



OFFICE OF RAIL REGULATION



GB rail industry financial information 2013-14

February 2015

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Executive Summary

Purpose of the document

1. This fourth annual publication of GB rail industry financial information helps strengthen the industry's accountability and deepens our understanding of the rail industry's finances to improve informed debate about the value for money of the industry for its funders. It is one in a series of publications which we produce as part of our transparency programme.
2. Our analysis is primarily focused on Network Rail and franchised passenger train operators. Whilst in financial terms freight and open access operators are much smaller components of the industry they are nonetheless important in themselves and we provide a high-level analysis of their contribution in Chapter 6. While we recognise the importance of the supply chain, our analysis also does not explicitly focus on sub-components of the industry which are not directly involved in the provision of rail services such as engineering contractors, rolling stock operating companies and other financial institutions. Our analysis also largely excludes investment in the Crossrail construction project because this does not yet form part of the operational railway¹.
3. The overlapping geographical boundaries of the rail industry make analysis of whole industry financial information at a sub-GB level complex. As explained in Chapter 6 (Methodology) we have made some changes to the way in which we analyse infrastructure costs between different geographies in this year's publication. We have restated our previously published industry analysis on a consistent basis and this is available on our website². Whilst we consider that the methods and data sources that we have employed provide a reasonable and informative analysis of the industry's finances at a sub-GB level we recognise that different approaches could be used which would give a different interpretation of, for example, where government is providing financial support. There are different views within the industry and it is important for readers to recognise this. **For this reason we suggest that care should be taken in interpreting those parts of our analysis that examine costs, income and government support at a sub-GB level.**
4. This report is the result of a continuing collaborative effort by a number of organisations. We are particularly grateful to Network Rail, franchised train operating companies, the Rail Delivery Group (RDG), the Department for Transport (DfT), Transport Scotland, the Welsh Government, Transport for London and Merseytravel without their support this publication would not have been possible.

¹ Information about investment in the Crossrail construction project is available at <http://www.crossrail.co.uk>.

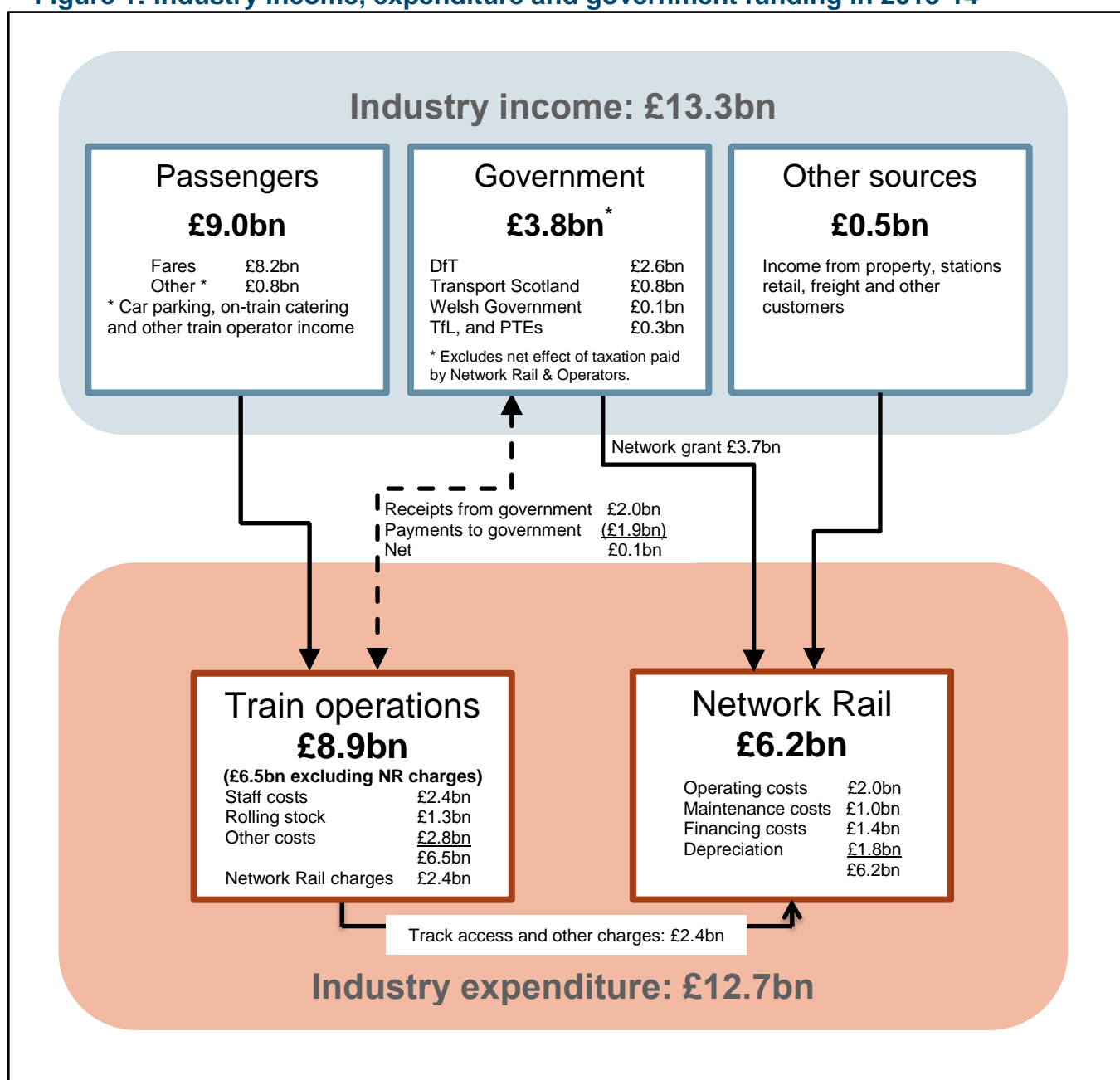
² <http://orr.gov.uk/publications/reports/gb-rail-industry-financial-information/gb-rail-industry-financial-information-2013-14>

Summary of our findings

Overall observations

5. Figure 1 below illustrates the rail industry's major sources of income and expenditure including government funding for the year 1 April 2013 to 31 March 2014 (2013-14). A presentation of the income and expenditure showing Network Rail's expenditure on a cash-basis is included in Table 3.5.

Figure 1: Industry income, expenditure and government funding in 2013-14



6. The cost of running Great Britain's railways was £12.7bn, a real terms increase of 0.7% from 2012-13³. Around half of these costs were incurred in train operations and half were incurred in managing the rail infrastructure. Our analysis suggests that the increase is both due to the industry adding capacity in response to growing passenger journey numbers and costs incurred by Network Rail associated with shortfalls in performance against its regulatory outputs. Adjusted for growth in passenger journeys, industry expenditure decreased by 2.5% in real terms from 2012-13.
7. Train operators and Network Rail recognised £3.8bn of income from government sources, a real terms decrease of 8.1% compared to 2012-13. Our analysis suggests that there were significant variations in the level of funding between England, Scotland and Wales with total government funding varying from £1.88 per passenger journey in England to £7.77 per journey in Scotland and £9.18 per journey in Wales⁴. Similarly the level of funding provided by government varied from 24% of total industry income in England to 61% in Scotland and 55% in Wales.
8. Passenger income was £8.2bn which equates to an average fare of £5.14 per passenger journey. Passenger income increased in real terms by 3.5% compared to 2012-13 which is largely due to the 5.7% increase in passenger journeys. As shown in Figure 2.3, around 64% of this income was from unregulated fares and 36% from regulated fares⁵.

Changes in industry finances since 2010-11

9. As summarised in Table 1 and Figure 2, our analysis shows that there have been substantial changes to the rail industry's finances over the four years from our first GB rail industry financials publication in 2010-11. Adjusted for inflation, our analysis shows that:
 - funding from government sources decreased by 16.4%. This equates to a 28.3% decrease in government's financial contribution per passenger journey;
 - passenger income increased by 10.8%. This was largely due to the 16.6% increase in passenger journeys with the average fare per passenger journey decreasing by 5.0%; and

³ The November RPI uplift is used throughout our analysis to adjust for the effect of inflation. The retail price index (RPI) increased by 2.6% from November 2012 to November 2013.

⁴ Government funding for infrastructure is allocated to Network Rail at the national level. Our sub-GB level analysis requires allocating industry income and costs to overlapping and misaligned geographies of franchises and operating routes. There is no definitive way to do this and different stakeholders have different views as to how this should be done. This means that care is required in understanding and interpreting our analysis because different approaches can give different allocations.

⁵ Though note that some unregulated fares are effectively capped by the price of regulated fares for the same journey type. As explained in Chapter 6 (Methodology), there are limitations to our fares analysis due to it not capturing all tickets for each origin destination flow.

- industry costs were unchanged. There was also substantial investment in the network with Network Rail spending £9.2bn on enhancement schemes including Reading Station Improvements, Edinburgh- Glasgow Improvement Plan and Thameslink. Crossrail, which is expected to be operational in 2018, is another important enhancement and investment in HS2 will become increasingly significant over the next few years.

Table 1: Industry income, government funding and expenditure

(£m except where stated)	Variance to 2013-14 ^a			
	2013-14	2012-13	2011-12	2010-11
Industry income				
Passenger fare income ^d	8,160	3.5%	7.2%	10.8%
Other income (incl. intra-industry)	3,733	10.9%	17.4%	14.6%
Less: intra-industry income ^b	-2,410	17.3%	31.5%	26.4%
	9,483	3.1%	5.9%	8.8%
Government funding	3,788	-8.1%	-12.0%	-16.4%
Industry expenditure				
Train operating expenditure (incl. intra-industry)	8,889	4.5%	7.2%	6.1%
Infrastructure expenditure	6,199	0.9%	3.3%	-3.6%
Less: intra-industry expenditure ^b	-2,410	17.3%	31.5%	13.2%
	12,678	0.7%	1.8%	0.0%
Surplus / (deficit) ^c	593	-18.3%	-26.1%	3.6%
Passenger income per passenger journey	£5.14	-2.1%	-1.4%	-5.0%
Passenger income per pass. km travelled	£0.14	0.2%	1.9%	0.5%
Government funding per pass. journey	£2.39	-13.0%	-19.1%	-28.3%
Industry expenditure per passenger journey	£7.99	-4.7%	-6.4%	-14.2%

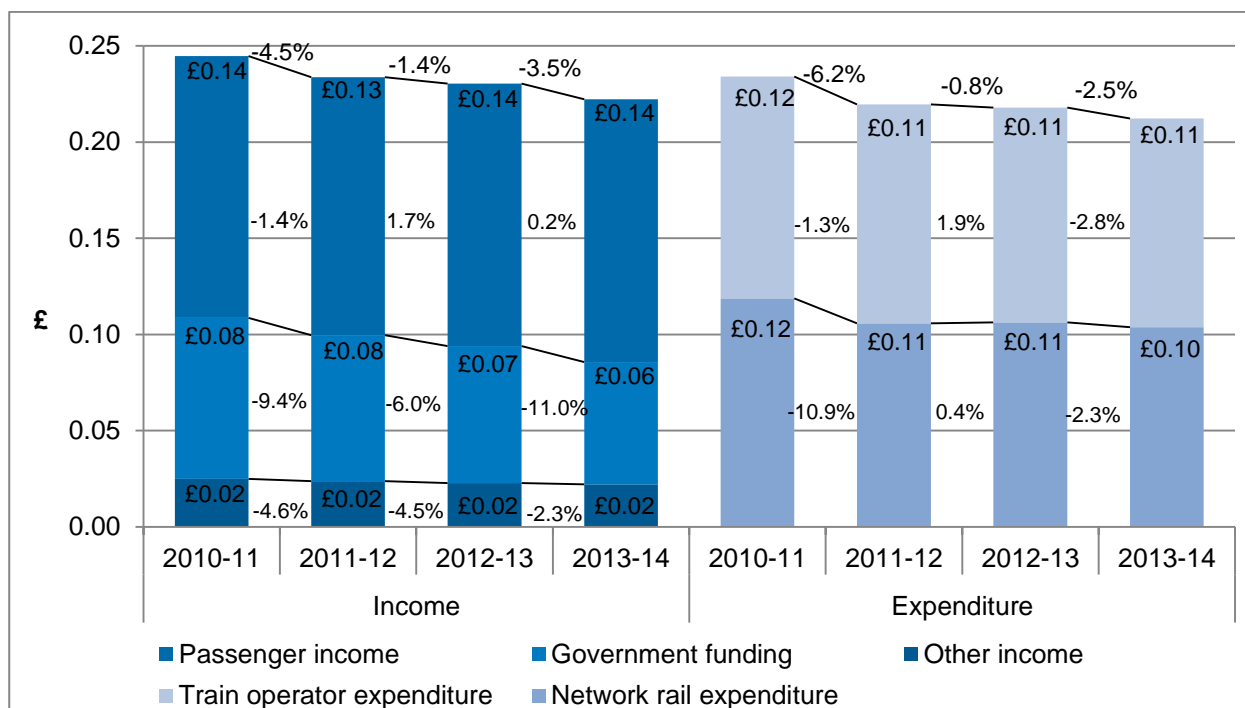
^a Adjusted for RPI inflation. Some 2011-12 and 2010-11 financial information has also been restated from information published in previous versions of this publication as we now have better information on the base costs of some operators.⁷

^b Track access and other charges paid by franchised train operating companies to Network Rail.

^c As explained in Chapter 6 (Methodology) this is not an accounting profit in a statutory reporting sense due to statutory financial reporting adjustments for the treatment of deferred tax, pension schemes, derivative fair values, dividends etc.

^d As explained in Chapter 6 (Methodology) train operator management accounts are used as the source for this figure, whereas the Rail Usage Statistics published figure uses LENNON data.

Figure 2: Industry income government funding and expenditure per passenger kilometre between 2010-11 and 2013-14



^a Excluding intra-industry income and expenditure.

Structure of this report

10. Our objectives for this work are explained in Chapter 1 (Introduction). Our key findings are explained in Chapter 2 (Key Findings) with more detailed financial information and analysis for the GB rail industry as a whole, and separately for England, Scotland and Wales in Chapter 3. This information is then presented for each of Network Rail’s ten regional operating routes in Chapter 4 and for each of the 19 franchised train operators in Chapter 5. The methodology underpinning our analysis is explained in Chapter 6. Supporting information is included as an annex to the report. Our analysis is also available in Excel format at our website⁶.

⁶ <http://orr.gov.uk/publications/reports/gb-rail-industry-financial-information/gb-rail-industry-financial-information-2013-14>

1. Introduction

Purpose of the report

- 1.1 Increasing transparency about the rail industry's finances should help to strengthen the industry's accountability and improve informed debate about the value for money of the industry for its funders, both passengers and governments. In its Rail 2020 report⁷, the Transport Select Committee fully endorsed this need for more transparency about the rail industry's finances. The UK Government and Scottish Government are also of the view that providing better information on public services will help to increase the usefulness of those services.
- 1.2 The complex structure of the British rail industry makes it difficult for stakeholders to understand the income, expenditure and government funding of the industry as a whole and we consider that transparency has a vital role to play in driving the behavioural changes necessary for rail industry reform.
- 1.3 The information presented within this report should:
 - (i) help passengers understand what they are paying for;
 - (ii) clarify where government, in its different forms, is providing support;
 - (iii) show interested parties to gain a better understanding of industry financial performance;
 - (iv) improve industry planning and co-operation;
 - (v) support increased route level and train operator accountability; and
 - (vi) provide better benchmarking data of costs and efficiencies.
- 1.4 Our industry financials publications provide a more comprehensive understanding of industry income and expenditure than has recently been available. They are the result of a collaborative effort by a number of organisations. We are particularly grateful to franchised train operating companies, Network Rail, the Rail Delivery Group (RDG), the Department for Transport (DfT), Transport Scotland, the Welsh Government, Transport for London (TfL) and Merseytravel⁸ without whose support this work would not have been possible.

⁷ This is available at <http://www.parliament.uk/business/committees/committees-a-z/commons-select/transport-committee/inquiries/parliament-2010/rail-2020/>.

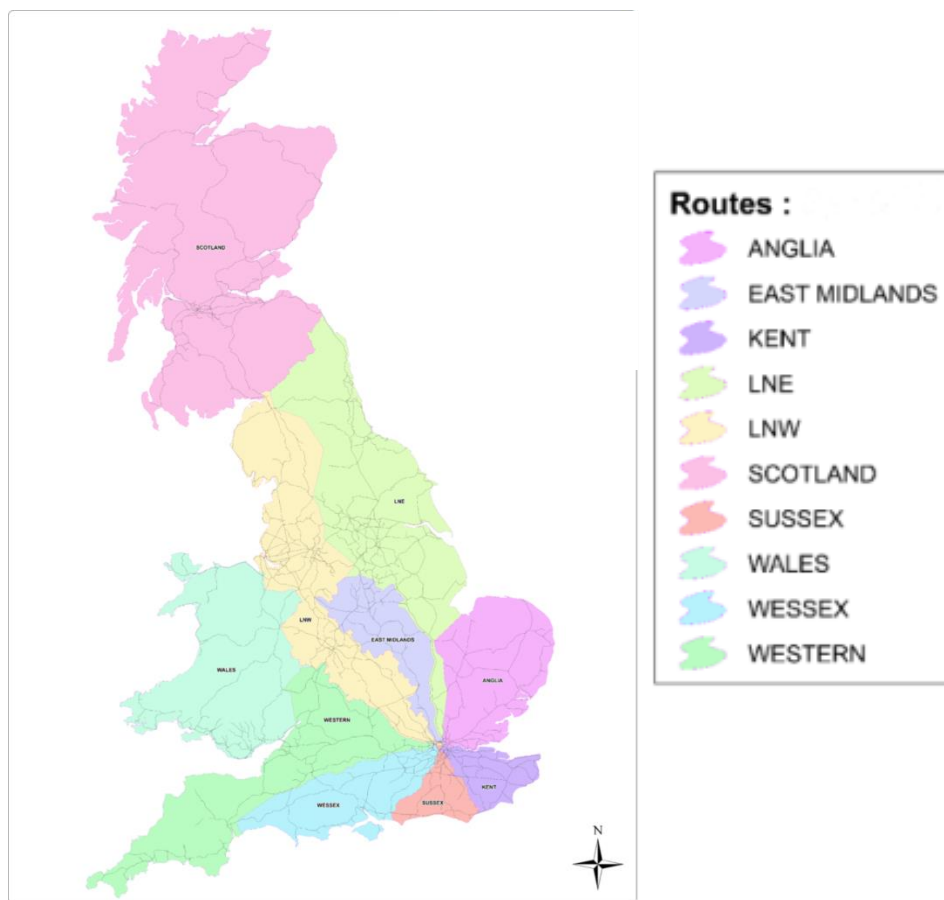
⁸ Merseytravel is the Merseyside passenger transport executive.

Industry structure and rationale for our analytical approach

- 1.5 The GB rail industry comprises the national rail infrastructure provider, Network Rail, franchised train operators which provide passenger services on the rail infrastructure, other freight and open access operators and the supply chain (rolling stock leasing companies, engineering contractors and other suppliers). The primary focus of our analysis is Network Rail and the franchised train operating companies.
- 1.6 Network Rail has ten regional operating routes whose geographies are shown in Figure 1.1. The operating routes are:
- Anglia
 - East Midland
 - Kent
 - London North East (LNE)
 - London North West (LNW)
 - Scotland
 - Sussex
 - Wessex
 - Western
 - Wales
- 1.7 Network Rail is a not-for-dividend company which uses its profits to reinvest in the industry or pay down debt⁹.

⁹ Network Rail was re-classified by the Office for National Statistics (ONS) as a public sector body in the national accounts on 1 September 2014 following a change to the European System of Accounts. The ONS's decision is largely a statistical matter and DfT has confirmed that ORR will remain the economic and safety regulator for the railway and the ONS's decision will have no effect on rail fares, performance, punctuality, timetables, or safety. Further information about the ONS decision is available at http://www.ons.gov.uk/ons/dcp171766_345415.pdf.

Figure 1.1: Geographical coverage of Network Rail’s ten regional operating routes

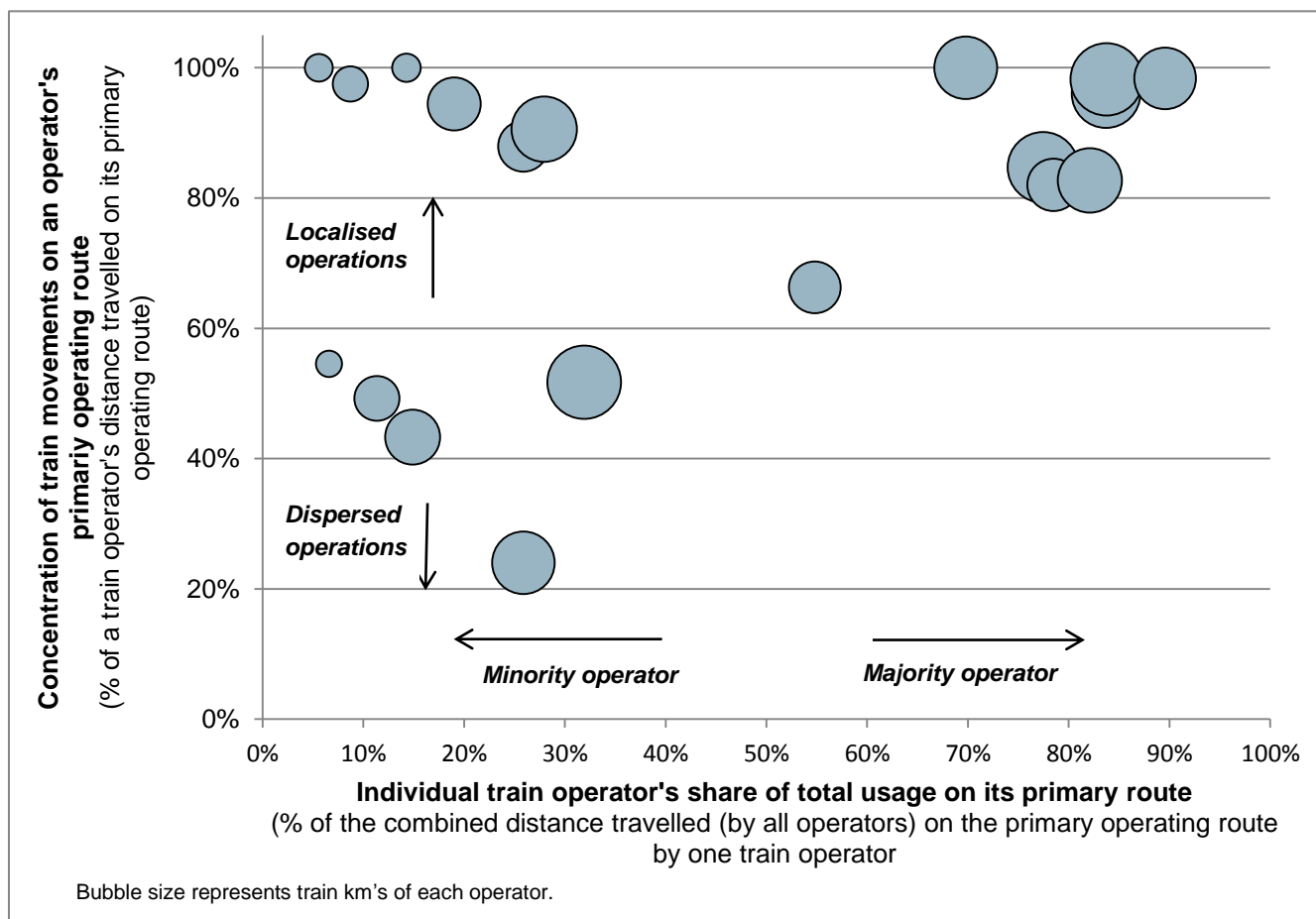


Source: Network Rail.

- 1.8 There are currently 19 train operators which operate passenger services under franchise from government. DfT is the franchising authority for the majority of England & Wales franchises (16). Transport Scotland, TfL and Merseytravel are the franchising authorities for the ScotRail, London Overground and Merseyrail franchises respectively.
- 1.9 As shown in Figure 1.2, there are significant overlaps between the geographies of rail franchises and also between the geographies of rail franchises and regional operating routes. For example, five franchises make use of the central spine of the west coast mainline (West Coast, West Midlands, London Overground, ScotRail and Southern)¹⁰.
- 1.10 Taken together with the different sources of government funding, this structure significantly complicates understanding of the rail industry’s finances at a sub-GB level. Further details are available in Annex A which shows the distance travelled by each train operator in each regional operating route in 2013-14.

¹⁰ As another example, of the six train operators which each travelled in excess of 2.5 million train kilometres on the London North East operating route (Cross Country, East Coast Mainline, East Midlands, Northern Rail, Transpennine Express and First Capital Connect) only one (East Coast Mainline) did not travel at least this distance on at least one other operating route.

Figure 1.2: Alignment and overlap of rail franchise geographies and operating routes



Source: ORR analysis.

1.11 For these reasons there is not one best way to present rail industry financial information at a sub-GB level. For example, geographical disaggregation by operating route is arguably more useful for understanding regional variances in the costs of managing the physical infrastructure, whereas disaggregation by train operators is arguably more useful for understanding variances in passenger income. Using a mixture of both is perhaps most useful for understanding some items such as government funding.

1.12 In order to best achieve our objectives for this work we consider that it is most informative to present financial information separately at a national, regional and train operator (passenger service) level within this report.

1.13 Our analysis is primarily focused on Network Rail and franchised passenger operators' income and expenditure. However we recognise that whilst in financial terms freight and open access operators are smaller components of the industry than franchised passenger services, they are nonetheless important components of the rail industry value chain and we provide an analysis of their financial contribution in Chapter 6 (Methodology). Our analysis does not explicitly focus on components of the rail industry which are not directly involved in the provision of rail services, in particular engineering

contractors, rolling stock leasing companies and other financial institutions. Whilst the supply chain is important it is not directly involved in the provision of railway services to customers. Our analysis also excludes the Crossrail and HS2 construction projects because these do not yet form part of the operational railway¹¹.

- 1.14 We have not attempted to analyse industry income and expenditure at a greater level of granularity, for example for individual train or passenger journeys. This would require a significant increase in the amount of data and analysis required, and its value would be questionable as many items of income and expenditure cannot accurately be attributed beneath the level at which costs are actually managed. However, we do provide analysis of average 'unit costs', for example, regional variances in industry costs per passenger journey.
- 1.15 The report does not make any comment on the value for money of the industry for taxpayers or passengers. However the affordability of rail and other regulated services are considered in a recent United Kingdom Regulators Network (UKRN) publication, 'Understanding affordability pressures in essential services'¹².

Structure of the report

- 1.16 Chapter 2 provides a summary of our key findings. Chapter 3 summarises rail industry financial information for Great Britain as a whole, and separately for England, Scotland and Wales. Chapter 4 summarises this information for each of the ten regional operating routes and Chapter 5 summarises this information for each of the 19 train operators. The methodology underpinning our analysis is explained in Chapter 6.
- 1.17 As previously noted, our analysis is also available in Excel format on our website¹³.
- 1.18 Annex A summarises the distance travelled by train operators in each regional operating route in 2013-14 and Annex B shows the contribution of government funding to Network Rail and Train Operators as a proportion of industry income analysed by operator in 2013-14.

¹¹ Information about investment in the Crossrail construction project is available at <http://www.crossrail.co.uk/about-us/funding#>.

¹² <http://www.ukrn.org.uk/wp-content/uploads/2015/01/UKRN-Affordability-Report.pdf>

¹³ <http://orr.gov.uk/publications/reports/gb-rail-industry-financial-information/gb-rail-industry-financial-information-2013-14>

Care required in understanding and interpreting our analysis

- 1.19 For the reasons explained above a significant challenge in developing and presenting our analysis is how to allocate financial information to the overlapping and misaligned geographies of franchises and operating routes.
- 1.20 Partly in response to stakeholder feedback on our 2012-13 publication we have made some changes to the way in which we analyse and allocate infrastructure costs between different geographies in this year's publication. The methodology underpinning our analysis and the changes that we made this year are explained in Chapter 6. We have also restated our previously published analysis on a consistent basis.
- 1.21 We consider that the methods and data sources that we have employed provide a reasonable and informative analysis of the industry's finances. However, at the sub-GB level we recognise that different approaches could be used to allocate infrastructure costs which would give a different interpretation of, for example, where government is providing financial support. Differing views exist across the industry on how these costs should be allocated and our approach is not supported by all stakeholders. Therefore it is important that these parts of the analysis are placed in their proper context and not given undue weight within the overall messages of this report. For this reason we suggest that care is taken in interpreting those parts of our analysis that examine costs, income and government support at a sub-GB level.
- 1.22 As explained in Chapter 6 (Methodology) we have revised aspects of how Network Rail's expenditure is allocated to franchises in this year's analysis and we have restated our analysis for previous years on a consistent basis.
- 1.23 There might be some differences in numbers in the tables in this report due to rounding.

Feedback

- 1.24 We welcome comments on the content of this document. These should be sent to:

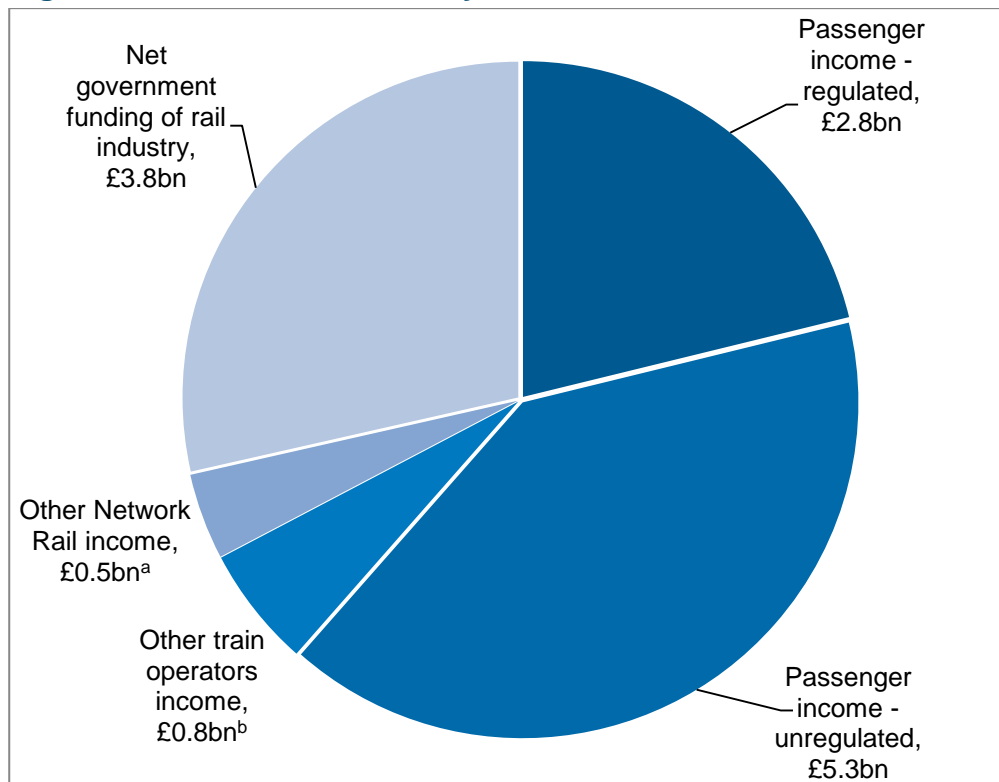
Customer correspondence team
Office of Rail Regulation
One Kemble Street
London
WC2B 4AN
Email: contact.cct@orr.gsi.gov.uk
Tel: 020 7282 2018

2. Key Findings

Industry income

2.1 The rail industry received £13.3bn of income in 2013-14. As shown in Figure 2.1, the majority of this income was from passenger fares (£8.2bn, 61%). Different parts of government contributed a total of £3.8bn (29%). Train operators received £0.8bn from car parking, on-board catering and other sources and Network Rail received £0.5bn from property, stations retail, freight and other customers.

Figure 2.1: Sources of industry income in 2013-14



^a Income from station retail outlets, property sales, freight and open access operators etc.

^b Income from car parking, on train catering etc.

Passenger income

- 2.2 Passenger income represents ticket income from passenger journeys, as opposed to non-ticket industry income such as catering and car parking¹⁴. Passenger income was £8.2bn in 2013-14 which was £0.5bn (6.2%) higher than in 2012-13. Adjusted for inflation, passenger income was £0.3bn (3.5%) higher than in 2012-13.
- 2.3 The increase in passenger income compared to 2012-13 needs to be considered in the light of the passenger growth. The number of passenger journeys increased in 2013-14 by 5.7%, although this varied significantly across the country (7.2% for operators predominantly serving London and the South East, 2.8% for regional operators and 1.1% for long distance 'Intercity' operators) and average journey distance decreased by 2.3%.
- 2.4 The average passenger income per journey (average fare) in 2013-14 was £5.14¹⁵ and the average income per passenger kilometre travelled was £0.14. Adjusted for inflation, the average passenger income per journey in 2013-14 decreased by 2.1% and the average passenger income per passenger kilometre travelled increased by 0.2%. These figures represent the change in the average revenue raised not changes in specific types of fare. Our analysis shows that the decreases in average passenger income per journey and average income per passenger kilometre appears to be the result of the majority of the passenger growth arising from shorter journeys in London and the South East.
- 2.5 Per passenger journey, average passenger income was highest in Wales (£5.79) followed by England (£5.17) and Scotland (£4.43). Per passenger kilometre travelled, average passenger income was highest in England (£0.14) followed by Wales (£0.12) and Scotland (£0.10).
- 2.6 On a passenger km basis, there was a high variability of passenger income between train operators, which is perhaps not surprising considering the different nature of the passenger services provided by the 19 franchises, covering both longer distance intercity, short distance commuter and rural services. London Overground received the highest passenger income per passenger kilometre travelled (£0.18 per passenger kilometre) and Merseyrail the lowest (£0.07 per passenger kilometre travelled). These differences will largely reflect pricing in different passenger markets, the differences in journey lengths (e.g. under current fares policy the price per km tends to be greater on shorter journeys than longer journeys) and the provision of government subsidy in areas where fare revenue and other industry income is lower but there are wider socio-economic benefits from the provision of rail services in that area.

¹⁴ Within the industry, passenger income is commonly known as farebox income.

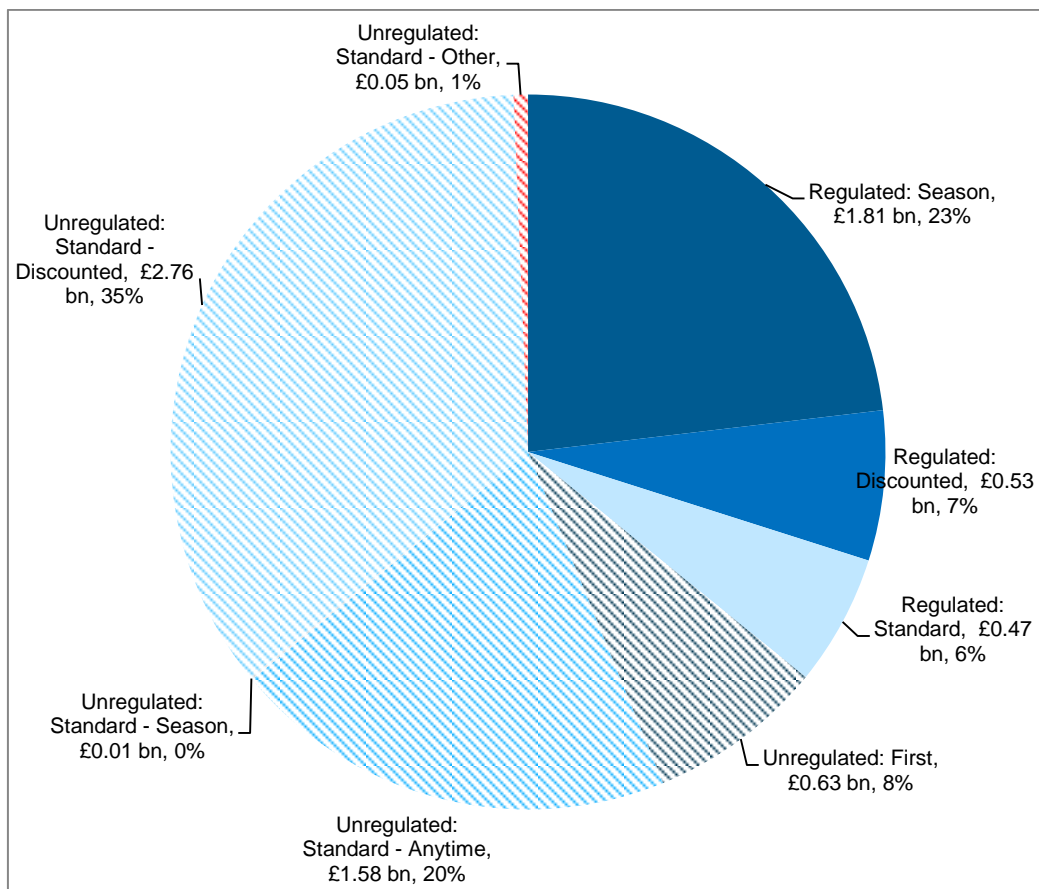
¹⁵ Calculated by dividing total passenger income by the total number of passenger journeys.

Contribution of different fare types to passenger income

- 2.7 Governments determine which fares are regulated through the specification of franchise agreements with train operators. In general fares regulation is considered necessary around major commuter cities where there are limited alternatives to rail travel. Fares regulation also applies outside urban areas, to some weekly season tickets, long-distance off-peak return fares and shorter distance standard return fares.
- 2.8 As shown in Figure 2.2 the majority (64%) of passenger income came from passengers using unregulated fares and the remainder (36%) from regulated fares. Our analysis also showed that 48% of all journeys were covered by unregulated fares. The greater contribution of unregulated fares to total passenger income is mostly due to the greater use of unregulated fares for standard on-the-day or advance purchase long-distance journeys (therefore higher than the average per journey cost of a regulated commuter season ticket)¹⁶.
- 2.9 During 2014, the largest share of passenger income came from unregulated discounted fares (35%), followed by regulated season fares (23%), unregulated standard anytime fares (20%) and first class travel (8%).

¹⁶ Some unregulated fares are effectively capped by the price of alternative regulated fares and as a result, the proportion of revenue which is effectively regulated, as opposed to directly regulated, will be higher than 36%.

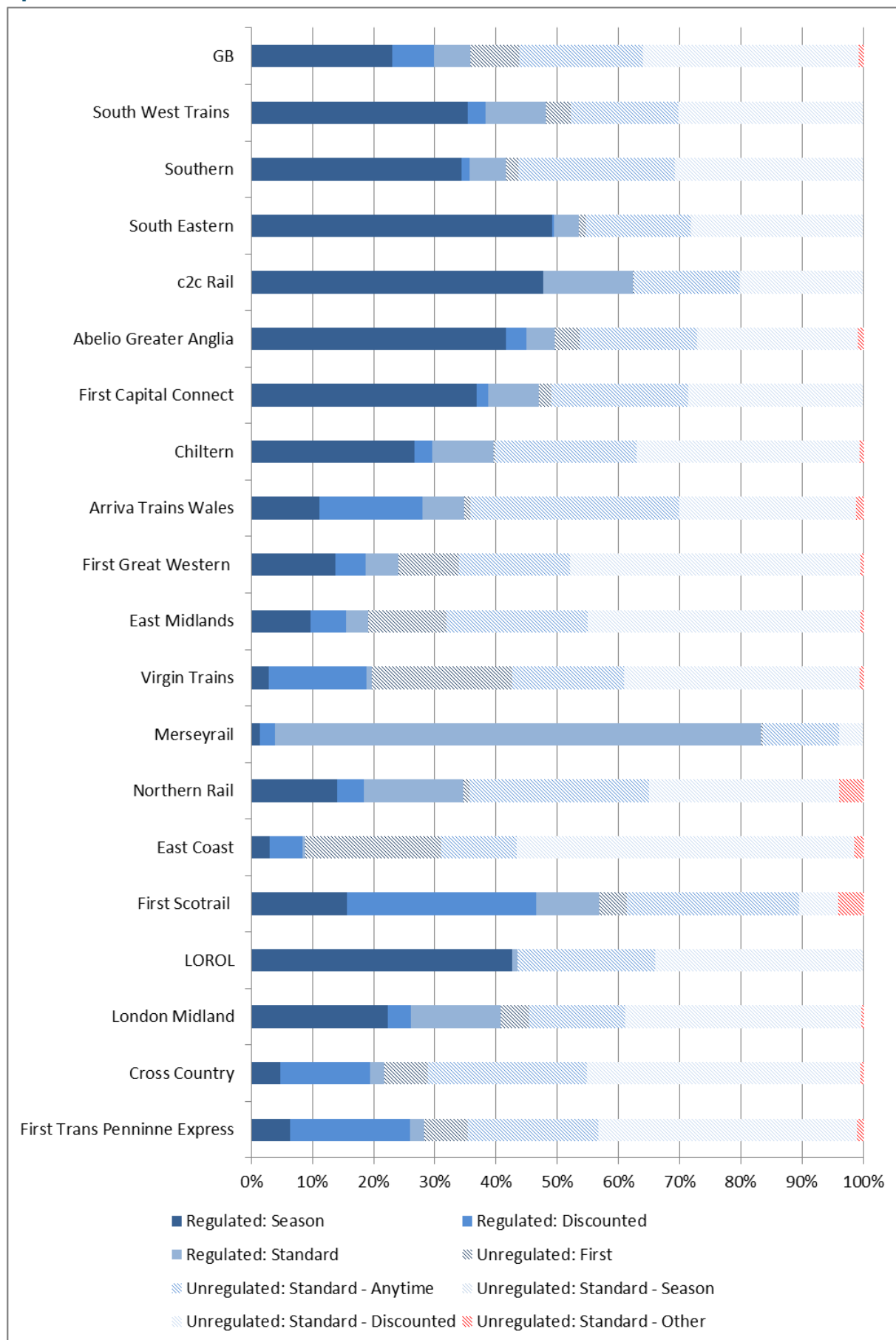
Figure 2.2: Contribution of regulated & unregulated fares to passenger income in 2014¹⁷



2.10 As shown in Figure 2.3 there are significant variances between the contributions from different ticket types to train operators' revenues, which reflects the different markets in which they operate. For example, regulated standard season tickets typically contribute around 30% of the revenues of train operators serving commuters in London and the South East, whereas for long distance operators they account for less than 10% of revenues. Likewise, unregulated discounted tickets make a greater contribution to the income of operators on long-distance routes.

¹⁷ We used the LENNON passenger income database to calculate the relative contribution of different fare types and applied this to train operators' total passenger income. As explained in Chapter 6 (Methodology), the LENNON data was for the calendar year 2014 and does not include all tickets for every origin destination flow. However we consider that our approach provides a reasonable estimate of the contribution of different fare types to overall passenger income.

Figure 2.3: Contribution of regulated & unregulated fares to passenger income by operator in 2014



Other industry income

2.11 The rail industry received £1.3bn of income in 2013-14 from sources other than passenger income and government funding, an increase of 0.9% in real terms from 2012-13. The increase is predominantly due to additional income raised by train operators. Train operators received £0.8bn from car parking, property rental, catering and other sales. Network Rail received £0.5bn from its stations and property portfolio, and charges to freight and open access train operators.

Government funding

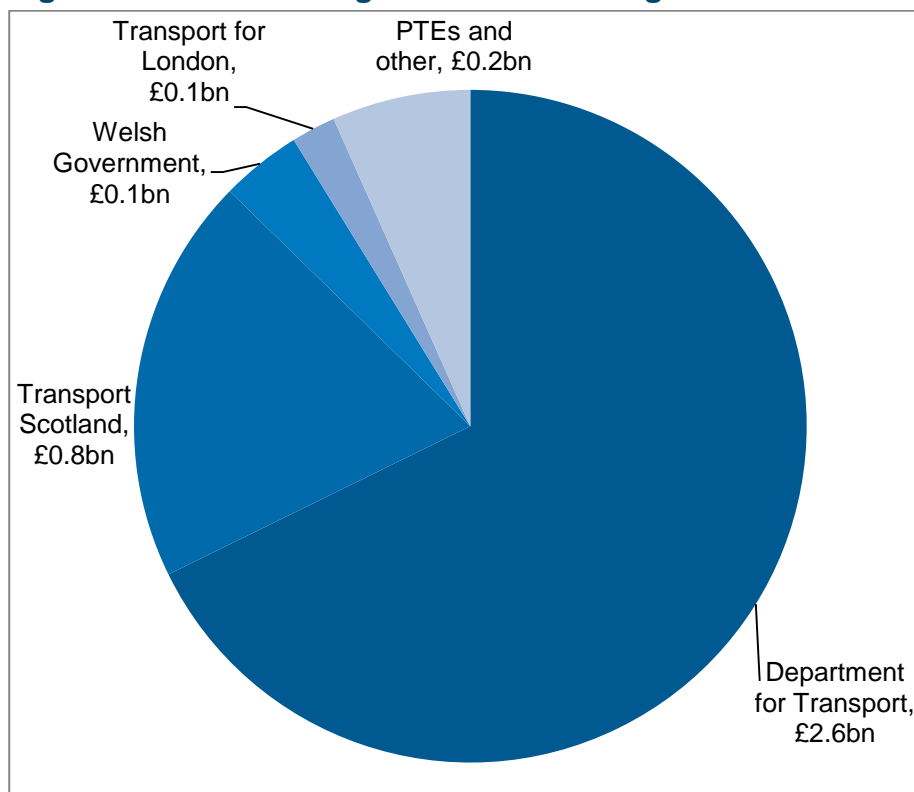
2.12 Industry income from government sources was £3.8bn¹⁸ in 2013-14, representing 28.5% of the industry's total income¹⁹.

2.13 The contributions from the various sources of government funding of the rail industry are shown in Figure 2.4. Whilst the Department for Transport was the largest single contributor (69%), other parts of government, most notably Transport Scotland and the Welsh Government, made regionally significant contributions.

¹⁸ Excludes taxation paid by Network Rail and Train Operators.

¹⁹ Our analysis primarily uses financial information from industry sources. Note that there are differences between the amount of franchise receipts and payments reported as income / expenditure by train operators and the amounts reported by government. Therefore, the figures quoted in this report may differ from ORR's Rail Finance Statistical Release. These differences are primarily due to differences in the timing of recognition of income (as required by accounting standards) and how funding from some passenger transport executive's funding has been reported. These differences are shown in Table 4.2.

Figure 2.4: Sources of government funding in 2013-14



2.14 Government as a whole contributed £3.7bn to Network Rail and made a net contribution of £0.1bn to train operators. However, there were significant regional variations which are examined below. In real terms, total government funding to the industry reduced by 8.1% compared to 2012-13 and by 12.0% compared to 2011-12.

2.15 Network Rail receives network grant from DfT and Transport Scotland in lieu of fixed track access charges that it would otherwise receive from franchised train operators. Therefore understanding changes to government funding, whether of Network Rail or of train operators needs to take into account the policy choices that governments have made about where industry funding is allocated. This means that movements in government funding to Network Rail or train operators in isolation cannot be used to draw conclusions about the efficiency of that part of the industry.

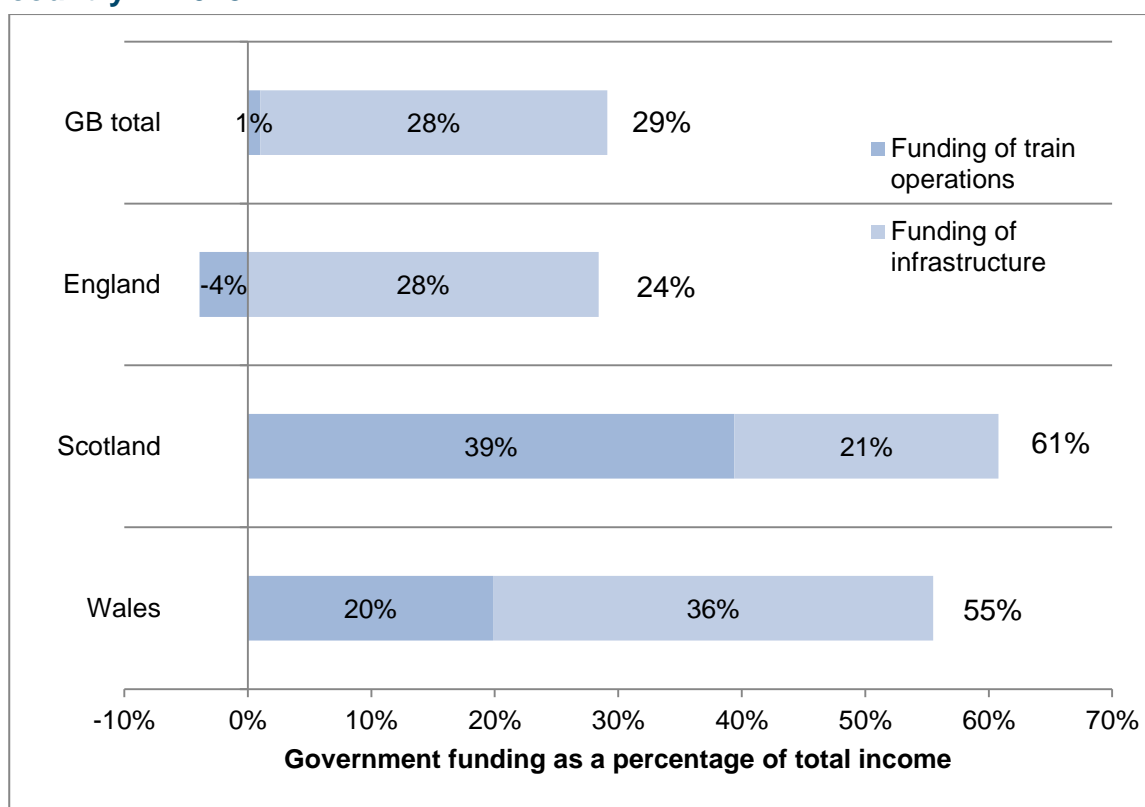
2.16 In real terms, since 2010-11 net government funding of Network Rail decreased by 10.7%, by 12.7% from 2011-12 and by 10.7% from 2012-13. This funding was set out in ORR's 2008 Periodic Review of Network Rail's revenue requirement for the funding period 2009-2014 (PR08)²⁰ and it has declined largely as a result of the efficiency savings that ORR challenged Network Rail to deliver over this period.

²⁰ <http://orr.gov.uk/what-and-how-we-regulate/regulation-of-network-rail/how-we-regulate-network-rail/previous-control-period/periodic-review-2008>.

2.17 Government's net £0.1bn contribution to train operators included £2.0bn of payments to some train operators, which were nearly offset by £1.9bn of receipts from other train operators. Our analysis shows that this net funding of train operators increased by £0.1bn from 2012-13.

2.18 Our analysis suggests that there are significant variations in the level of government funding between England, Scotland and Wales. However, due to the overlapping and misaligned geographies of franchises and operating routes there are different ways in which government funding can be allocated to different geographies and therefore care is required in understanding and interpreting our analysis. Government funding varied from £1.88 per passenger journey in England to £7.77 per passenger journey in Scotland and £9.18 per passenger journey in Wales. As a proportion of total industry income, England had the lowest level of government funding at 24%, compared to 55% for Wales and 61% for Scotland.

Figure 2.5: The contribution of government funding to total industry income by country in 2013-14



2.19 Annex B shows total government funding to Network Rail and train operators as a percentage of total industry income across rail franchises. Using the infrastructure cost allocation method explained in Chapter 6 (Methodology) our analysis suggests that passengers on regional franchises were the greatest beneficiaries of government funding with passengers on intensively used London commuter and intercity franchises receiving substantially less support. Our analysis suggests that the income from

passengers (and other customers) of two franchises, East Coast and South West Trains, is sufficient to cover the costs of the relevant train and network operations.

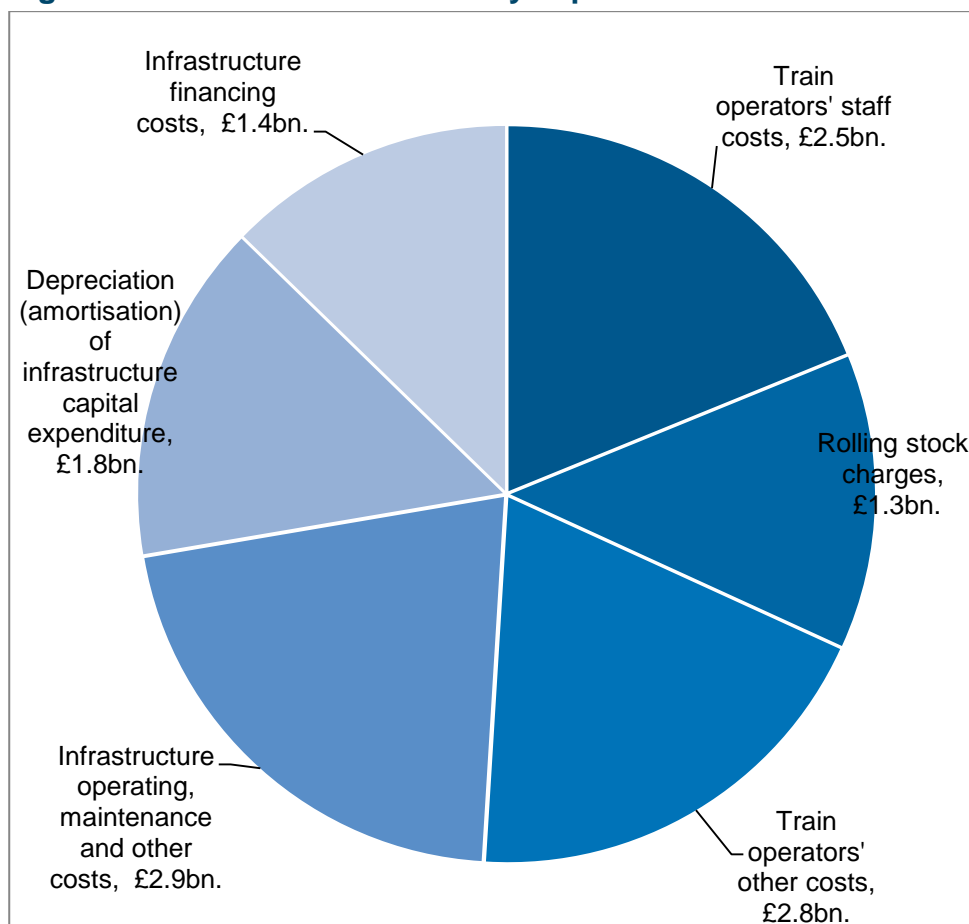
2.20 The regional differences in government funding largely reflect the fact that the rail network has a largely fixed cost base whereas there are significant differences in regional passenger markets. For example, on rural franchises there is lower and more dispersed demand and greater competition for passengers from other modes of transport. In comparison there is greater underlying demand and rail is often the only viable transport option for many commuter routes.

2.21 Importantly, for these reasons the level of government funding received cannot be used as an indicator of the financial effectiveness of any individual train operator.

Industry expenditure

2.22 Total industry expenditure in 2013-14 was £12.7bn of which £6.5bn (51%) was incurred in train operations and £6.2bn (49%) was incurred in operating rail infrastructure, excluding intra-industry charges.

Figure 2.6: Breakdown of industry expenditure in 2013-14



^a Fuel, train maintenance costs etc.

^b Includes traction electricity.

Train operators' expenditure

- 2.23 Train operators' expenditure excluding Network Rail charges was £6.5bn in 2013-14, a real terms increase of 0.4% compared to 2012-13. Taking account of inflation and passenger growth (i.e. the total distance travelled by passengers), train operators' costs decreased by 2.8% compared to 2012-13.
- 2.24 Average train operator expenditure was £0.11 per passenger kilometre travelled. Using this measure, train operators' expenditure was highest in Wales (£0.15 per passenger kilometre), followed by Scotland (£0.14 per passenger kilometre) and England (£0.10 per passenger kilometre). These variances are likely to reflect different levels of passenger usage (i.e. the average number of passengers on a train). Average train densities were 125 passengers per train in England, compared to 78 in Scotland and 67 in Wales.
- 2.25 Average train operator expenditure was £12.75 per train kilometre travelled. Using this measure England had the highest average train operator costs (£13.13 per train kilometre), followed by Scotland (£10.92 per train kilometre) and Wales (£10.07 per train kilometre). These variances will likely reflect the different lengths of trains (trains in England have, on average, more carriages per train), and also the type of trains that are in use (England has a higher proportion of higher cost rolling stock, for example, Pendolino trains).
- 2.26 There are significant variances in train operating costs between franchises. There will be many reasons for these variances including the nature of the franchise specifications, such as local geography and demographics which drives rail demand, as well as other drivers of costs which are more controllable by train operators such as staff salaries. There are also other costs which are only partially controllable by train operators, for example, rolling stock leasing costs where train operators have only limited choice about what trains they can operate²¹. In addition rolling stock lease arrangements can vary significantly between operators, for example if train maintenance is included, so called wet leases. This report does not seek to investigate or explain the reasons for the differences in train operating costs across franchises. For the reasons stated above care is required in interpreting our analysis in this area and the information provided cannot be used to draw conclusions about the comparative financial performance of individual operators. However, this is clearly an important subject and by providing more transparent information about train operators' costs we hope to inform the public debate about the value for money of the rail industry as a whole.

²¹ For example, rolling stock charges paid by Virgin Trains were £119m and those paid by East Coast were £46m. A key driver for this variance is likely to be the costs associated with the type and age of rolling stock used by these operators. The Virgin fleet mostly comprises Class 390 Pendolinos with an average age of ten years. East Coast's fleet mostly comprises InterCity 225s with an average age of 28 years (source: ORR Data Portal).

2.27 Train operators paid £2.4bn in track access and other charges to Network Rail, an increase of 17.3% compared to 2012-13. This increase is mostly due to increased fixed track access charges as set out in PR08.

Infrastructure expenditure (Network Rail)

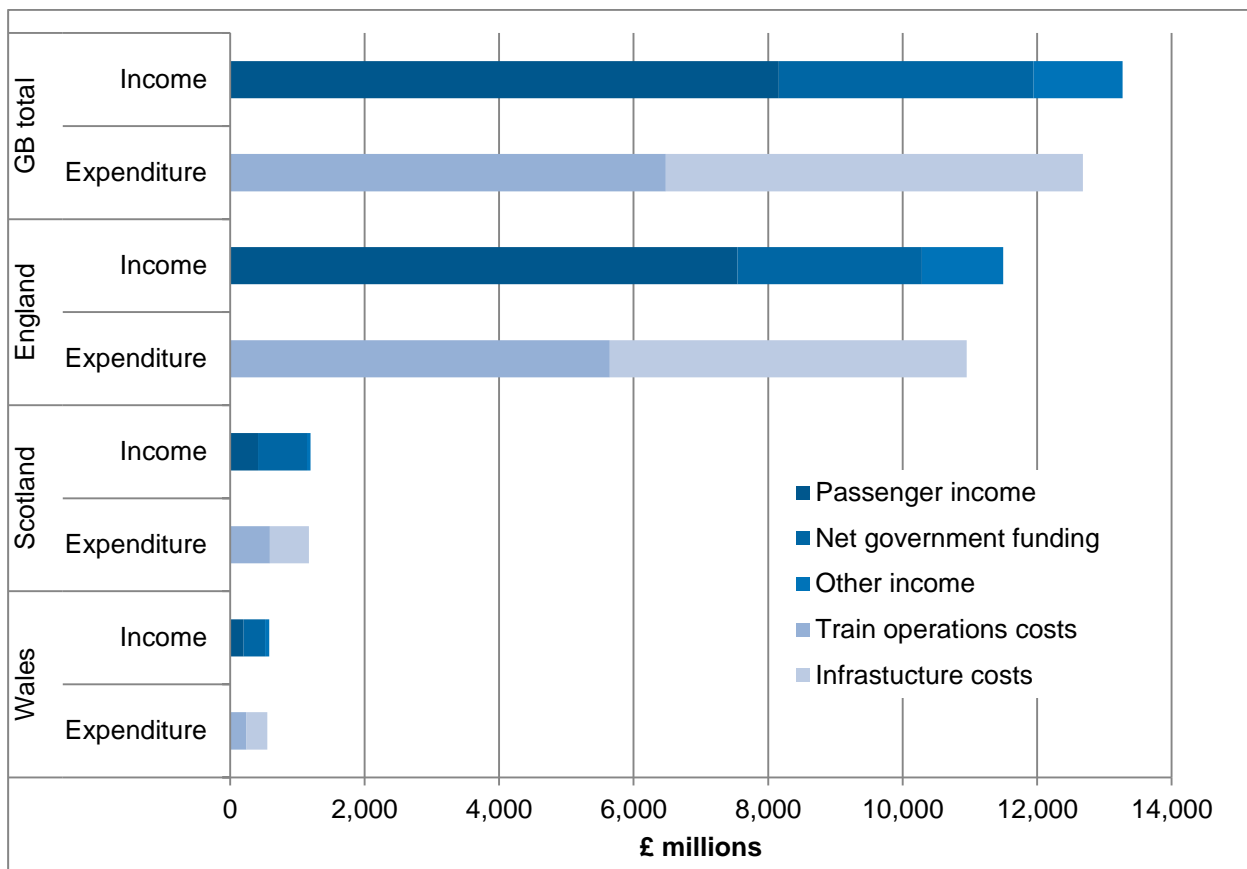
2.28 Expenditure on rail infrastructure was £6.2bn in 2013-14, a real terms increase of 0.9% compared to 2012-13²². The increase is largely due to costs of reorganisation, a financial penalty for missed regulatory outputs and increased compensation payments to train operators for missing network performance requirements.

2.29 Network Rail average expenditure was £0.20m per track kilometre. Using this measure, Network Rail's expenditure was highest in England (£0.22m per track kilometre) followed by Scotland (£0.14m per track kilometre) and Wales (£0.13m per track kilometre).

2.30 Network Rail spent £6.7bn on capital projects (renewals and enhancements to the network) in 2013-14. This expenditure was £4.9bn greater than the £1.8bn of amortisation of capital expenditure that ORR included in its PR08 determination and has been included as capex amortisation / depreciation in our industry costs analysis. This difference represents additional investment and was funded by Network Rail borrowing.

²² Our analysis includes £15m of infrastructure expenditure by TfL on the core East London Line. For convenience, we generally only refer to Network Rail in this analysis.

Figure 2.7: Comparison of income and expenditure for GB, England, Scotland and Wales in 2013-14



3. GB rail industry financial information disaggregated by country

- 3.1 GB rail industry financial information for 2013-14 is presented in this chapter, together with separate analysis for England, Scotland and Wales.
- 3.2 Our analysis shows that the cost of running the railway in 2013-14 was £12.7bn of which the majority (£11.0bn) was incurred in England, followed by £1.2bn in Scotland and £0.5bn in Wales. Government provided £3.7bn of funding. Passenger income was £8.1bn and other income (car parking, stations and property income etc.) was £1.3bn.

Table 3.1	Summary of industry income, expenditure and government funding in 2013-14
Table 3.2	Industry income in 2013-14
Table 3.3	Industry expenditure in 2013-14
Table 3.4	Government funding of the rail industry in 2013-14
Table 3.4a	Sources of government funding
Table 3.5	Industry income, expenditure and government funding in 2013-14 using a cash-based approach for Network Rail's capital expenditure ²³
Table 3.6	High level analysis of industry financial information in 2013-14

²³ The approach adopted in Table 3.5 shows in cash terms Network Rail spending on renewals and enhancements to the rail network during the year rather than the fixed asset depreciated expense shown in Table 3.1.

Table 3.1: Summary of industry income, expenditure and government funding in 2013-14

£m	GB total	England	Scotland	Wales
Industry income^a				
Passenger income	8,160	7,543	415	201
Other income	3,733	3,108	467	159
Less: intra-industry income ^b	-2,410	-1,898	-412	-99
	9,483	8,752	469	261
Industry expenditure^a				
Franchised train operators expenditure	8,889	7,542	1,002	345
Rail infrastructure expenditure	6,199	5,306	584	309
Less: intra-industry expenditure ^b	-2,410	-1,898	-412	-99
	12,678	10,950	1,173	555
Income less expenditure	-3,195	-2,197	-704	-294
Government funding^a	3,788	2,741	728	320
Surplus / (deficit)^c	593	544	24	26

^a Tables 3.2, 3.3 and 3.4 provide more detailed information about industry income, expenditure and government funding.

^b Track access and other charges paid by franchised train operating companies to Network Rail.

^c As explained in Chapter 6 (Methodology) this is not an accounting profit in a statutory reporting sense due to statutory financial reporting adjustments for the treatment of deferred tax, pension schemes, derivative fair values, dividends etc .

Table 3.2: Industry income in 2013-14

£m	GB total	England	Scotland	Wales
Franchised train operators				
Passenger income	8,160	7,543	415	201
Other	772	687	39	47
	8,932	8,230	454	248
Network Rail income				
Fixed charges	1,464	1,062	322	80
Variable charges	626	571	43	12
Other	871	788	63	20
	2,961	2,421	428	112
Less: Network Rail income from franchised train operators (per NR)	-2,410	-1,898	-412	-99
Total industry income	9,483	8,752	469	261

Table 3.3: Industry expenditure in 2013-14

£m	GB total	England	Scotland	Wales
Franchised train operators				
Staff costs	2,453	2,109	235	108
Fuel costs – diesel	313	253	38	22
Fuel costs – traction electricity (paid to NR)	277	258	18	1
Rolling stock charges	1,269	1,091	132	46
Network Rail charges	2,134	1,641	395	99
Other operating expenditure	2,385	2,141	179	66
Interest & exceptional expenditure/income ^a	-4	-4	0	-1
Corporation tax	64	53	6	5
	8,889	7,542	1,002	345
Infrastructure				
Controllable operating costs	1,071	914	98	59
Non-controllable operating costs ^b	546	479	54	13
Maintenance ^c	967	833	84	50
Amortisation of capital expenditure	1,828	1,513	218	97
Financing costs	1,428	1,228	121	79
Corporation tax	-5	-5	0	0
Other	364	344	9	11
	6,199	5,306	584	309
Less: Network Rail income from franchised train operators (per NR)	-2,410	-1,898	-412	-99
Total industry expenditure	12,678	10,950	1,173	555

^a Represents interest receivable.

^b Includes traction electricity, business rates.

^c This includes £15m that TfL spent on maintaining the East London Line (ELL), which is part of the London Overground network.

Table 3.4: Government funding of the rail industry in 2013-14

£m	GB total	England	Scotland	Wales
Franchised train operators (source: train operators)^a				
Franchise payments to government	-1,905	-1,836	-38	-32
Franchise receipts from government	1,127	494	502	131
Profit sharing/other revenue support	735	711	7	17
Total excluding PTE funding	-43	-631	472	116
Passenger Transport Executive (PTE) funding	178	178	0	0
	135	-453	472	116
Franchised train operators (source: government excluding PTEs)^a				
Franchise payments to government	-1,231	-1,192	-32	-7
Franchise receipts from government	1,191	572	491	128
	-40	-621	460	121
Infrastructure (Network Rail)				
Government grants	3,780	3,283	288	209
Rebates to government	-142	-104	-32	-6
TfL (East London Line)	15	15	0	0
	3,653	3,194	256	203
Net government funding (source: train operators + Network Rail accounts)^a	3,788	2,741	728	320
Net government funding (source: government + Network Rail accounts)^a	3,613	2,574	716	324

Table 3.4a: Sources of government funding

Sources of government funding	Total	Train operators	Network Rail
£m			
Department for Transport	2,613	-769	3,382
Transport Scotland	762	506	256
Welsh Government	152	152	0
Transport for London	83	68	15
Passenger Transport Executives ^b	178	178	0
	3,788	135	3,653

^a The franchise payments/receipts to train operators per government is available on the ORR data portal <http://dataportal.orr.gov.uk/displayreport/report/html/0913a84d-b740-4111-b6f8-bf6470e2d7b7>. There are differences in the amount of Government funding recognised in train operators' and government financial statements. We understand that this is largely due to the income recognition criteria set out in accounting standards which require train operators to match receipts from government in the period in which the relevant expenditure occurs in their income statements. Therefore, the timing of the recognition of this income in train operators' financial statements will not necessarily match the expenditure shown in government's financial statements.

^b This comprises Passenger Transport Executive (PTE) funding of Northern Rail.

Table 3.5: Industry income, expenditure and government funding in 2013-14 using a cash-based approach for Network Rail's capital expenditure²⁴

£m	GB total	England	Scotland	Wales
Industry income				
Passenger income	8,160	7,543	415	201
Other income	3,733	3,108	467	159
Less: intra-industry income	-2,410	-1,898	-412	-99
	9,483	8,752	469	261
Industry expenditure				
Train operators	8,889	7,542	1,002	345
Network Rail non-capex expenditure	4,371	3,794	366	212
Network Rail capex - renewals	3,701	3,153	337	211
Network Rail capex - enhancements	2,962	2,655	261	46
Less: intra-industry expenditure	-2,410	-1,898	-412	-99
	17,513	15,245	1,553	714
Income less expenditure (cash basis)	-8,030	-6,493	-1,084	-453
Government funding	3,788	2,741	728	320
Income less expenditure including net government funding (cash basis)	-4,242	-3,752	-356	-134

²⁴ This approach shows the actual amount of money that Network Rail spent during the year. Table 3.1 presents the information consistent with the accruals-based accounting approach recognising the cost of an asset over its useful life. Therefore table 3.1 includes within infrastructure costs the amortisation of capital expenditure whereas table 3.5 includes Network Rail capex – renewals and enhancements on a cash basis.

Table 3.6: Analysis of industry financial information in 2013-14

	GB total	England	Scotland	Wales
Government funding				
Share of government funding (%)	n/a	72.4%	19.2%	8.4%
Government funding / total income (%)	28.5%	23.8%	60.8%	55.0%
Government funding per passenger journey (£)	2.39	1.88	7.77	9.18
Government funding per passenger km travelled (£)	0.06	0.05	0.17	0.19
Passenger income				
Passenger income / total income (%)	61.5%	65.6%	34.7%	34.7%
Passenger income per passenger journey (£)	5.14	5.17	4.43	5.79
Passenger income per passenger km travelled (£)	0.14	0.14	0.10	0.12
Industry expenditure				
Industry expenditure per train km travelled (£)	24.95	25.48	21.73	22.75
Industry expenditure per passenger km travelled (£)	0.21	0.20	0.28	0.34
Train operator expenditure per passenger km travelled (£)	0.11	0.10	0.14	0.15
Network Rail expenditure per train km travelled (£)	12.20	12.35	10.82	12.68
Network Rail expenditure per passenger km travelled (£)	0.10	0.10	0.14	0.19
Train operator share of total costs (%)	51.1%	51.5%	50.2%	44.3%
Income / expenditure				
Passenger income / industry expenditure (%)	64.4%	68.9%	35.4%	36.3%
Income (excl. gov funding) less expenditure per passenger journey (£)	-2.01	-1.51	-7.51	-8.44
Income (excl. gov funding) less expenditure per passenger km (£)	-0.05	-0.04	-0.17	-0.18

4. GB rail industry financial information disaggregated by operating route

- 4.1 Our analysis of rail industry financial information for 2013-14 is presented separately for each of Network Rail's ten regional operating routes in this chapter.
- 4.2 Our analysis shows that there are significant variations in industry income, expenditure and government funding across the ten regional operating routes. These variations are summarised in the Executive Summary.

Table 4.1	Summary of industry income, expenditure and government funding in 2013-14 by regional operating route
Table 4.2	Industry income in 2013-14 by regional operating route
Table 4.3	Industry expenditure in 2013-14 by regional operating route
Table 4.4	Government funding of the rail industry in 2013-14 by regional operating route
Table 4.5	Industry income, expenditure and government funding in 2013-14 using a cash-based approach for Network Rail's capital expenditure by regional operating route ²⁵
Table 4.6	High level analysis of industry financial information in 2013-14

²⁵ The approach adopted in Table 4.5 shows the amount of money that Network Rail spent on renewals and enhancements to the rail network during the year rather than the fixed asset depreciated expense shown in Table 4.1

Table 4.1: Summary of industry income, expenditure and government funding in 2013-14 by regional operating route

£m	Operating route										Total
	Anglia	Kent ^c	London North East	London North West	East Midlands	Sussex	Wessex	Western	Wales	Scotland	
Industry income^a											
Passenger income	975	783	1,143	1,715	466	722	969	771	201	415	8,160
Other income	336	295	588	718	235	278	322	334	159	467	3,733
Less: intra-industry income	-191	-188	-370	-525	-75	-143	-211	-195	-99	-412	-2,410
	1,120	890	1,362	1,908	626	858	1,079	909	261	469	9,483
Industry expenditure^a											
Train operators	807	842	1,384	2,075	263	632	768	771	345	1,002	8,889
Infrastructure	573	478	1,049	1,413	325	396	522	550	309	584	6,199
Less: intra-industry expenditure	-191	-188	-370	-525	-75	-143	-211	-195	-99	-412	-2,410
	1,189	1,132	2,063	2,963	513	885	1,079	1,126	555	1,173	12,678
Income less expenditure	-68	-242	-702	-1,055	113	-28	1	-216	-294	-704	-3,195
Government funding^a	143	322	535	1,194	208	59	-15	295	320	728	3,788
Surplus^b	75	79	-167	139	321	32	-14	79	26	24	593

^a Tables 4.2, 4.3 and 4.4 provide more detailed information about income, expenditure and government funding.

^b As explained in Chapter 6 (Methodology) this is not an accounting profit in a statutory reporting sense due to statutory financial reporting adjustments for the treatment of deferred tax, pension schemes, derivative fair values, dividends etc .

^c Some of Southeastern's services in Kent make use of High Speed 1 rail infrastructure, the cost of which is excluded from our analysis. Therefore care is required in comparing Kent to other operating routes.

Table 4.2: Industry income in 2013-14 by regional operating route

£m	Operating route										Total
	Anglia	Kent ^a	London North East	London North West	East Midlands	Sussex	Wessex	Western	Wales	Scotland	
Franchised train operators											
Passenger income	975	783	1,143	1,715	466	722	969	771	201	415	8,160
Other	55	57	125	169	49	82	77	71	47	39	772
	1,030	840	1,268	1,884	515	805	1,046	842	248	454	8,932
Infrastructure (Network Rail)											
Fixed charges	102	94	257	215	113	72	89	120	80	322	1,464
Variable charges	69	56	84	156	41	57	60	48	12	43	626
Other	110	88	122	178	32	67	96	95	20	63	871
	281	238	463	549	186	196	245	263	112	428	2,961
Less: income from train operators	-191	-188	-370	-525	-75	-143	-211	-195	-99	-412	-2,410
Total industry income	1,120	890	1,362	1,908	626	858	1,079	909	261	469	9,483

^a Some of Southeastern's services in Kent make use of High Speed 1 rail infrastructure, the cost of which is excluded from our analysis. Therefore care is required in comparing Kent to other operating routes.

Table 4.3: Industry expenditure in 2013-14 by regional operating route

£m	Operating route										Total
	Anglia	Kent ^a	London North East	London North West	East Midlands	Sussex	Wessex	Western	Wales	Scotland	
Franchised train operators											
Staff costs	219	194	397	545	68	197	243	247	108	235	2,453
Fuel costs – diesel	9	0	67	78	21	1	15	62	22	38	313
Fuel costs – traction electricity (paid to NR)	41	37	38	62	5	34	39	1	1	18	277
Rolling stock charges	185	111	180	279	37	92	109	98	46	132	1,269
Network Rail charges	150	150	332	463	70	109	173	194	99	395	2,134
Other operating expenditure	202	345	348	640	58	193	189	166	66	179	2,385
Interest and exceptional expenditure / (income)	0	3	3	-3	1	0	-7	0	-1	0	-4
Corporation tax	2	0	20	12	3	7	6	3	5	6	64
	807	842	1,384	2,075	263	632	768	771	345	1,002	8,889
Infrastructure (Network Rail)											
Controllable opex	103	78	180	259	52	75	83	84	59	98	1,071
Non controllable opex	68	53	80	126	18	49	62	23	13	54	546
Maintenance ^b	119	68	138	243	52	48	80	85	50	84	967
Amortisation of capital expenditure	145	142	323	399	93	101	142	166	97	218	1,828
Financing costs	118	115	262	324	76	82	115	135	79	121	1,428
Corporation tax	-1	0	-1	-1	0	0	-1	0	0	0	-5
Other	20	22	67	63	34	41	40	57	11	9	364
	573	478	1,049	1,413	325	396	522	550	309	584	6,199
Less: Network Rail income from franchised train operators (per NR)	-191	-188	-370	-525	-75	-143	-211	-195	-99	-412	-2,410
Total industry expenditure	1,189	1,132	2,063	2,963	513	885	1,079	1,126	555	1,173	12,678

^a Some of Southeastern's services in Kent make use of High Speed 1 rail infrastructure, the cost of which is excluded from our analysis. Therefore care is required in comparing Kent to other operating routes.

^b This includes £15m that TfL spent on maintaining the East London Line (ELL).

Table 4.4: Government funding of the rail industry in 2013-14 by regional operating route

£m	Operating route										Total
	Anglia	Kent ^b	London North East	London North West	East Midlands	Sussex	Wessex	Western	Wales	Scotland	
Franchised train operators (source: train operators)^a											
Franchise payments to government	-227	-26	-413	-132	-105	-174	-486	-274	-32	-38	-1,905
Franchise receipts from government	33	4	133	301	1	16	1	4	131	502	1,127
Profit sharing / other revenue support	47	77	113	28	78	13	175	179	17	7	735
Total excluding PTE funding	-146	55	-166	198	-26	-144	-310	-91	116	472	-43
PTE funding	0	0	93	84	1	0	0	0	0	0	178
	-146	55	-73	281	-25	-144	-310	-91	116	472	135
Franchised train operators (source: government excluding PTEs)^a											
Franchise payments to government	-179	-18	-296	-99	-36	-172	-325	-66	-7	-32	-1,231
Franchise receipts from government	16	98	131	300	5	8	2	12	128	491	1,191
	-163	79	-166	201	-31	-164	-323	-54	121	460	-40
Network Rail											
Government grant to NR	286	275	628	941	237	212	307	397	209	288	3,780
Less: Network Rail rebates to Government	-12	-9	-20	-28	-4	-9	-11	-11	-6	-32	-142
TfL East London Line	15	0	0	0	0	0	0	0	0	0	15
	290	266	608	913	233	203	296	386	203	256	3,653
Net government funding (source: train operators + NR accounts)^a	143	322	535	1,194	208	59	15	295	320	728	3,788
Net government funding (source: government + NR accounts)^a	127	346	442	1,114	202	39	-28	332	324	716	3,613

^a The franchise payments/receipts to train operators per government is available on the ORR data portal <http://dataportal.orr.gov.uk/displayreport/report/html/0913a84d-b740-4111-b6f8-bf6470e2d7b7>. There are differences in the amount of Government funding recognised in train operators' and government financial statements. We understand that this is largely due to the income recognition criteria set out in accounting standards which require train operators to match receipts from government in the period in which the relevant expenditure occurs in their income statements. Therefore, the timing of the recognition of this income in train operators' financial statements will not necessarily match the expenditure shown in government's financial statements.

^b Some of Southeastern's services in Kent make use of High Speed 1 rail infrastructure, the cost of which is excluded from our analysis. Therefore care is required in comparing Kent to other operating routes.

Table 4.5: Industry income and expenditure in 2013-14 using a cash-based approach for Network Rail's capital expenditure by regional operating route

£m	Operating route										Total
	Anglia	Kent ^a	London North East	London North West	East Midlands	Sussex	Wessex	Western	Wales	Scotland	
Industry income											
Passenger income	975	783	1,143	1,715	466	722	969	771	201	415	8,160
Other income	336	295	588	718	235	278	322	334	159	467	3,733
Less: intra-industry income	-191	-188	-370	-525	-75	-143	-211	-195	-99	-412	-2,410
	1,120	890	1,362	1,908	626	858	1,079	909	261	469	9,483
Industry expenditure											
Train operators expenditure	807	842	1,384	2,075	263	632	768	771	345	1,002	8,889
Network Rail non-capex expenditure	428	336	726	1,014	232	295	380	384	212	366	4,371
Network Rail capex - renewals	275	261	607	883	193	222	314	398	211	337	3,701
Network Rail capex - enhancements	159	485	420	481	163	181	114	652	46	261	2,962
Less: intra-industry expenditure	-191	-188	-370	-525	-75	-143	-211	-195	-99	-412	-2,410
	1,478	1,736	2,767	3,928	776	1,187	1,364	2,009	714	1,553	17,513
Income less expenditure (cash basis)	-357	-846	-1,406	-2,020	-150	-329	-285	-1,100	-453	-1,084	-8,030
Government funding	143	322	535	1,194	208	59	-15	295	320	728	3,788
Surplus / (deficit) (cash basis)	-214	-524	-871	-826	58	-270	-299	-805	-134	-356	-4,242

^a Some of Southeastern's services in Kent make use of High Speed 1 rail infrastructure, the cost of which is excluded from our analysis. Therefore care is required in comparing Kent to other operating routes.

Table 4.6: Analysis of industry financial information in 2013-14

	Operating route										Total
	Anglia	Kent ^a	London North East	London North West	East Midlands	Sussex	Wessex	Western	Wales	Scotland	
Government funding											
Share of government funding (%)	3.8%	8.5%	14.1%	31.5%	5.5%	1.6%	-0.4%	7.8%	8.4%	19.2%	100%
Gov. funding / total income (%)	11.3%	26.6%	28.2%	38.5%	25.0%	6.4%	-1.4%	24.5%	55.0%	60.8%	28.5%
Gov. funding per pass. journey (£)	0.57	1.60	3.24	4.65	6.02	0.29	-0.06	3.02	9.18	7.77	2.39
Gov. funding per pass. km (£)	0.02	0.07	0.05	0.09	0.11	0.01	0.00	0.05	0.19	0.17	0.06
Passenger income											
Pass. income per pass. journey (£)	3.87	3.88	6.93	6.68	13.46	3.49	3.97	7.90	5.79	4.43	5.14
Pass. income per passenger km (£)	0.15	0.16	0.11	0.13	0.24	0.15	0.14	0.13	0.12	0.10	0.14
Industry expenditure											
Industry exp. per train km (£)	23.85	32.26	24.60	25.30	30.27	24.98	23.04	25.25	22.75	21.73	24.95
Industry exp. per pass. km (£)	0.19	0.24	0.20	0.23	0.27	0.19	0.16	0.19	0.34	0.28	0.21
Train operator exp. per pass. km (£)	0.10	0.14	0.10	0.12	0.10	0.10	0.08	0.10	0.15	0.14	0.11
Network Rail exp. per train km (£)	11.49	13.63	12.51	12.06	19.18	11.18	11.15	12.33	12.68	10.82	12.20
Network Rail exp. per pass. km (£)	0.09	0.10	0.10	0.11	0.17	0.08	0.08	0.09	0.19	0.14	0.10
Train operator share of total costs (%)	51.8%	57.8%	49.1%	52.3%	36.6%	55.3%	51.6%	52.2%	44.3%	50.2%	51.1%
Income / expenditure											
Pass. income / industry exp. (%)	82.0%	69.1%	55.4%	57.9%	90.8%	81.6%	89.8%	68.5%	36.3%	35.4%	64.4%
Income (excl. gov funding) less expenditure per pass. journey (£)	-0.27	-1.20	-4.26	-4.11	3.26	-0.13	0.00	-2.22	-8.44	-7.51	-2.01
Income (excl. gov funding) less expenditure per pass. km (£)	-0.01	-0.05	-0.07	-0.08	0.06	-0.01	0.00	-0.04	-0.18	-0.17	-0.05

^a Some of Southeastern's services in Kent make use of High Speed 1 rail infrastructure, the cost of which is excluded from our analysis. Therefore care is required in comparing Kent to other operating routes.

5. GB rail industry financial information disaggregated by train operator

- 5.1 Our analysis of rail industry financial information for 2013-14 is presented separately in this chapter for each of the 19 train operators.
- 5.2 Our analysis shows that there are significant variations in industry income, expenditure and government funding across the 19 train operators. These variances are summarised in the Executive Summary.
- 5.3 There will be many reasons for these variances including the nature of the franchise specifications, such as local geography and demographics, as well as other drivers of costs which are more controllable by train operators, such as staff salaries. There are also other costs which are only partially controllable by train operators, for example, rolling stock leasing costs where train operators have only limited choice about what trains they can operate. This report does not seek to investigate or explain the reasons for the differences in train operating costs across franchises. For the reasons stated above care is required in interpreting our analysis in this area and the information provided cannot be used to draw conclusions about financial performance of individual operators. However, this is clearly an important subject and by providing more transparent information about train operators' costs we hope to inform the public debate about the value for money of the rail industry as a whole.

Table 5.1	Industry income, expenditure and government funding
Table 5.2	High level analysis of industry financial information in 2013-14
Table 5.3	High level analysis of industry financial information in 2013-14 by train operator

Table 5.1: Summary of industry income, expenditure and government funding in 2013-14 by train operator

£m	Train operator																				Total		
	Source	c2c Rail	Chiltern	Cross Country	East Coast	East Midlands	Greater Anglia	Abellio	First Great Western	Northern Rail	South-eastern ^a	Southern	South West Trains	Connect	First Capital	First Trans Pennine Express	Arriva Trains Wales	Virgin Trains	London Midland	LOROL		Merseyrail	First Scotrail
Franchised Train operators																							
Passenger income	1	141	157	431	645	318	625	808	232	668	686	891	549	189	122	907	276	149	48	317			8,160
Franchise receipts & PTE funding from government	1	0	0	31	0	13	0	0	346	69	0	0	0	66	152	0	57	68	82	506			1,389
Other	1	4	16	7	72	43	33	83	56	44	84	71	46	13	49	47	41	13	19	32			772
Franchised train operator income	3	145	173	470	717	374	658	891	635	781	770	961	594	267	323	954	374	230	149	855			10,321
Staff costs	1	32	46	89	132	87	134	260	221	175	183	207	129	59	98	157	119	71	51	201			2,453
Fuel costs diesel (TOCs own usage)	1	0	13	34	18	43	5	64	25	0	0	8	0	19	19	25	7	1	0	31			313
Fuel costs (traction electricity paid to NR)	2	7	0	0	22	0	31	0	5	34	34	37	29	0	0	42	15	4	6	12			277
Rolling stock charges ^b	1	29	22	147	46	28	135	71	37	103	89	91	72	60	40	119	44	17	12	105			1,269
Franchise payments to government	1	4	9	0	217	0	164	118	0	0	153	297	195	0	0	97	0	0	0	0			1,255
Corporation tax	1	2	0	0	10	4	-1	4	9	0	7	6	3	5	5	2	-2	1	4	4			64
Other (including Network Rail charges) ^b	1	63	84	190	274	198	193	360	308	471	279	299	156	107	144	503	199	135	62	489			4,514
Franchised train operator expenditure	3	137	174	460	719	360	661	878	605	782	745	945	584	251	306	947	382	229	135	842			10,143
Franchised train operator inc less exp^c	3	8	-1	10	-1	14	-3	12	29	-1	25	16	10	16	17	7	-8	1	14	13			178
Network Rail																							
Franchised train operator access charges	2	24	38	124	117	88	125	156	141	139	122	144	89	48	80	201	83	11	19	346			2,095
Net government grant	3	45	60	271	194	246	261	336	323	255	244	246	220	144	180	322	167	59	43	38			3,653
Other	3	13	16	38	38	41	48	78	72	71	55	82	49	24	37	60	43	12	12	77			866
Network Rail income	3	82	114	432	349	374	434	571	537	464	421	472	357	215	297	582	294	82	74	461			6,614
Network Rail expenditure	3	77	107	400	326	343	403	530	498	434	393	444	330	198	275	544	274	77	69	479			6,199
Network Rail income less expenditure^c	3	5	7	33	23	32	31	41	38	31	29	28	27	17	22	39	20	5	5	-18			415
Total industry income^d	3	227	287	902	1,067	749	1,092	1,461	1,171	1,245	1,191	1,433	952	482	620	1,537	667	312	223	1,317			16,936
Total industry expenditure^d	3	214	282	860	1,045	703	1,064	1,408	1,103	1,216	1,138	1,389	914	449	582	1,491	656	306	204	1,321			16,343
Industry income less expenditure^c	3	14	5	42	22	46	28	53	67	30	53	44	37	34	38	46	12	6	19	-4			593
Less: net government funding ^e	3	-41	-50	-302	23	-258	-97	-218	-669	-324	-90	51	-25	-209	-331	-225	-225	-127	-125	-544			-3,788
Industry income less expenditure excl. government funding^c	3	-28	-45	-260	45	-213	-69	-165	-602	-294	-37	95	12	-176	-293	-179	-213	-120	-106	-548			-3,195
Dividends paid by train operator^f	3	8	0	0	0	0	0	0	27	5	23	16	5	30	16	10	0	5	16	21			183

Source: (1) Train operators' management accounts; (2) Network Rail's regulatory accounts; and (3) ORR analysis. As explained in para 1.17 & 2.25 there are many reasons for variances between costs and care is needed in interpreting our analysis.

^a Care is required in comparing Southeastern's income and expenditure to other franchised train operators due to some of Southeastern's services use of the High Speed 1 rail infrastructure. ^b Rolling Stock lease arrangements can vary significantly between operators for example some receive a maintenance service as part of the lease charge and other do not. This report does not seek to investigate or explain the reasons for the differences in train operating costs across franchises. ^c As explained in Chapter 6 (Methodology) this is not an accounting profit in a statutory reporting sense due to statutory financial reporting adjustments for the treatment of deferred tax, pension schemes, derivative fair values, dividends etc. ^d Including government funding and intra-industry income and expenditure. ^e Calculated as the sum of the government funding of rail infrastructure and the franchise receipts and payments lines within this table. ^f Dividends paid will not necessarily be reflective of the profits earned in that year. Profitable operators may pay dividends during or following the end of their franchise periods.

Table 5.2: Government Premium / Funding in 2013-14 by train operator

£m	Train operator																			Total		
	c2c Rail	Chiltern	Cross Country	East Coast	Midlands East	Greater Anglia	Abellio Greater Western	First Great Western	Northern Rail	South – eastern ^b	Southern	South West Trains	First Capital Connect	First Trans Pennine Express	First Trans Wales ^c	Arriva Trains Wales ^c	Virgin Trains	London Midland	LOROL		Merseyrail	First Scotrail ^e
Franchised train operators (source: train operators)^a																						
Franchise payments to government	-2	-9	-91	-217	-123	-197	-296	0	-6	-153	-454	-254	0	-5	-97	0	0	0	0	0	0	-1,905
Franchise receipts from government	0	0	0	0	0	0	0	187	0	0	0	0	69	156	0	58	68	82	506			1,127
Franchise profit sharing and other revenue support	-2	0	122	0	136	34	177	-19	75	0	158	60	-4	0	0	-1	0	0	0	0	0	735
Total excluding PTE funding	-4	-9	31	-217	13	-164	-118	168	69	-153	-297	-195	66	152	-97	57	68	82	506			-43
Passenger Transport Executive (PTE) funding	0	0	0	0	0	0	0	178	0	0	0	0	0	0	0	0	0	0	0	0	0	178
	-4	-9	31	-217	13	-164	-118	346	69	-153	-297	-195	66	152	-97	57	68	82	506			135
Franchised train operators (source: government excluding PTEs)^a																						
Franchise payments to government	-4	-5	0	-207	0	-160	-74	0	0	-165	-312	-203	0	0	-101	0	0	0	0	0	0	-1,231
Franchise receipts from government	0	0	32	0	4	0	0	172	97	0	0	0	62	153	0	66	29	84	494			1,191
	-4	-5	32	-207	4	-160	-74	172	97	-165	-312	-203	62	153	-101	66	29	84	494			-40
Rail infrastructure																						
Government grant to Network Rail	47	62	279	200	251	269	347	334	262	252	256	226	148	186	332	173	45	45	65			3,780
Less: Network Rail rebates to government	-2	-3	-9	-6	-5	-8	-10	-11	-8	-8	-10	-6	-5	-6	-10	-6	-1	-2	-27			-142
TfL East London Line	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	15	0	0			15
	45	60	271	194	246	261	337	324	255	244	246	220	144	180	322	168	59	43	37			3,653
Total government funding (source: train operators + NR accounts)^a	41	50	302	-23	258	97	218	669	324	90	-51	25	209	331	225	225	127	125	544			3,788
Total government funding (source: government + NR accounts)^a	41	55	303	-13	249	100	263	495	352	78	-66	17	205	332	221	234	88	127	531			3,613

As explained in paragraph 1.17 and 2.25 there are many reasons for variances between train operators' costs/income and care is needed in interpreting our analysis.

^a There are differences in the amount of Government funding recognised in train operators' and government financial statements. We understand that this is largely due to the income recognition criteria set out in accounting standards which require train operators to match receipts from government in the period in which the relevant expenditure occurs in their income statements. Therefore, the timing of the recognition of this income in train operators' financial statements will not necessarily match the expenditure shown in government's financial statements. The franchise payments/receipts to train operators per government is available on the ORR data portal <http://dataportal.orr.gov.uk/displayreport/report/html/0913a84d-b740-4111-b6f8-bf6470e2d7b7>.

^b Care is required in comparing Southeastern's income and expenditure to other franchised train operators due to some of Southeastern's services use of the High Speed 1 rail infrastructure.

^c Government funding from Welsh Government and Transport Scotland respectively.

Table 5.3: Analysis of industry financial information in 2013-14 by train operator

£m	Train operator																			Total
	c2c Rail	Chiltern	Cross Country	East Coast	East Midlands	Abellio Greater Anglia	First Great Western	Northern Rail	South-eastern ^a	Southern	South West Trains	First Capital Connect	First Trans Pennine Express	Arriva Trains Wales	Virgin Trains	London Midland	LOROL	Merseyrail	First Scotrail	
Government funding																				
Share of government funding	1.1%	1.3%	8.0%	-0.6%	6.8%	2.6%	5.8%	17.7%	8.6%	2.4%	-1.3%	0.7%	5.5%	8.8%	5.9%	5.9%	3.3%	3.3%	14.4%	100.0%
Funding / total income	21.3%	21.5%	38.9%	-3.2%	40.1%	12.3%	18.9%	66.4%	30.3%	10.1%	-5.3%	3.9%	48.8%	62.8%	18.4%	39.5%	42.6%	62.7%	57.7%	28.5%
Funding per pass. journey (£)	1.06	2.21	8.84	-1.15	10.72	0.72	2.19	7.12	1.81	0.50	-0.23	0.21	8.03	11.09	7.03	3.51	0.93	2.91	6.30	2.39
Funding per pass. km (£)	0.04	0.04	0.09	0.00	0.12	0.02	0.04	0.30	0.07	0.02	-0.01	0.01	0.13	0.28	0.04	0.09	0.15	0.19	0.19	0.06
Passenger income																				
Per pass. journey (£)	3.63	6.87	12.62	32.42	13.21	4.62	8.11	2.47	3.74	3.77	4.00	4.66	7.24	4.09	28.41	4.30	1.10	1.13	3.67	5.14
Per passenger km (£)	0.14	0.13	0.13	0.13	0.14	0.14	0.14	0.11	0.15	0.15	0.15	0.14	0.11	0.10	0.15	0.12	0.18	0.07	0.11	0.14
Industry expenditure																				
Industry exp. per train km (£)	26.87	21.80	22.67	32.12	26.64	22.42	26.21	20.66	32.69	24.39	22.82	24.03	23.43	21.05	32.58	22.73	36.84	27.57	20.52	24.95
Industry exp. per pass. km (£)	0.17	0.19	0.23	0.14	0.27	0.18	0.19	0.43	0.24	0.19	0.15	0.16	0.24	0.42	0.19	0.24	0.35	0.27	0.33	0.21
Train operator exp. per pass. km (£)	0.10	0.10	0.10	0.07	0.11	0.08	0.10	0.20	0.14	0.10	0.08	0.07	0.12	0.18	0.10	0.12	0.25	0.17	0.17	0.11
Network Rail exp. per pass. km (£)	0.07	0.09	0.12	0.06	0.15	0.09	0.09	0.23	0.10	0.09	0.07	0.09	0.12	0.24	0.09	0.12	0.09	0.10	0.17	0.10
Train operator share of total costs (%)	57.3%	53.2%	45.5%	53.2%	42.7%	47.3%	51.9%	47.0%	58.3%	53.5%	51.2%	45.8%	50.0%	43.8%	53.6%	50.7%	73.6%	61.6%	49.4%	51.1%
Income / expenditure																				
Pass. income / industry exp. (%)	78.3%	68.5%	58.8%	92.7%	53.2%	81.8%	73.4%	24.7%	64.2%	81.1%	97.9%	90.0%	47.7%	25.0%	77.4%	49.6%	51.3%	26.8%	33.5%	64.4%
Income (excl. gov funding) less expenditure per pass. journey (£)	-0.72	-1.97	-7.60	2.25	-8.83	-0.51	-1.65	-6.40	-1.65	-0.20	0.43	0.10	-6.75	-9.80	-5.60	-3.32	-0.89	-2.48	-6.35	-2.01
Income (excl. gov funding) less expenditure per pass. km (£)	-0.03	-0.04	-0.08	0.01	-0.10	-0.02	-0.03	-0.27	-0.07	-0.01	0.02	0.00	-0.11	-0.25	-0.03	-0.09	-0.14	-0.16	-0.19	-0.05

As explained in paragraph 2.25 there are many reasons for variances between train operator's costs and income and care is needed in interpreting our analysis.

^a Care is required in comparing Southeastern's income and expenditure to other franchised train operators due to some of Southeastern's services use of the High Speed 1 rail infrastructure.

6. Methodology

Source data

Rail infrastructure financial data

- 6.1 Network Rail publishes both statutory and regulatory financial statements for each financial year running 1 April to 31 March. The format of the regulatory financial statements is prescribed by ORR and includes comprehensive information about the company's income and expenditure²⁶. The regulatory financial statements have been disaggregated between England & Wales and Scotland since 2006-07 and since 2011-12 include statements on income and expenditure for each regional operating route.
- 6.2 In comparison to statutory accounts, regulatory financial statements have (a) arguably more meaningful and detailed categorisations of income and expenditure and (b) include regionally disaggregated information, accordingly we have used financial information from Network Rail's regulatory financial statements rather than their statutory financial statements within our analysis.
- 6.3 Our analysis also includes a small component of expenditure by TfL on the East London Line. This information was provided in a submission to us by TfL.

Franchised train operators financial data

- 6.4 There are currently 19 train operators which operate regional passenger services under franchise from government. As summarised in Annex A, DfT is the franchising authority for the majority of England & Wales franchises. Transport Scotland, TfL and Merseytravel have franchising authority for the ScotRail, London Overground and Merseyrail franchises respectively.
- 6.5 Statutory financial statements are available from Companies House for all train operators. However, due to the flexibility of the Companies Act financial reporting requirements, there are significant differences between the information presented within different train operators individual statutory financial statements. This limits the extent to which this information can be used to develop an understanding of whole industry income and expenditure. In particular:
 - (a) train operators' statutory financial statements have different financial year-ends, complicating comparisons across consistent time frames²⁷;

²⁶ Our regulatory accounting guidelines for Network Rail are available at: <http://orr.gov.uk/publications/guidance/regulatory-accounts>.

(b) items of income and expenditure are presented in different formats and with different levels of detail (in both the primary statements and the accompanying notes); and

(c) differences in accounting policies may result in differences to reported income and expenditure. This may be somewhat mitigated by the similar nature of train operators' businesses and what we understand to be similar accounting policies are applied within the industry.

6.6 Franchised train operators are also required to provide four-weekly management accounts to the franchising authorities as part of their franchise agreements. Using these management accounts avoids the problems noted above for the purposes of our analysis. In particular:

(a) four-weekly management accounts can be collated over the same twelve month timeframe, thereby avoiding the problem of different year-ends; and

(b) the formats of management accounts provided to franchising authorities are largely standardised and include detailed information about income and expenditure.

6.7 For these reasons, with the agreement of train operators, we have used information from franchised train operators' management accounts within our analysis.

Disaggregation of financial information

6.8 There are various ways in which GB rail industry financial information can be analysed. These include:

(a) at the **national level** for Great Britain in total and separately for England, Scotland and Wales;

(b) at a **regional level**, for example, separately for each of Network Rail's regional operating routes;

(c) at the **passenger service level**, for example, separately for each franchise train operator, or in aggregate for similar types of passenger services (such as for long distance or regional operators); and

(d) at a greater level of granularity, for example for individual train journeys.

6.9 As the usefulness of these different forms of analysis will depend on their intended use, there is no one right way, or best way to present our findings. For example, regionally disaggregated information is arguably more useful for understanding regional variances in investment, whereas disaggregation by service type is arguably more useful for understanding variances in passenger revenues. Using both is useful for understanding some items such as government funding.

6.10 We have chosen to present financial information separately at a national, regional operating route and franchise level within this report as this allows us to best meet the objectives set out in paragraph 1.3²⁸.

6.11 We have not attempted to analyse industry income and expenditure at a greater level of granularity, for example for individual train journeys. Whilst this could provide additional useful information it would require a significant increase in the amount of data and analysis required, and its value would be questionable as many items of income and expenditure cannot currently be accurately attributed at a more detailed level.

²⁸ Publishing information in this way is similar to the requirements of International Financial Reporting Standard (IFRS) 8 *Operating Segments*. IFRS 8 requires companies to segmentally report certain Statement of Financial Performance (profit & loss) and Statement of financial position (balance sheet) items by geographical area and by business activity.

National and regional analysis – basis of disaggregation

6.12 The methodology underpinning the national and regional operating route analyses presented in Chapters 2 and 3 is explained below.

Network Rail financial information

6.13 The majority of Network Rail's regionally disaggregated financial information included within our analysis has been taken from Network Rail's 2013-14 regulatory financial statements. To prepare this information, Network Rail classified income and expenditure into three categories dependent on how the items are managed:

(a) *directly attributed* - route managed. Income and expenditure in this category is currently managed at route level, e.g. signallers. As there is alignment between management responsibility and route, such items can be directly attributed to an individual operating route;

(b) *centrally managed – attributable to routes*. For these items, management responsibility may not be locally based, however, the income and expenditure are incurred locally, so attributing these items to the applicable operating route is relatively straightforward. These include the majority of renewals and enhancements costs; and

(c) *centrally managed – network wide*. Income and expenditure in this category is incurred for the whole network, for example, insurance costs. Network Rail has allocated network-wide income and expenditure to operating routes based on the total number of train miles travelled in each operating route.

6.14 Our analysis includes some items of expenditure (depreciation/amortisation, financing costs, corporation tax and rebates) that Network Rail has reported separately for England & Wales, and Scotland but not separately between England & Wales operating routes. Within our analysis depreciation/amortisation and financing costs have been allocated between England & Wales operating routes in proportion to our estimate of the regulatory asset base within each operating route²⁹. This is a change to the approach taken in previous years where these costs were allocated in proportion to train kilometres travelled in each route. Corporation tax and rebates have been allocated between England & Wales operating routes in proportion to train kilometres travelled in each route as this is consistent with Network Rail's approach for allocating network wide costs between operating routes.

²⁹ Our indicative disaggregation of Network Rail's regulatory asset base for each of its England & Wales operating routes is explained in Annex D of our 2013 periodic review of Network Rail's outputs and funding. This is available at http://orr.gov.uk/data/assets/pdf_file/0011/452/pr13-final-determination.pdf.

Franchised train operators' financial information

- 6.15 As explained in Chapter 1 (Introduction) there are significant overlaps between the geographies of rail franchises, between the geographies of rail franchises and regional operating routes, and between the geographies of rail franchises and England, Scotland and Wales. These overlaps significantly complicate any analysis of franchised train operators' income and expenditure between regional operating routes and between England, Scotland and Wales. Our methodology for allocating train operators' income and expenditure is explained below.
- 6.16 We have allocated train operators' income between operating routes and England, Scotland and Wales using revenue information from the rail industry's central ticketing system, LENNON³⁰ on the proportion of that operators income earned relating to the part of journeys in the relevant operating route³¹. As explained in previous publications, we consider that this provides a better allocation of income than using train distance travelled.
- 6.17 Train operators' expenditure has been allocated between regional operating routes, and between England, Scotland and Wales in proportion to train distance travelled in each operating route in 2013-14³². This is considered a reasonable approach for allocating expenditure across operating routes, as the majority of train operators' expenditure (staff, rolling stock, fuel and maintenance costs) is expected to vary closely with train distance travelled. It also seems a reasonable approach for allocating centrally incurred train operator overheads and franchise payments to and from government.

Analysis of regulated and unregulated passenger income

- 6.18 The analysis of regulated and unregulated passenger income presented in Figures 2.2 and 2.3 was sourced from the LENNON database. The LENNON income data was mapped to regulated and unregulated ticket types to produce a Fares Index Dataset which enables an analysis of the contribution of regulated and unregulated ticket types for each train operator's total passenger income.
- 6.19 Whilst we consider that the approach that we have used is sufficiently robust to provide a high level summary of the relative contribution of different ticket types to train operators' income, we recognise that there are limitations. Firstly, the Fares Index

³⁰ The LENNON database holds information on the majority of rail tickets purchased in Great Britain and is used to allocate the revenue from ticket sales between train operating companies. The LENNON database is the source of the passenger income figure published as part of the ORR's Rail Usage Statistics here, however for the reasons explained in paragraph 6.6 we use train operators management accounts as the source of passenger income.

³¹ As an example the LENNON database indicates that 23.2% of Cross Country's passenger income was generated from the part of journeys in the London North East operating route therefore 23.2% of the Cross Country passenger income per the train operators accounts has been allocated to that operating route.

³² The train distance travelled information was provided to us by Network Rail and is considered the most appropriate currently available to the industry. Network Rail has identified some issues relating to route boundaries which it is currently improving. However, these are likely to have only a minor effect on our analysis.

Dataset was only available for the calendar year January to December 2014 whereas the rest of our analysis is for the period April 2013 to March 2014³³. Also, there are limitations to the number of ticket types that are captured in the Fares Index Dataset so some revenues may be excluded (for example, where a short-term promotional fare is introduced or where a ticket covers more than one mode of transport). For the latter, we think that this is more likely to affect the data for Merseyrail and London Overground due to the greater use of flexible travelcards by passengers on these operators.

Franchise level analysis – basis of disaggregation

6.20 The methodology underpinning the franchise level analysis presented in Chapter 4 is explained below.

Franchised train operators' financial information

6.21 As explained earlier in this chapter, the train operator financial information included within our analysis has been taken from train operators' cumulative management accounting submissions to government for the period 1 April 2013 to 31 March 2014.

6.22 As shown in Table 3.4, 4.4 and 5.2, there are differences in the amounts of government funding recognised in train operators' and government's financial statements. This is largely due to the income recognition criteria set out in accounting standards which require train operators to match receipts from government in the period in which the relevant expenditure occurs in their income statements. Therefore, the timing of the recognition of this income in train operators' financial statements will not necessarily match the expenditure shown in government's financial statements. These differences can be quite large in any one year for some train operators.

6.23 The operating model for London Overground is different to that used by other train operators. Instead of franchising the services out, Rail for London (RfL), a subsidiary of TfL, has entered into a concession agreement with London Overground Rail Operations Limited ('London Overground') to run services. This operating contract means that RfL retains risk on revenue, and reports the passenger income, whilst leaving the train operator to manage performance of the service. As the majority of ticket income is with RfL, the revenue and cost split between the London Overground and RfL is very different to that between other train operators and government. To support our analysis, London Overground and TfL worked together to provide consolidated information for London Overground that is consistent with the financial information for other train operators.

³³ Our analysis of regulated and unregulated passenger income data was done on a calendar year basis as per the source data.

Network Rail financial information

- 6.24 We have changed the way in which we analyse and attribute some of Network Rail's costs between different franchises in this year's publication. Firstly for the reasons described below we have changed how maintenance costs are allocated from train distance travelled to variable usage charge paid by each franchisee in that route. Secondly we have changed the allocation of network grant from train distance travelled so that it is allocated in proportion to residual Network Rail income less expenditure calculated for each franchise. We have also restated our previously published analysis on a consistent basis. The impact of these changes and the change described in paragraph 6.14 is small for the majority of operators. Those most affected are Scotrail and East Coast where the change in methodology accounts for a change in network grant allocation of -£146m and £83m respectively in 2012-13. Because this part of our analysis is to an extent an exercise in allocating fixed costs between different customers it is important to understand that there is no definitive method for allocating these costs (and related government funding) between franchises. Whilst we consider that the methods that we have employed provide a reasonable analysis we recognise that different approaches could be used and there different views about how this should be done. We therefore suggest that care is needed in interpreting this part of our analysis.
- 6.25 Given the amount of detailed work that Network Rail has undertaken over the past four years to identify and attribute its costs at a route level³⁴ we consider that Network Rail's expenditure presented at route level (as described in paragraphs 6.13 – 6.14) provides the best starting point for analysing its income and expenditure by franchise. The starting point for this part of our analysis is to allocate Network Rail's income and expenditure in proportion to train operators' activities in each regional operating route. Put simply, if a train operator does not operate in a particular operating route, none of Network Rail's expenditure in that route will be allocated to that train operator.
- 6.26 Whilst recognising there is no definitive way to allocate Network Rail's expenditure between train operators the approach we have used is as follows:
- (a) maintenance costs in each operating route has been allocated to franchises in proportion to the variable usage charge paid by each franchisee in that route. We consider that this approach best reflects how Network Rail's maintenance activities vary with the wear and tear to its network caused by train usage;
 - (b) depreciation/amortisation and financing costs has been allocated in proportion to train distance travelled by each franchise in each operating route. We have adopted this approach because physical presence on the network is arguably a more meaningful way to allocate largely fixed costs which relate to long-life assets than measures which relate to short-term (variable) wear and tear. So for example, our

³⁴ See <http://www.networkrail.co.uk/devolution.aspx> for further details.

approach aims to allocate the cost of replacing a signal box to franchises in proportion to the number of trains that make use of that signal box;

(c) other income and expenditure in each route has been allocated in proportion to train distance travelled by each franchise operator in that operating route. This is essentially the same approach as we have used for allocating train operators' income and expenditure to regional operating routes. This is a simplifying approach which we consider appropriate for these comparatively smaller categories of income and expenditure; and

(d) network grant has been allocated in proportion to the residual Network Rail income less expenditure that we have calculated for each franchise.

A cash-based approach for Network Rail's capital expenditure

6.27 The majority of Network Rail's renewals and enhancements expenditure is capitalised and amortised (or depreciated) over the life of the assets for statutory financial reporting purposes. Network Rail's amortisation in our PR08 determination and its regulatory accounts is based on the long-run annual average investment expenditure that is required in order to maintain the network in a steady state³⁵.

6.28 Network Rail's expenditure presented in Tables 1, 3.1, 3.3, 4.1, 4.3 and 5.1 includes the annual depreciation / amortisation charge for capital expenditure taken from Network Rail's regulatory financial statements³⁶, rather than the amount of cash spent on these renewals and enhancements projects. This is consistent with the accruals-based accounting approach to recognise the cost of an asset over its useful life. However, it is also informative to understand the actual cashflows of the rail industry as well as income and expenditure as reported on an accruals basis. We have therefore presented industry income and expenditure, including Network Rail's capital expenditure on a cash basis in Tables 2.5 and 3.5.

Adjustments to determine industry income and expenditure

6.29 Similar to the consolidation adjustments that are required to prepare group statutory financial statements, adjustments are required to our analysis to avoid overstating industry income and expenditure for financial transactions that are internal to the industry.

³⁵ See Chapter 15 of our PR08 determination for further details. <http://orr.gov.uk/what-and-how-we-regulate/regulation-of-network-rail/how-we-regulate-network-rail/previous-control-period/periodic-review-2008>

- 6.30 Network Rail's income from franchise operators includes fixed and variable usage charges, traction electricity charges and stations income. Network Rail's regulatory financial statements include information on these items for each franchise operator. This information has been used to determine the appropriate consolidation adjustment to Network Rail's income and train operators' expenditure to avoid overstating industry income and expenditure.
- 6.31 Franchise operators perform a variety of services on behalf of other operators including station access, train maintenance and staffing. However, franchise operators have informed us that these services typically represent less than 2% of turnover. No adjustment has been made in our analysis for this internal industry income on the grounds of materiality.

Industry surplus / (deficit)

- 6.32 Table 1, and similar disaggregated tables included within our report, show the net difference between industry income and expenditure (either a surplus or deficit) based on companies' management and regulatory accounting information. This amount will be different to aggregate statutory profits due to the different way they have been prepared and statutory financial reporting requirements for the treatment of deferred tax, pension schemes, derivative fair values, dividends etc. There are also timing differences between Network Rail's revenue and expenditure due to its ability to phase the timing of its expenditure differently within a control period compared to the assumption in our periodic review.

Freight and open access operations

- 6.33 To improve transparency about the finances of the whole rail industry, we have also undertaken a limited analysis using the most recently available statutory financial statements, to estimate the income and expenditure of freight and open access train operators.

Table 6.1: Non-franchised train operators' income and expenditure

£m	Turnover	Operating costs	Other costs / income	Profit after tax
Freight operators¹				
GB Rail Freight ^a (part of the Eurotunnel Group)	109	96	3	9
Colas Rail ^a (part of the Colas Group)	186	166	17	2
DB Schenker ^a (part of Deutsche Bahn AG)	445	417	-9	37
Mendip ^a	23	21	2	0
Direct Rail Services ^b (part of the Nuclear Decommissioning Authority)	60	56	2	2
Freightliner ^b (part of the Freightliner Group)	181	145	30	6
	1,004	902	46	57
Open access operators²				
Grand Central ^a (part of Deutsche Bahn)	33	29	3	40 ³⁷
Heathrow Express ^a (part of Heathrow Airport Holdings)	67	61	6	5
Hull Trains ^b (part of First Group)	24	22	2	2
	124	112	12	47
Open access operators (international)				
Eurostar ^a (owned by SNCF & LCR & NMBS/SNCB ^c)	882	749	133	72

^a Year ended 31 December 2013.

^b Year ended 31 March 2014.

^c Société Nationale des Chemins de fer Français & London and Continental Railways & Nationale Maatschappij der Belgische Spoorwegen / Société nationale des chemins de fer belges.

¹ Freight operators paid £58m of access charges to Network Rail in 2013-14 (source: Network Rail).

² Open access operators paid £24m of access charges to Network Rail in 2013-14 (source: Network Rail).

6.34 As explained in Chapter 1 (Introduction), our analysis for the industry (in Chapters 2 to 5) does not include freight and open access train operators' income and expenditure as, financially, these are smaller components of the industry than franchised train operators, information is reduced public interest because they are not direct recipients of government support.

6.35 Our analysis includes Network Rail's income from freight (£58m) and open access operations (£24m) in 2013-14³⁸ because they cannot easily be separately identified. Our analysis also includes, but does not separately identify, Network Rail's costs incurred from freight and open access operations so as not to overly complicate our analysis³⁹.

³⁷ During the year inter-company debts due to other group companies were waived, amounting to £38m.

³⁸ These items are included within the Network Rail 'other income' category.

³⁹ As part of our 2013 periodic review we estimated that freight avoidable costs are around £300m to £400m per annum. This represents the element of Network Rail's fixed costs which we estimated is attributable to freight services.

High Speed 1

6.36 To improve transparency about the finances of the whole rail industry, we have included below some high level analysis of HS1, the rail infrastructure concession that connects London to the Channel Tunnel.

6.37 The focus of our analysis in the rest of this report is the GB franchised rail industry and our analysis does not explicitly include High Speed 1 Ltd ('HS1'), due to the difficulty of reliably separating HS1's costs arising from national and international train operations⁴⁰. However, our analysis does include franchised train operators' income and expenditure from operations on HS1 (specifically the Southeastern train operator).

6.38 HS1's latest statutory financial statements are for the 12 months ended 31 March 2014 and are summarised in Table 6.2.

Table 6.2: Summary of HS1's income and expenditure for the 12 months ended 31 March 2014

	£m
Turnover	289
Operating expenditure	-242
Net interest payable	-158
Loss before tax	111
Decrease in cash	191

6.39 HS1 made an approximate £111m loss on its day-to-day operations, and its cash reserves decreased by approximately £191m during the 12 month period covered in our analysis.

Non-financial information

6.40 We have included some non-financial information in our analysis to inform users' interpretation of the financial information presented. This non-financial information has been taken from the ORR data portal, ORR's official database of railway statistics⁴¹.

⁴⁰ This is a similar issue to the difficulty of separately identifying Network Rail's infrastructure costs in relation to freight and open access operations which is explained above.

⁴¹ Data covering a range of rail statistics is available at <http://orr.gov.uk/statistics/data-portal>.

Annex A - Geographical overlap of rail franchises and regional operating routes

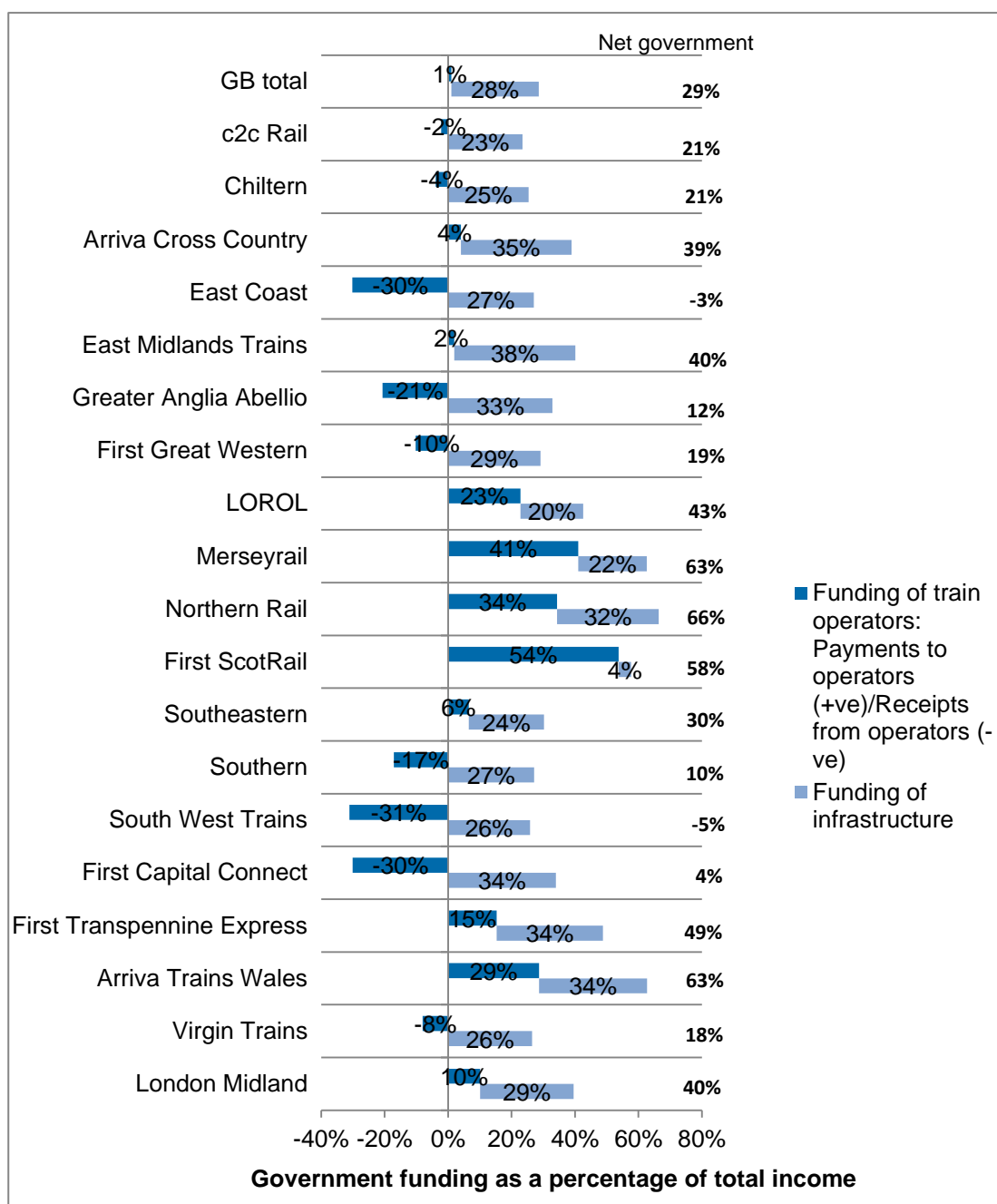
Table A1: Distance travelled by train operators in each regional operating route in 2013-14

Franchise	Franchise operator	Franchising authority	Operating route										Total train km travelled (millions)	
			Anglia	Kent	London North East	London North West	East Midlands	Sussex	Wessex	Western	Wales	Scotland		
Essex Thameside	c2c Rail	DfT	6.7	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	6.7
Chiltern	Chiltern	DfT	0.0	0.0	0.0	10.3	0.0	0.0	0.0	0.2	0.0	0.0	0.0	10.5
Cross Country	Cross Country	DfT	1.2	0.0	8.0	8.1	2.6	0.0	1.7	7.8	0.9	2.0	0.0	32.4
East Coast	East Coast	DfT	0.0	0.0	19.3	0.0	0.0	0.0	0.0	0.0	0.0	2.4	0.0	21.7
East Midlands	East Midlands	DfT	1.2	0.0	10.3	1.5	9.5	0.0	0.0	0.0	0.0	0.0	0.0	22.5
Greater Anglia	Abellio Greater Anglia	DfT	34.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	34.1
Greater Western	First Great Western	DfT	0.0	0.0	0.0	0.1	0.0	0.6	3.3	34.7	3.3	0.0	0.0	42.0
Northern	Northern Rail	DfT	0.0	0.0	23.8	21.4	0.3	0.0	0.0	0.0	0.0	0.0	0.0	45.5
South Eastern	Southeastern	DfT	0.0	31.5	0.0	0.0	0.0	0.3	0.0	0.0	0.0	0.0	0.0	31.8
South central	Southern	DfT	0.0	2.3	0.0	0.8	0.0	28.9	2.6	0.0	0.0	0.0	0.0	34.6
South Western	South West Trains	DfT	0.0	0.0	0.0	0.0	0.0	0.1	39.2	0.6	0.0	0.0	0.0	39.9
Thameslink Great Northern	First Capital Connect	DfT	1.8	0.9	14.1	0.0	4.5	4.0	0.0	0.0	0.0	0.0	0.0	25.4
Trans Pennine Express	First Transpennine Express	DfT	0.0	0.0	8.4	7.4	0.0	0.0	0.0	0.0	0.0	1.2	0.0	16.9
Wales & Borders	Arriva Trains Wales	DfT	0.0	0.0	0.0	3.8	0.0	0.0	0.0	0.2	19.3	0.0	0.0	23.3
West Coast	Virgin Trains	DfT	0.0	0.0	0.0	32.2	0.0	0.0	0.0	0.0	0.6	3.1	0.0	36.0
West Midlands	London Midland	DfT	0.0	0.0	0.0	23.1	0.0	0.0	0.0	1.1	0.2	0.0	0.0	24.5
London Overground	LOROL	TfL	4.8	0.4	0.0	1.2	0.0	1.4	0.1	0.0	0.0	0.0	0.0	7.9
Merseyrail Electrics	Merseyrail	Merseyside PTE	0.0	0.0	0.0	6.5	0.0	0.0	0.0	0.0	0.0	0.0	0.0	6.5
ScotRail	First ScotRail	Transport Scotland	0.0	0.0	0.1	0.8	0.0	0.0	0.0	0.0	0.0	45.3	0.0	46.1
Total train distance travelled (km millions)			49.8	35.1	83.9	117.1	16.9	35.4	46.8	44.6	24.4	54.0	0.0	508.1

Annex B - Government funding contribution to Network Rail & operators

Due to the overlapping and misaligned geographies of franchises and operating routes there are many different approaches to the allocation of infrastructure costs which give different outcomes for the allocation of government funding to operators and operating routes. It is important that it is recognised that there is no definitive view on how this should be done and therefore care is required in understanding and interpreting our analysis. This is discussed further in Chapter 1. The methodology underpinning our analysis is explained in Chapter 6.

Figure B1: The contribution of government funding to Network Rail and Train Operators as a proportion of industry income analysed by operator





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