecast (2012-2043) alongside the significant modal shift forecast from a regular 3h 44m service. The GNER application would see an additional 5.8 million seats per annum added to the route, far more than that proposed by either ICEC or First Group.

This also questions why the DfT has not sought to use the flexibility that was bought with the IEP specification to serve new markets via real PSO services such as Huddersfield/Scarborough/Cleethorpes rather than seek to compete with recently developed Grand Central commercial services at Bradford, Sunderland and Teesside (note not Hull).

The fleet deployment plans which now seem to be driving the proposed ICEC timetable fail to make effective use of the capability of the fleet of IEP trainsets procured by DfT to enable the delivery of the franchise service specification. In particular, the use of pairs of coupled 5 car IEP trainsets through to destination instead of the planned splitting of services at key nodes to enable two final destinations to be served by one path on the core ECML would seem to undermine the original business case of the inherent flexibility procured – at significant cost to the taxpayer - by DfT. This approach leads to a number of untenable outcomes:

- further inefficiency in the use of valuable capacity on the core ECML
- the proposal to operate trains which may be too long to be accommodated by the infrastructure

- the deployment of short-formed 25 year old IC225 trainsets on the key fast franchised Anglo-Scottish services.

DfT has assumed that the open access services will be operated by existing trains and will therefore not have the performance characteristics of Class 390 (Edinburgh) or IEP (Bradford/ Cleethorpes). While it is reasonable to point out any delivery risks, the DfT assumption clearly shows that they have not assessed the applications submitted by GNER. Therefore their results are fundamentally flawed.

This is particularly important in relation to the Edinburgh service, where time savings from tilt operation are essential to achieving the transfer from air forecast in the business plan. Clearly it would be possible for the ORR to specify minimum performance characteristics of the rolling stock as a condition for granting access rights to GNER.

It is also worth noting that the DfT states: "*Additional performance risks will be imported if GNER are not able to secure new rolling stock and resort to using phased out Class 225s…*" Of course we now know it is short formed, 7 car 'Phased out' 225s that is the train of choice for ICEC to deliver its flagship 'fast' Edinburgh – King's Cross service. Not only does this downgrade the service, it reduces seating capacity, and will, according to the DfT, introduce additional performance risks.

**The Annex – Financial Impact on DfT Budget**

DfT state that the Secretary of State bears 80% of the revenue loss from ICEC's inability to obtain paths for Monday to Friday key services. It is also not clear if 'key' equates to 'core' services as listed in the Annex. It is then not made clear if this 80% is gross or net revenue. If it is the former it appears to be a very poor deal as ICEC will be able to make savings in energy, maintenance, variable track access and staff costs.

In certain circumstances of course 'surplus' IEP sets could be used by other operators. Midland Main Line electrification has been approved but no announcement has been made concerning rolling stock for this route. In addition First Great Western has now indicated the requirement to replace IC125 with 7 x 9 car and 22 x 5 car Hitachi sets on the GWML. There will be no surplus IEP vehicles, and no impact on the Secretary of State's budget, whatever ICEC decide to do.

More fundamentally, DfT has created a contractual relationship with ICEC that provides a commercial incentive to resist competition. The legality of this under the Railways Act 1993 and European law needs to be investigated. From ORR's viewpoint, this creates the position that the commercial interests of ICEC and the DfT are so closely aligned that they should be considered together as just another applicant for track access rights. They are clearly not an independent agency in this matter. This then also questions the 'guidance' and 'advice' that the DfT give the ORR, which in effect seeks to provide benefits to itself.

Thirdly, the DfT's analysis is based on the use of MOIRA. As clearly set out in PDFH, this is inadequate for the assessment of open access applications. In particular, the PDFH elasticities are not valid for assessing air-rail competition and the impacts of new through services.

Fourthly, DfT argue that the reduced revenue predictability that they claim would result from competition would "*possibly [lead to] cutbacks in service quality*". All evidence from the rail, and other consumer service markets is that competition incentivises providers to improve quality of service not reduce it. It is extraordinary and perverse to assume that this case would be different, especially with such a market-focussed operator as ICEC (VTEC).

**The Annex – IEP Business Case**

The total value of the IEP contract (over 27.5 years) is £2.8bn for East Coast Phase 1 and Phase 2 (Informed Sources, Modern Railways, September 2013). This is for 497 vehicles. According to the DfT the withdrawal of one Edinburgh service (if it was necessary) would 'cost' £2.03bn (over 30 years). This would be for 54 vehicles[1], as, until the recent ICEC application was made, the expectation was that all ICEC services would be operated by IEP. No evidence is provided.

A key issue in relation to the IEP Business Case is the role of the DfT in the procurement and management of the trains. As the House of Commons Public Accounts Committee has stated, the decision to procure the train directly has put "*the financial burden and risk on the taxpayer, should the passenger forecasts be wrong and fewer trains are needed than expected*".

[1] 6 x 7 car 225 short formed sets would operate 2 hourly to Edinburgh – so it is reasonable to expect the opposite hour would require 6 x IEP sets (9 car), although no detail of the number of train sets is included in the document.

This again incentivises the DfT to resist competition from open access. However, as the procurer of the trains, DfT is in a strong position to find alternative uses for them if they are not needed on the East Coast Main Line. Unsurprisingly, this has not been considered in DfT's analysis. This inevitably creates a major bias given that there are potential uses for any surplus IEP sets elsewhere on the network as mentioned earlier.

It appears logical that DfT should welcome open access operators to the network who will provide new trains at no cost or risk to the taxpayer, allowing the DfT to deploy any surplus sets they may have purchased elsewhere, further reducing the taxpayer burden.

DfT's assessment claims that GNER's proposals depend on enabling infrastructure for IEP, which will increase capacity on ECML. There seems to be confusion here between the East Coast Connectivity project, which will increase capacity through grade separation and track layout changes, and the enabling works to permit IEP to operate. The latter works comprise:

- Gauge clearance;
- Review of station operations;
- OHLE modifications;
- Traction power supply enhancements.

The IEP enabling works only increase capacity to the extent that they allow trains with more seats and better acceleration to operate. The East Coast Connectivity project and the traction power supply upgrades provide benefits that are independent of the rolling stock used. Provided the enhanced infrastructure is used, the benefits of these investments should be realised.

The IEP specific enabling works do provide some benefit to the Bradford/ Cleethorpes service (where IEP trains are proposed), although again the benefits of public investment are being realised to meet passenger need. As IEP is not proposed for the GNER Edinburgh service, the works required to accommodate 26 metre vehicles and 10 car sets are irrelevant. Even so GNER will be investing in the infrastructure itself to accommodate its tilting trains. This very same work on the West Coast Main Line was paid for by the taxpayer.

DfT set out the results of their economic appraisal of the open access proposals in Table B.5. Without more information about the detailed appraisal assumptions and a more detailed Transport Economic Evaluation (TEE) table, it is not possible to provide detailed comments on the table. However the following observations are relevant:

- The results are highly dependent on the modelling outputs that are inputs to the appraisal. Reference is made to the IEP modelling suite, but it is not clear if this reflects the impacts of the proposed services reliably;
- The header to the table states that the appraisal period was 60 years. Further down the document says 30 years – which is it?;
- It is disappointing that DfT has found an error that has led to them increasing the cost of IEP by £169 million (in Present Value terms) since financial close. If they had not, for some unexplained reason, transferred £133 million in revenue from open access to ICEC, the BCR would have fallen further to around 5.5;
- The results are highly dependent on the invalid service assumptions made by the DfT and almost certainly do not reflect the most appropriate use for any displaced IEP sets.

**The Annex – Impact on Future Intercity Rail Investment**

Perhaps the most significant statement in the whole Annex is "*the long term impact on rail investment from allocation of an important access right to an open access operator would likely be significant*". This is very close to being a statement of opposition to open access in principle, a direct contravention of government policy.

Clearly it considers government investment only and does not recognise the high level of investment in infrastructure and UK specific trains proposed by GNER, potentially releasing IEPs for use elsewhere on the ECML or on other routes.

Implicitly it assumes that franchise premia paid by operators on commercial routes should be used to help finance subsidies for loss making lines. The result is that fares on profitable lines are higher than in a competitive market with resulting disbenefits to users. In effect, DfT is seeking to impose a monopoly and extract monopoly rents to fund other routes. This cross-subsidy is economically inefficient (as debated at great length at the time of bus deregulation). This is clearly in conflict with ORR's duty to promote competition and a major disbenefit to passengers who now fund 71% of the cost of the railways.

DfT raise the question of how maintenance would be funded. We are surprised that the DfT is not aware that this is already covered by variable track access charges. The comment is therefore irrelevant.

**The Annex – Impact on Passengers and Current Franchise Services**

DfT's arguments in this section completely ignore the benefits of competition in driving up service quality and the ability of ICEC to respond by amending its timetable to take advantage of gaps in provision. Publicly owned East Coast coped and thrived for many years with increasing open access competition on the ECML, and there is nothing to suggest that a customer focused organisation like Virgin would be unable to do likewise.

While DfT do recognise that GNER might offer lower fares, they state this would be limited by the need to fund new rolling stock. Clearly this depends on price elasticities in different market segments and available capacity. DfT's statement directly contradicts their assumption that GNER would not be able to obtain new trains.

**The Annex – Performance considerations**

The GNER service would provide over 5.8 million additional seats per year, significantly more than is proposed by ICEC on this route, and more than that proposed by combining the First Group application with the ICEC proposal.

It appears the DfT believes that it is the increasing number of operators on the route that "*would likely*" have adverse performance impacts. What they mean is of course 'non-franchised' operators who are not subject to DfT will and direction. The statement, as are many from DfT, is unfounded and provided without evidence, and is an attempted slur on the professional competence of commercial operators.

The DfT go on to state that "*if alternatives such as Class 180 or 225 with different operational and reliability characteristics are used additional risks for performance could be imported*". The only operator wishing to use Class 225 is ICEC!

Flighting of fast trains offers significant capacity and performance benefits, and this has been evidenced on the ECML since Grand Central 'squeezed in' its 1603 Bradford, between the 1600 (first stop York) and 1606 Leeds. With different operators and such a large volume of advance tickets now purchased, regular interval departures on long distance services are nowhere near as valuable as they once were.

It is also further disappointing that the DfT, without evidence or justification, always consider ‘others’ to be the problem. GNER proposes to use tried and tested Class 390 Pendolino trains on its services, whereas ICEC propose to use 25 year old 225s and untried new build Class 800/801. It is frankly ludicrous to suggest that GNER may import performance risk when it is clear that the risk lies in using old trains (which DfT has already stated) and in using untested new build. No doubt the DfT would have used the opposite argument against GNER had the rolling stock circumstances been reversed.

**Conclusions**

Unfortunately the DfT Annex is extremely hostile to the principle of open access, despite having no evidence to support its position. While, in theory, there could be some impact on the DfT’s budget and the IEP business case, DfT’s analysis is so flawed and biased that no reasonable regulator could accept it as a basis on which to make decisions.

The content and quality of the Annex raises once again the veracity of any arguments put forward by the DfT in relation to open access services and competition in general, littered as it is with inaccuracy, contradictions and lack of evidence.

Passengers fund 71% of the cost of the railway and that will increase, and yet an organisation that funds just 19% now controls, or seeks to control every aspect of the industry, with passengers merely an afterthought.

Despite all this, Claire Perry’s letter is very supportive of open access and encourages ORR to take a balanced view of its duties in determining the GNER track access applications. We would urge the ORR to support her.

Yours sincerely

Ian Yeowart

**Alliance Rail Holdings**
88 The Mount, York, YO24 1AR
Tel: 01904 628904 – email: info@alliancerail.co.uk – Website: www.alliancerail.co.uk
Registered Office: Admiral Way, Doxford International Business Park, Sunderland, SR3 3XP
Registered in England Number: 07026295

**Alliance Rail Holdings**
88 The Mount, York, YO24 1AR
Tel: 01904 628904 – email: info@alliancerail.co.uk – Website: www.alliancerail.co.uk
Registered Office: Admiral Way, Doxford International Business Park, Sunderland, SR3 3XP
Registered in England Number: 07026295