Chiltern Railways

If you think our way, travel our way.

Marylebone Station

Great Central House
Melcombe Place
London NW1 6JJ

Telephone: 0207 3333051
E-mail: graham.cross@chilternrailways.co.uk

Graham Cross
Business Development Director

John Larkinson
Office of Rail Regulation
One Kemble Street
London
WC2B 4AN

And e mailed to: draft.determination@orr.gsi.gov.uk

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Draft Determination Consultation Response from Chiltern Railways

Thank you for the opportunity to set out our response to the ORR's Draft Determination for CP5.

Chiltern Railways is a franchised passenger train operator which provides services from Marylebone station in London to Buckinghamshire, Oxfordshire, Warwickshire and the West Midlands. We have a long Franchise Term of 20 years, which runs to the end of 2021, and which was justified on the basis of our commitments to infrastructure investment and service improvement. Chiltern has to date leveraged over £600m of investment into the route, and has in several cases led the industry in devising and implementing schemes. We take 100% revenue risk so are accountable to our shareholders for the performance of both our cost and revenue base without further DfT support.

Chiltern Railways broadly welcomes the CP5 Draft Determination. We believe it strikes an acceptable balance between driving Network Rail to be more efficient, in the absence of competitive or equity pressures, and ensuring that it has sufficient funding available to enable it to deliver the reliable and quality outputs which our business model requires and which our passengers rightly expect, in the context of a growing railway.

In general we support the ATOC response but wish to make some specific points of our own, which follow.

Regulated Outputs
We do accept that it is preferable to set a relatively small number of broad brush regulated outputs for key areas, as opposed to establishing an exhaustive list of requirements which leaves management no room to manoeuvre and / or which creates contradictions. However against this:

- We were surprised to see that renewals volumes were not a regulated output despite the fact that a large proportion of the proposed settlement is based off acceptance of Network Rail's renewals volume forecast requirements. The absence of this measure seems to us to create the hazard of Network Rail spending the allowance but not actually renewing the volumes of infrastructure it is funded to renew, because it fails in the tasks of achieving the efficiency targets.
- We were surprised that asset condition is not in itself a regulated output but is relegated to be only an indicator; with the output requirement being focussed on improving records. We welcome a requirement on Network Rail to improve its asset management data and records, but we think this should be accompanied by a regulated output which requires asset condition not to fall below prescribed levels – again to add certainty that the renewals plans which underpin the pricing of the draft determination will actually be delivered
- On train service reliability we welcome the requirement to ensure that at CP5 exit no operator has PPMs below 92.5%, but want to be reassured that Network Rail will not be permitted to do this by withdrawing resources from well performing routes (such as Chiltern) as part of a process of levelling down. We welcome the suggestion that JPIPs be aligned to periodic review output targets.

System Operator

One observation from Chiltern is that PR13 seems to have been focussed on asset stewardship plus performance targets. This perhaps overlooks the fact that the policy context is for a growing railway. PR13 obviously deals with the enhancement schemes which DfT has specified in its HLOSs, many of which are major schemes to create capacity, but we are concerned that there is an absence of a framework to encourage Network Rail to get more capacity out of the existing system. We see this in access arguments on the East and West Coast main lines where Network Rail is programmed to prioritise performance results over sale of capacity.

There are many ways of creating additional capacity without embarking upon major schemes, such as:

- Reviewing sectional running times and making sure they are fully up to date to reflect the capability of modern traction types, and don't just reflect historical averages
- Challenging the existence of permanent speed restrictions, the rationale for which may be absent
- Challenging the impositions of approach control and double reds in circumstances where SPAD risk is now more effectively mitigated by TPWS
- Challenging planning headways to see if these can be improved in the light of recent infrastructure changes
- Seeking out areas where pockets of capacity can be released by making modest infrastructure changes, such as intermediate signals or easing of speed restrictions.

Our concern is that Network Rail currently lack an incentive to chase out these initiatives because the incentive signals they receive are about achieving performance targets and maintaining and renewing the asset. We would expect a world class system operator to naturally seek out these initiatives. We note the proposal for a CP5 volume incentive and have studied the 33 paragraph explanation in the Draft Determination but have not been able to reach a clear understanding on what it would mean for us. To be effective the mechanism needs to be understandable by train planners, route planners, and account managers, and not just be a theoretical mechanism understood only by experts in King's Place.

Commercial Agreements

We welcome the move to encourage Network Rail and operators to enter into commercial arrangements which will reward operators if real cost savings on schemes can be achieved. We believe that the pain / gain share mechanism included in our 101st Supplemental which enables the Bicester to Oxford upgrade is an exemplar of how this model may operate. Our experience is that usually cost savings come in the scoping stage, by stripping out scope which isn't supported by income or which won't be used by timetabled trains; rather than at the build stage. So we would suggest that to be fully effective the mechanism needs to start early on in scheme design, and not just at the construction stage.

Process for Confirming Enhancement Schemes

We recognise that it was not possible for ORR to pre-agree at this stage a list of CP5 enhancement schemes with RAB Addition allowances. Nor was it desirable to publish budgets on a scheme by scheme basis, to maintain an incentive for delivery below budget. Chiltern will participate fully with Network Rail in supporting the process in particular for the Marylebone Capacity Metric. Our one note of caution is that we need the platform lengthening schemes to be in use in mid 2015, to coincide with our rolling stock procurement plans, so would not want there to be any risk of slow to develop schemes holding up the approval of well developed schemes.

Schedules 4 and 8

At present we have secured ORR approval for a bespoke set of CP5 MRE rates which both Chiltern and NR believe will strike an appropriate incentive for CP5. As regards benchmarks we are confused as to the current picture and note that there are two different sets of NR benchmarks circulating neither of which seems to bear resemblance to the JPIP trajectories we have discussed with Network Rail. At the time of writing we are unable to understand our overall position on performance regimes for CP5 so it is hard to assess whether they are going to have the intended incentive effect. It is reasonable to expect that we will untangle these issues over the next few months but the effort needed to understand what is being proposed is something of a burden and we echo the concerns of others that this aspect of PR13 displays evidence of room for improvement.

Network Rail Cost of Capital for Investment Framework Schemes

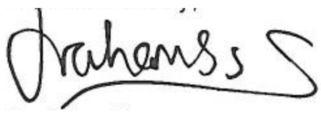
Chiltern welcomes ORR's proposal on page 429 of the Draft Determination that Network Rail be allowed a rate of return of 4.91% on Investment Framework schemes during CP5. The reduction from the current 6% will bring into viability a number of hitherto unviable investment framework candidate schemes. However we are of the view that 4.91% is still too high. We note it has been set in the light of a study of what other regulators have allowed, as opposed to by studying what borrowing rates can be achieved elsewhere. Network Rail take no risk on Investment Framework schemes so Chiltern does not believe that any risk premium should be factored into the rate of return, so we encourage ORR to determine that in fact the rate should be lower than 4.91%.

TOCs as Customer

Chiltern believes that close working between a TOC and Network Rail can deliver outcomes which would not be possible if the two remained behind their traditional contractual boundaries. We are keen therefore to open up more opportunities for working with Network Rail, many of which do not need any regulatory involvement. We are resistant to moves which leave Network Rail thinking that its true customer is ORR or DfT. Therefore we are of the opinion that the government's financial support for Network Rail should be channelled more through TOC subsidy / FTAC and less through Network Grant, to reinforce the message that TOCs and FOCs are the true customers of Network Rail.

I am happy to discuss any aspect of this response with you or your colleagues.

Yours sincerely,



Graham Cross
Business Development Director

Cc:

ORR: Alan Price

Chiltern: Rob Brighouse; Duncan Rimmer; Andrew Munden

Arriva: Steve Murphy; Roger Cobbe, Amanda Furlong

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